IN THE SUPREME COURT OF BERMUDA

(COMMERCIAL COURT)

COMPANIES (WINDING-UP)

2017: No. 133

IN THE MATTER OF CUMULUS EASTERN EUROPEAN PROPERTY FUND LIMITED

AND IN THE MATTER OF THE COMPANIES ACT 1981

REASONS

(in Chambers)

Winding-up- Bermuda Monetary Authority public interest petition-appointment of joint liquidators pursuant to First Meetings of Creditors and Contributories-whether meetings validly convened and held-costs of unsuccessful opposition to application-Investment Funds Act 2006 section 36-Companies Act 1981, section 171(c); Companies (Winding-Up) Rules 1982, rules 3, 103 and 158

Date of hearing: April 4, 2018
Date of Reasons: April 5, 2018

Mr Jayson Wood and Ms Lilla Zuill, Zuill & Co (Harneys), for the Joint Provisional Liquidators

Mr Andrew Lucas, an Objecting Contributory did not appear

Background

1. On April 12, 2017 the Bermuda Monetary Authority petitioned under section 36 of the Investment Funds Act 2006 (the "IFA") for the Company to be wound-up on the grounds of various breaches of the IFA and rules made under it. On July 14, 2017, having found that the first three of the statutory breaches pleaded in paragraph 16 of the Petition had been proved, Hellman J granted an Order winding-up the Company. He also appointed Roy Bailey of EY Bermuda Ltd and Keiran Hutchinson of EY Cayman Ltd. to act as joint provisional liquidators of the Company (the "JPLs").

2. By Summons dated January 31, 2018, following First Meetings of Creditors and Contributories held on January 12, 2018, the JPLs applied to be appointed Joint Liquidators. On February 16, 2018, I ordered directions for the filing of evidence in support of and in opposition to the Summons, and also directed that:

"*2. The JPLs give all known creditors and voting members of the Company written notice of the Summons within 7 days from the date of this Order with such notice to contain a statement that anyone wishing to appear on the Summons must signify their intention to do so by 9 March 2018.*

3.The Summons shall be advertised once in the Bermuda Royal Gazette within 7 days from the date of this Order with such advertisement to contain a statement that anyone wishing to appear on the Summons must signify their intention to do so by 9 March 2018."

3. A Notice of Intention to Appear and an Affidavit sworn by Mr Andrew Lucas, each dated March 9, 2018, were emailed to the JPLs and filed in Court on the same date by Mr Lucas acting in person. The JPLs filed three Affidavits in response and prepared a 17 page Skeleton Argument, 10 pages of which were devoted to responding to Mr Lucas' case that the results of the First Creditors' Meeting should be quashed and the Meeting reconvened.

4. In the event Mr Lucas did not actually appear but by an email dated April 3, 2018 invited the Court to consider the matters he had placed before the Court. Having heard Mr Wood for the JPLs, I granted the Order appointing the JPLs as Joint Liquidators and awarded the JPLs their costs of and incidental to responding to Mr Lucas' objections. I now give reasons for that decision.

The First Meetings

The JPLs' evidence

5. By way of background the First Bailey Affidavit explained that the Company had two directors and that its Investment Manager was a company incorporated in the United Kingdom with two directors, one of whom was Mr Lucas. The Company's shares were divided into two classes, redeemable preference shares and non-redeemable ordinary shares. The ordinary shareholders upon a winding-up were only entitled to receive the nominal paid up value of their shares (Mr Lucas was entitled to £50). The preference shareholders were entitled to receive any surplus, assuming a solvent distribution. The JPLs' provisional view was, subject to uncertainties about the realisable value of the Company's assets, that there would likely be a shortfall for preference shareholders, but that investor/creditors would be paid in full.

6. At the Contributories' Meeting the only two members, each holding 50 Ordinary Shares (par value of £50) attended. One (Mr Lucas) voted in favour of alternative permanent liquidators with a committee of inspection and the other abstained. The appointment of a committee of inspection was deferred as there were insufficient nominations.

7. At the Creditors Meeting, proofs submitted by Mr Lucas on behalf of himself (£5463.67) and four other purported creditors (with claims totalling £442,598.16) were rejected for voting purposes. As regards Mr Lucas, this was because he filed no evidence to support his asserted creditor status. As regards the other four individuals, this was because they invested on terms that their nominee would be the preference shareholder entitled to exercise redemption rights. Nine creditors whose claims were admitted for voting purposes (with claims totalling US$1,623,219.48) voted for the appointment of the JPLs as permanent liquidators and for a committee of inspection. The Chairman abstained as regards a general proxy provided to him by KPMG Cyprus. The appointment of a committee of inspection was deferred as there were insufficient nominations.

Mr Lucas' evidence

8. Mr Lucas challenged the validity of the vote at the Creditors' Meeting and sought an Order reconvening the Meeting on the following grounds:

   (1) underlying investors were unfairly being excluded from the voting process. Many who had been excluded wished to nominate the same alternative liquidators as he had nominated. It was unclear why some "*some investors are being treated as creditors and others as contributories*";

   (2) former director Mr Stephens' claim for US$96,759.20 should not have been allowed for voting purposes because in the Offering Document he had expressly waived his right to any salary;

   (3) there had been non-compliance with the Companies (Winding-Up) Rules 1982 in relation to proxy forms (rules 103 and 108[1]).

9. In addition to these direct attacks on the validity of the vote, Mr Lucas sought to lend credence to his case that alternative permanent liquidators should be appointed by criticising the JPLs conduct in relation to collateral matters, most significantly:

   - failing give adequate notice of the of the *inter partes* hearing of the present Summons by only serving actual Summons and supporting materials upon request rather than initially;

[1] Rule 108 provides:

"***Holder of proxy not to vote on matter in which he is financially interested***
108 No person acting either under a general or a special proxy shall vote in favour of any resolution which would directly or indirectly place himself, his partner or employer in a position to receive any remuneration out of the estate of the company otherwise than as a creditor rateably with the other creditors of the company:

Provided that where any person holds special proxies to vote for an application to the Court in favour of the appointment of himself as liquidator he may use the said proxies and vote accordingly."

- questioning the ability of the JPLs to effectively investigate the Company's affairs; and

- asserting that the JPLs had failed carry out appropriate investigations and/or had misconstrued the relevant matters requiring investigation.

The JPLs' reply evidence

10. The Second Bailey Affidavit responded substantively to Mr Lucas' Affidavit. The Second Joynson Affidavit refuted Mr Lucas' account of a telephone conversation about the status of underlying investors. The First Zuill Affidavit placed before the Court copies of correspondence between the JPLs and Mr Lucas in relation to the hearing of the present Summons. Most points were refuted in a clear and straightforward manner, save perhaps the suggestion that Mr Stephens' proof should have been rejected for voting purposes[2].

Findings

11. I shall record my findings on the most controversial factual matters after setting out the governing legal principles. However four issues can be dealt with more summarily.

12. The first is the complaint that rule 108 was contravened because the Meeting Chairman (Mr Bailey) voted a general proxy in his own favour. That complaint is wholly misconceived as the record clearly shows that the Chairman abstained and that KPMG's claim was not counted for voting purposes. I found that no breach of rule 108 occurred.

13. The second is the complaint that the JPLs failed to comply with this Court's Directions Order by giving notice of the inter partes hearing without initially serving the application itself. This complaint is wholly misconceived. The February 16, 2018 Directions Order did not require service of the Summons. It merely obliged the JPLs to give "*written notice of the Summons within 7 days from the date of this Order with such notice to contain a statement that anyone wishing to appear on the Summons must signify their intention to do so by 9 March 2018.*" Had the Court wished to require service of the Summons itself, the quoted wording would not have been used. Mr Lucas himself exhibits an email dated February 23, 2018 from the JPLs enclosing a Notice which complies with the relevant requirements of the Directions Order.

14. The third is the status of Mr Lucas as a creditor. His proof was rejected at the First Meeting on the grounds of insufficient evidence to support his claim, there being no support for it in the Company's books and records. Mr Wood pointed out that he did

[2] The complaint that this proof had been admitted on its merits was unambiguously rejected, however.

not remedy this deficiency in his Affidavit. I found that there was no credible evidence before this Court that Mr Lucas was anything other than a contributory or member of the Company.

15. The fourth is the question raised as to the basis on which some investors were permitted to vote as creditors and others not. The JPLs' straightforward explanation that investors awaiting receipt of redemption proceeds have been treated as creditors and that only registered nominee shareholders are entitled to make redemption requests (and claim redemption proceeds) was not contradicted by any credible evidence. I rejected the suggestion that eligible creditors were denied the right to vote as such without just cause.

The appointment of joint (permanent) liquidators after the first statutory meetings: governing legal principles

16. Although Mr Lucas deftly avoided inviting the Court to give effect to the result of the Contributories Meeting in preference to the vote of Creditors' Meeting, his case implicitly sought to achieve this result. The only resolution passed at the First Meetings in favour of alternative permanent liquidators was the vote cast on his own behalf at the Contributories' Meeting. As Mr Wood was eager to point out, even if the rejected creditor proofs had been allowed, the outcome of the vote would have been the same. Equally, the result would be unaltered if Mr Stephens' vote in favour of the JPLs ought to have been disallowed I rejected the unsubstantiated suggestion that potential creditors supportive of Mr Lucas' preferred choice of joint liquidators were wrongly denied an opportunity to vote as creditors at the First Meeting of Creditors. So in practical terms the Court was confronted with a contributory seeking to override the wishes of the creditors as to who the Joint Liquidators should be.

17. It is against this factual background that the question of the governing legal principles for making the permanent appointment fell to be considered. I was assisted by the following statement of general principles set out in the JPLs' Skeleton Argument. In *Re Opus Offshore Limited* [2017] SC (Bda) 154 Com (17 February 2017), Hellman J stated as follows:

> "67. *The principles applicable to the appointment of a liquidator were helpfully identified by HH Judge Maddocks in Fielding v Seery [2004] BCC 315 Ch D at para 33. As summarised in Stanley International Betting Ltd v Stanleybet UK Investments Ltd [2011] BCC 691 Ch D by Stuart Isaacs QC, sitting as a Deputy High Court Judge, they include:*
>
> > *'(1) The test in relation to the appointment of a liquidator is whether it will be conducive to both the proper operation of the process of liquidation and to justice as between all those interested in the liquidation.*

(2) Although the majority vote of the creditors will in the normal course prevail, creditors holding the majority vote do not have an absolute right to the choice of liquidator.

(3) A liquidator should not be a person nor be the choice of a person who has a duty or purpose which conflicts with the duties of the liquidator. He should in particular not be the nominee of a person against whom the company has hostile or conflicting claims or whose conduct in relation to the affairs of the company is under investigation.

(4) By contrast, it is not an objection to a liquidator that he is allied to or the choice of a person who is concerned to pursue the claims of the company through the liquidator."

18. It was very properly conceded that the local and English case law supporting the principle that the views of the majority of creditors normally prevail dealt with insolvent companies. Accordingly, the JPLs did not rely solely on the presumption that creditors wishes will normally prevail. Reliance was also placed on the fact Mr Lucas was the only person seeking to nominate alternative liquidators and he was someone against whom the liquidators might have to make an adverse claim. Such a person ought not, according to the third principle articulated by Stuart Isaacs QC in *Stanley International Betting Ltd v Stanleybet UK Investments Ltd [2011] BCC 691*, to be nominating permanent liquidators.

19. The latter point has particular force in the context of the present case. The present proceedings were commenced by way of what can only properly be viewed as a public interest petition, presented by the BMA, the relevant regulatory authority. The gateway to the ultimate finding that it was just and equitable for the Company to be wound-up under the Companies Act 1981 was, as the Winding-Up Order recited, the following provisions of the Investment Funds Act 2006:

"***Winding up on petition from the Authority***
36. (1) The Authority may present a petition to the Supreme Court for the winding up of a fund which—

(a) having been authorised under this Act has had its authorisation revoked; or

(b) is operating, or has been operating, as an investment fund in contravention of any provision of this Act.

(2) On such a petition, the Supreme Court may wind up the fund if it is of the opinion that it is just and equitable that the fund be wound up.

(3)Part XIII (Winding Up) of the Companies Act 1981 shall apply to the winding up of a mutual fund company under this section…."

20. Where the BMA has wound-up a fund and nominated joint provisional liquidators, in my judgment this gives rise to a strong presumption that their nominees are suitable to be appointed as permanent liquidators. In the case of a 'private' petition, the dominant consideration is justice as between the private stakeholders. Where a public interest petition is concerned such private interests are still important; but they are supplemented by the need to ensure that the public interests which prompted the winding-up in the first place are also served. It is inconceivable in a case such as the present that justice in this expanded sense would be seen to be done were the Court to prefer the shareholders' nominees to the creditors' and (indirectly, admittedly) the regulator's nominee as Joint Liquidators. To my mind, the most pertinent guiding principle articulated by Stuart Isaacs QC in the *Stanley International Betting Ltd* was the most overarching one:

> "*(1) The test in relation to the appointment of a liquidator is whether it will be conducive to both the proper operation of the process of liquidation and to justice as between all those interested in the liquidation.*"

Findings: the merits of the contributory's challenge to the First Creditors' Meeting

21. Having found that Mr Lucas has failed to establish his right to vote as a creditor, it followed that he lacked the standing to seek to quash and reconvene the First Meeting. The main purpose of his intervention appeared to me to be more to ward off potential adverse proceedings by the Joint Liquidators; not to advance "*the proper operation of the process of liquidation and to justice as between all those interested in the liquidation*". In these circumstances, no need to resolve the queries raised by a contributory about the JPLs' capacity to investigate the Company's affairs or their conduct of the provisional liquidation arose. After all, as counsel pointed out, these queries were raised by a person with a miniscule commercial stake in the liquidation and who was also a potential debtor of the Company.

22. On the other hand, if credible evidence had been placed before the Court of a fundamental flaw in the convening of the First Meeting of Creditors, the provenance of the evidence might well be irrelevant. No such evidence was adduced, however. It was conceded by the JPLs that the proxy forms prescribed by the Rules have been adapted. This is expressly permitted by the Rules. Rule 3 of the Companies (Winding Up Rules) 1982 provides:

> "*3. The forms in the Appendix, where applicable and where they are not applicable forms of the like character, with such variations as circumstances may require, shall be used. When such forms are applicable any costs occasioned by the use of any other or more prolix forms shall be borne or disallowed to the party using the same, less the Court shall otherwise direct.*"

23. The most potentially serious defect identified by Mr Lucas was a breach of the following rule:

> "*103 General and special forms of proxy [Forms 62 and 63] shall be sent to the creditors and contributories with the notice summoning the meeting, and neither the name nor description of the Official Receiver or liquidator or any other person shall be printed or inserted in the body of any instrument of proxy before it is so sent.*"

24. The proxy forms invited the persons completing them to indicate whether they were voting for or against the resolution that an application should be made for the JPLs to be appointed as Joint Liquidators. The JPLs were identified by name at the bottom of the forms in a description of the first of the two resolutions. Mr Wood submitted, I initially felt somewhat unconvincingly, that the intention of this rule was to prevent the provisional liquidator nominating himself as the proxy holder. However, I was ultimately satisfied that this was the most sensible interpretation which could be placed on this rule, especially when one takes the prohibition on proxy holders voting in their own financial interest (rule 108) into account. Further and in any event, I was satisfied that having regard to the statutory purpose of the First Meetings, that in this context there could be no objection to the JPLs' names being listed in the proxy forms. The inclusion of their names was essential to enable persons voting to indicate whether they supported the first resolution or not. Section 171 of the Companies Act 1981 provides:

> "*(b) the provisional liquidator shall summon separate meetings of the creditors and contributories of the company for the purpose of determining whether or not an application is to be made to the Court for appointing a liquidator in the place of the provisional liquidator.*"

25. Even if there were any defect, the JPLs' counsel reminded the Court of the following important rule which is clearly designed to prevent technical points being taken in winding-up proceedings, which ought to be efficient and pragmatically run:

> *"**Formal defect not to invalidate proceedings***
> *158 (1) No proceedings under the Act or the rules shall be invalidated by any formal defect or by any irregularity, unless the Court before which an objection is made to the proceeding is of opinion that substantial injustice has been caused by the defect or irregularity and that the injustice cannot be remedied by any order of that Court.*
>
> *(2) No defect or irregularity in the appointment or election of the Official Receiver, liquidator or member of a committee of inspection shall vitiate any act done by him in good faith.*"

26. Mr Wood aptly referred to two statements in two authorities which supported the proposition that even if the convening and conduct of the meeting was technically defective, it would make no sense to incur the costs of reconvening because the result would likely be the same.

27. Firstly, in a case where it was established that proofs were wrongly rejected for voting purposes at a meeting of creditors, *Re a debtor (No 222 of 1990), ex parte the Bank of Ireland and others* [19992] BCLC 137, Harman J (at 146 d-f) held:

> "*On considering the voting figures…it seems to me to be unnecessary for me to order the summoning of a further meeting*".

28. A similar approach was adopted by Lewison J in *Re Power Builders Surrey Ltd* [2009] 1 BCLC 250 at 260d-e. However, counsel relied in particular on the broader statement of principle which appears at 259g-h where the judge stated:

> "*[26]… The court must also, I think, be mindful that the summoning of a new meeting is likely to involve expense both for creditors, and also for the office - holder whose fees will be paid in priority to any dividend for creditors. Where insolvency is involved, the court should be concerned to minimise the costs involved.*" [Emphasis added]

Costs

29. The last quoted judicial statement reflects a golden thread which runs through insolvency law and practice. It is reflected in rule 158 of the Rules, which make it clear that technical irregularities do not without more invalidate any steps taken in the proceedings. The function of the liquidation process is always to maximize the returns to stakeholders and minimize liquidation costs. This is not a winding-up proceeding where it is clear that all stakeholders will make a full recovery regardless of what costs the liquidators incur. Accordingly, I felt bound to accede to the JPLs' application for the costs occasioned by Mr Lucas' decision to seek relief from this Court which he lacked appropriate standing to seek and which was found to be unmeritorious in any event. It is important that parties to winding-up proceedings who unsuccessfully pursue applications for their own personal benefit should not be permitted to do at the expense of other stakeholders in the liquidation.

Conclusion

30. For the above reasons on April 4, 2018 I granted the JPLs' application for their appointment as Joint Liquidators.

Dated this 5th day of April 2018 _____
IAN RC KAWALEY CJ