IN THE GRAND COURT OF THE CAYMAN ISLANDS

FINANCIAL SERVICES DIVISION

CAUSE NO: FSD 33 OF 2011 (ASCJ)

IN THE MATTER OF THE COMPANIES LAW (2010) REVISION

BETWEEN:	**RMF MARKET NEUTRAL STRATEGIES (MASTER) LIMITED**	**PLAINTIFF**
AND	**DD GROWTH PREMIUM 2X FUND (In Official Liquidation)**	**DEFENDANT**

IN OPEN COURT
BEFORE THE HON. ANTHONY SMELLIE, CHIEF JUSTICE
THE 24TH -26TH SEPTEMBER 2014, 17TH NOVEMBER, 2014

APPEARANCES: Mr. Peter McMaster QC, Mr. Jeremy Walton and Mr. Jeremy Snead of Appleby for the Joint Official Liquidators ("JOLs") of the DD Grown Premium 2X Fund (in Liquidation) ("the 2X Fund");

Mr. Nigel Meeson QC, Mr. Ben Hobden and Erik Bodden of Conyers Dill & Pearman (Cayman) Limited for RMF Market Neutral Strategies (Master) Limited ("RMF").

Insolvent hedge fund company – payments made to investor for redemption of shares – whether payments made from capital – whether payments unlawful – whether payments recoverable by the liquidators for being undue or fraudulent preferences.

JUDGMENT

1. The defendant (the 2X Fund) is a Cayman Islands hedge fund company in liquidation. This judgment is delivered upon the 2X Fund's claim to recover from the plaintiff (RMF) five sums paid by the 2X Fund to RMF. The action started out as a claim by

RMF for a negative declaration[1] that it is not liable to repay the five sums paid to it by the 2X Fund and so the normal roles of plaintiff and defendant are here reversed. To reduce the risk of confusion, reference to the parties will be by their names (the **2X Fund** and **RMF** respectively) rather than as plaintiff and defendant.

2. RMF was a shareholder in the 2X Fund and the sums in question were paid by the 2X Fund to RMF after RMF served two notices to redeem shares in the 2X Fund in satisfaction of liabilities arising under those notices. The sums paid were as follows:

   (1) USD10,428,584 and

   (2) USD2,085,716 on 12 January 2009;

   (3) USD5,000,000 on 22 January 2009;

   (4) USD2,500,000 on 30 January 2009; and

   (5) USD3,000,000 on 6 February 2009;

   a total of USD23,014,300.

3. The claim to recover the payments to RMF is in the nature of what has come to be described in the investments industry as a "clawback" claim[2] by the 2X Fund JOLs. The JOLs claim recovery on behalf of all "creditors" of the 2X Fund – said to be those redeemed shareholders who were to be regarded as creditors at the times the payments were made to RMF but who received no payment for their shares or who received payments which did not satisfy the *pari passu* principle.

4. The parties' respective pleaded cases are contained in two Statements of Grounds, in which RMF responds to the 2X Fund. In directions hearings on 18 December 2013

[1] By its Originating Summons filed on 21 February 2011.
[2] A widely used term since the United States Sarbanes-Oxley Act 2002, which, among other things, requires the United States Securities and Exchange Commission to pursue the repayment of incentive compensation from senior executives who are involved in fraud.

and 15 August 2014, I directed that issues to be resolved by the Court at this trial will be confined to the claims set out in the 2X Fund's Statement of Grounds at paragraphs 57 to 60 and 64 to 67 and RMF's defences to those claims set out at paragraphs 12 to 15 of RMF's Statement of Grounds. The issues to be resolved now are described below. I also on 18 December 2013, directed discovery in relation to these issues and that the parties should prepare and file a Statement of Agreed Facts ("SOAF") and a Statement of Non-Agreed Facts ("SONAF"), attaching the documents to which the parties wish to refer in support of their cases.

5. The 2X Fund, in the cited paragraphs of its Statement of Grounds, relies on a number of separate causes of action in support of its claim to the disputed sums and these are described below. An account of certain agreed facts that are common to all of the causes of action, is provided by Mr. McMaster, with necessary changes by me, as follows.

THE COMMON FACTUAL BACKGROUND

Master/Feeder Fund Structure.

6. The 2X Fund was a feeder fund. Information to would-be investors about its Master Fund (also a Cayman Islands company) and the relationship between the 2X Fund and the Master Fund is contained in the Offering Memorandum (**OM**). It is stated in the OM (and was therefore intended from the outset) that the 2X Fund would invest "*substantially all of its capital in* [*the Master Fund*]". However (and as the OM makes clear) it was not intended that the 2X Fund's investment in the Master Fund would take the form of shares in the Master Fund.

7. The OM explains that the 2X Fund invests in the Master Fund on a leveraged basis and that the DD Growth Premium Fund also invests in the Master Fund, but on an unleveraged basis (" the Unleveraged Fund" or "the 1X Fund"). This meant that returns from the Master Fund to the 2X Fund, (unlike in some respects in the case of the 1X Fund), were returns on investment, not returns of equity by way of redemption of shares in the Master Fund.

8. Those returns on investment at the level of the 2X Fund, were used to pay redeeming shareholders based on the Net Asset Value calculations ("the NAV") declared by the Administrator of the 2X Fund (PNC Global Investment Servicing (Europe) Limited, ("PNC") as required by the Articles of the 2X Fund, from time to time.

9. It is pivotal to the present dispute whether those returns on investment, when used by the 2X Fund to pay redeeming shareholders, were to be regarded as payments out of capital or payments out of share premiums and, if the latter, whether nonetheless to be treated as payments out of capital for the purposes of the Companies Law, section 37(6) (a), in particular.

10. As this issue is indeed pivotal to the outcome of this dispute, I will proceed here to set out the rest of the factual context required for its resolution as the first issue.

11. The intended trading strategy of the Master Fund is described in the OM (internal page 9) as follows:

> *"…The Master Fund seeks to achieve its objective generally by investing in approximately 40/50 long short pairs primarily in US equities with a focus on large-caps. Each pair is composed of correlated stocks …"*

12. Pairs investment in correlated stocks is a well-known trading strategy. The Master Fund would attempt to identify two related stocks (i.e. a pair) that were inconsistently

valued in relation to one another by the market (i.e. one too high and one too low). Once such a pair had been identified, a long position would be taken in the undervalued stock (in the expectation of making gains when it rose) and a short position would be taken in the overvalued stock (in the expectation of making a profit when it was sold short and repurchased at lower prices when prices fell). Some investments in pairs were effected through derivative instruments known as "outperformance options".

13. The investment strategy was arrived at to ensure that the assets of the Master Fund (and in turn those of the 2X Fund) would be highly liquid at all times. This informed the investors' expectations that their redemption payments would be made within the deadlines set by the Articles and OM (the "constitutional documents").

Mr Alberto Micalizzi

14. The Investment Manager of the Master Fund was Dynamic Decisions Capital Management Limited ("DDCM") and the Manager of the 2X Fund was Dynamic Decisions Capital Management (Cayman) Limited. Mr Alberto Micalizzi was a director of each of those entities, as well as of the Master Fund, the 2X Fund and of the 1X Fund. He was also a director and Chief Investment Officer of the 2X Fund and the Chief Executive Officer of the Master Fund. He was central to the decisions taken by the 2X Fund to make all of the five disputed payments. This is not only an agreed fact but is also clearly apparent from the evidence (in Bundle C/G/1/106 to 245, in particular). This evidence will be of import when I come to address the JOLs' allegation that RMF obtained a fraudulent preference due to the actions taken by Mr Micalizzi in particular and will be examined in detail below in that context.

Master Fund Trading Losses

15. Until September 2008, the Master Fund traded without making untoward losses. Indeed, the indications are that their results were on the whole positive until this point. This appears from the Man Investment[3] monthly comments from September 2007 to September 2008. This is also borne out by the UK Financial Services Authority's (as it was then called ("FSA")) Decision Notice rendered on the inquiry into Mr. Micalizzi's conduct, resulting in loss of his licence and a fine of £3 million (Bundle 2.C.4.1790]). It is agreed, however, that thereafter the Master Fund suffered catastrophic losses related in particular to the collapse of the derivatives market triggered by the collapse of Lehman Brothers in 2008 [SOAF ¶80]. It is agreed that the losses in October 2008 were USD76,256,846 and in November 2008 were USD172,692,209. It is further agreed that the financial position of the Master Fund on 30 November 2008, was that its net asset value was minus $69 million. I am also invited to look carefully at the agreed table at SOAF ¶26.1, to see exactly what is further agreed as to the financial condition of the Master Fund and the 2X Fund at the material times[4].

16. I note the following aspects of this agreed table:

    (1) The NAV recorded by PNC the Administrator, was USD385 million but this was grossly overstated.

    (2) The assets were overstated:

[3] The parent company of RMF, comments in reports in the evidence bundle

[4] This table sets out the Master Fund's financial position as determined by the Master Fund JOLs as at 30 November 2008. It has been agreed for the purposes of the SOAF that Facts stated in the SOAF as determined, calculated, reported or stated by the Master JOLs are to be treated as agreed facts for the purposes of these proceedings.

(i) by USD273 million, being the value of certain entries in relation to worthless bonds (the Asseterra bonds – as to which more will be said below); and

(ii) by USD24 million, being the overstatement in relation to certain debt instruments.

(3) The true value of the assets before unpaid redemption liabilities as at 30 November 2008, was USD87.5 million.

(4) Unpaid redemption liabilities amounted to USD157 million.

(5) The parties are agreed that the Master Fund's liabilities therefore exceeded its assets by USD69.5 million, as at 30 November 2008.

The 2X Fund maintains that this agreed table shows an insolvent fund which was propped up on paper by a massive overstatement of the value of the Asseterra bonds. This, though not agreed by RMF, ought not to be controversial, says the JOLs, being a matter of simple arithmetic as shown above.

17. Things only got worse in December 2008 – January 2009: it is agreed that the Master Fund made a further loss in December 2008 of $146 million [SOAF ¶80]. By the end of December 2008, the agreed financial position of the Master Fund was minus USD251 million. [Agreed table at SOAF ¶28.1, which corresponds to the table at SOAF ¶26 but is for the month of December].

18. The historical explanation for the monthly losses appears to be the unwinding of previously recognised (but unrealised) gains on outperformance options, consequent on market volatility in the wake of the collapse of Lehman Brothers [[U.K. FSA

Decision Notice ¶23 and ¶24]. The losses appear to have represented about 85% of NAV [FSA. Decision Notice ¶4].]

Non-Reporting of Losses

19. The losses in October 2008 through January 2009 were not reported to investors. On the contrary, as shown in the SOAF and Bundle B of the evidence:

    (1) The loss in October 2008 was USD76 million yet the Investment Manager DDCM reported growth of 1.21% in October.

    (2) The loss in November 2008 was USD173 million, yet the DDCM reported growth in this month of 2.11%.

    (3) The loss in December 2008 was USD146 million, yet the DDCM reported growth in this month of 2.07%.

    This reporting was reflected in RMF's own internal reports on the performance of its investment in the 2X Fund[5], which are clearly based on the information provided by DDCM [see e.g. B/G/2//406 to 408], reporting positive returns for each of October, November and December 2008.

The Asseterra bonds

20. Tables agreed by the parties and showing the financial position of the Master Fund as determined by the Master Fund JOLs as at the end of November and December 2008, show the role of the Asseterra bonds in creating a positive reported NAV. The table for November 2008 [SOAF ¶26.1] demonstrates that the reported NAV was overstated by USD273 million by reference to these bonds and the table for

[5] Published monthly by RMF's custodian, CITCO Bank, Nederland, N.V.

December 2008 [SOAF ¶28.1] shows that the NAV in this month was overstated by USD546 million by reference to these bonds.

21. The Asseterra bonds were debt instruments purchased by the Master Fund acting by Mr Micalizzi, for a fraction of their face value[6]. The agreed facts in relation to these bonds are as follows:

(1) The bonds comprised five medium term convertible notes, each one with a nominal value of USD100 million, producing a total face value of $500 million and with a maturity date of 1 February 2018.

(2) The first purchase was dated as of 30 October 2008 and was for two bonds with a total face value of USD200 million. Only USD5 million was ever paid for these bonds (ignoring the transaction fee of USD1.25 million) (the "**October Bonds"**).

(3) The second purchase was dated 11 November 2008 and was for a further three bonds with a total face value of USD300 million (the "**November Bonds"**). Nothing was ever paid for these bonds.

In fact it appears from the FSA. Decision Notice, that the October Bonds and the November Bonds may both have been acquired in a single transaction on 10 November 2008, artificially split into two; the first of which was backdated in order to allow it to be used in calculating NAV as at 31 October 2008 [Decision Notice, C/G4/1792/¶28]. It also appears that although nothing was in fact paid for the November Bonds, it had been agreed that a further USD10 million would be paid for these bonds.

[6] The bonds were obtained through a Nevada entity as issued by an Australian entity (Asseterra) which purported to own large reserves of high performance diesel fuel.

22. It is agreed between the parties, that the October Bonds (for which only USD5 million was paid) resulted in the Master Fund Administrator preparing a monthly NAV report for October 2008 on the basis that these bonds had a market value of USD190 million. That was on the supposed basis that, despite the fact that only USD5 million had been paid for the October Bonds, they had a stated cost price of USD100 million and that there was an additional unrealised gain plus interest on the bonds of USD90 million [SOAF ¶88]. The monthly NAV report for the following month, November 2008, included both the October Bonds and the November Bonds. Despite the fact that only USD5 million had been paid for these bonds (with the possibility that another USD10 million was due) the report for November attributed a total value of USD519 million to them [SOAF ¶88]. This was USD19 million more than their face value and USD504 million more than was to be paid for them at the time they were acquired.

23. As the figures in the SOAF reveal, it was the inclusion of the Asseterra bonds at these values in the NAV reports that allowed the Investment Manager to report positive growth in the Master Fund and 2X Fund, despite the enormous losses that had occurred in the final quarter of 2008. [There is a calculation in the FSA. Decision for each of the three months of this quarter that shows in more detail how the Asseterra bonds valuations were used to justify reporting trading profits in each of these months [C/G4/1835/¶5 and onwards] and it shows how trading losses in each of October, November and December 2008 were offset and slightly overtopped by so called "profits" from the bond purchases being booked in those months. The result was that

the losses for each of those months (as agreed and set out at paragraph 19 above) were turned into the growth figures shown in the reports from the DDCM.

24. The Master Fund JOLs have attempted to sell the Asseterra bonds, but they are considered to be worthless [SOAF ¶89]. The bonds have never produced a return and there is no evidence that any of the issuer, guarantor or owner of the assets by which the bonds were supposedly collateralised, were parties of any substance [FSA Decision Notice ¶72].

Share redemption provisions for the 2X Fund

25. The 2X Fund had an authorised share capital of 50,000,000 shares, of which 10 were Founder shares and the rest were Ordinary shares. 25,000,000 of the Ordinary Shares were denominated in USD and 24,999,990 were denominated in EUR(the other 10 being the Founder Shares). Ordinary Shares were redeemable and the contract for redemption was governed by the Articles and OM of the 2X Fund. The provisions follow a familiar form and can be summarised as follows:

    (1) The company was obliged to redeem its shares upon request being properly made by written notice (Art. 68).

    (2) Shares could only be redeemed on a Redemption Day (Art. 68).

    (3) Redemption Days occurred on the first business day of every month (see the definitions in the Articles and OM).

    (4) The price to be paid to redeem each share was the NAV per ordinary share prevailing on the Redemption Day (Art. 68).

    (5) While the NAV calculations were to be done by PNC, the NAV per ordinary share on the Redemption Day was the figure determined by the directors as at

the close of business on the Valuation Day preceding the Redemption Day (Art. 44). Valuation Days occurred on the last day of each month.

(6) No time was set for the determination of NAV but the Articles and OM required the redemption payment to be made as soon as possible and in any event, not later than 14 business days after the Redemption Day [Art. 74 and OM 90]. It must therefore follow:

(7) That the NAV was to be determined as soon as possible and in time to allow the redemption payment to be made no later than the last (ie: 14th) day for payment.

(8) Whether or not payment had been made for the shares, the subject of a redemption notice; those shares ceased to be outstanding at the close of business on the relevant Valuation Day and afterwards the price of those shares was considered to be a liability of the company (Art. 49).

26. Therefore under the Articles, a shareholder who had submitted a valid redemption request became a creditor of the company for the amount owed under the Articles on the day following the Valuation Day. That this is the proper construction of the Articles which are expressed in such terms, was accepted in the arguments before me and, as a matter of legal construction, settled by the Privy Council in ***Culross Global SPC Limited v Strategic Turnaround Master Partnership Ltd*** 2010 (2) CILR 364.

RMF's redemption requests

27. RMF was a subscriber to 693,630.656 ordinary shares in the 2X Fund. RMF made two redemption requests:

(1) On 29 October 2008 it sought to redeem 87,466.106 ordinary shares denominated in USD – reference 000027 ("**request 27"**). The Valuation Day for this request was Friday 28 November 2008 and the Redemption Day was Monday 1 December 2008.

(2) On 31 October 2008 it sought to redeem 437,330.534 ordinary shares denominated in USD – reference 000028 ("**request 28"**) – the Valuation and Redemption Days for this request were the same as for request 27.

RMF held 168,834.016 shares in the 2X Fund after these redemptions. These shares were the subject of a redemption request in January 2009 that was unsuccessful when redemptions were suspended, following the suspension of the calculation of NAV. More will be said about this later on in this judgment.

28. It was expected, on the basis of the published NAV prevailing at the date of requests 27 and 28 (that is: USD118.88 per share), that they would yield around USD62 million to be paid 14 business days after the Redemption day of 1st December 2008. RMF was not the only shareholder to submit a redemption request for 1 December 2008 – there were 6 other investors who submitted requests for the same day [SOAF ¶22] (together with RMF, the "**December redeemers"**).

29. In accordance with the construction of the Articles as outlined above, the shares of all seven December redeemers ceased to be outstanding at the close of business on the Valuation Day (Friday 28 November 2008) and as of 29 November 2008, the December redeemers became creditors of the 2X Fund for whatever they were entitled to receive on redemption. These entitlements are summarised (anonymously

as to the other six) at paragraph 22 of the SOAF for a total of approximately USD79 million as follows:

RMF	87,466.106 shares at USD118.880 = USD10,397,970.68 (requested 29 October 2008, amended 10 November 2008)
RMF	437,330.534 shares at USD118.880 = USD51,989,853.88 (requested 31 October 2008)
Investor 4	43,000 shares at USD118.880 = USD5,111,840 (requested 29 October 2008)
Investor 10	30,942.43 shares at USD118.880 = USD3,678,436.08 (requested 29 October 2008)
Investor 11	11,776.58 shares at USD118.800 = USD1,399,999.83 (requested 24 October 2008)
Investor 7	12,707.66 shares at USD118.880 = USD1,510,686.62 (requested 22 October 2008)
Investor 12	USD300,000 (at USD118.880 per share = 2,523.553 shares)[7] (requested 24 October 2008)
Investor 13	26,385.658 shares at EUR 118.788 = EUR 3,134,299.54 ($4,525,615.11) (requested 28 October 2008)
Totals	EUR 3,134,299.54 (US$4,525,615.11) US$74,388,787.09

30. The redemption payments, as explained above, were due within 14 business days of the Redemption Day. It is agreed that this means that the payments were due by 19 December 2008[8] (taking into account 14 business days between the 1st – 19th) [SOAF ¶22]. It is agreed that this means that as of 19 December 2008, the 2X Fund had a liability to the seven December redeemers of USD79 million, viz: to RMF - USD62 million and to the six others, USD17 million.

The 2X Fund's receipt of cash and payments
out on of 12 January 2009 and subsequently

31. On 8 January 2009 the 2X Fund received a payment from the Master Fund of USD14 million. Prior to this receipt, the 2X Fund had no cash [[SOAF ¶42].] It is agreed

[7] This was a request for a redemption of a fixed cash amount, rather than of an amount of shares but of course, accepted as redemption of shares.

[8] And calculated by reference to exchange rates from EUR to USD available as of this date.

that most of this money (USD12.5 million) was paid to RMF a few days later on the 12 January 2009 [[SOAF ¶45].] The JOLs invite the Court's attention to two aspects of the position immediately before this payment was made: the first is the insolvency of the 2X Fund and the second is the way in which it is asserted that RMF, the only redeemer paid anything on 12 January 2009, was preferred over three of the other six redeemers, who were also to be regarded as creditors, on 12 January 2009 and subsequently. It must also be noted in this context however, that the other three received 100% and so could themselves be regarded as having been preferred over RMF and the others who received nothing.

32. The December redeemers were partially paid as follows:

Investor	Amounts received (and dates)	Percentage
RMF	USD5,085,716.76 (USD2,085,716.76 paid on 12 January 2009; USD3,000,000 paid on 6 February 2009)	
RMF	USD17,928,583.91 (USD10,428,583.91 paid on 12 January 2009; USD5,000,000 paid on 22 January 2009; USD2,500,000 paid on 30 January 2009)	(in total USD23 million or 36.89% as a percentage of $62 million)
Investor 4	USD5,111,840(USD1,022,368 paid on 16 January 2009; USD4,089,472 paid on 20 January 2009)	100%
Investor 7	Unpaid.	0%
Investor 10	Unpaid.	0%
Investor 11	Unpaid.	0%
Investor 12	USD300,000 (paid on 26 January 2009)	100%
Investor 13	EUR 3,134,299.54 (EUR 1,600,000 paid on 30 January 2009; EUR 500,000 paid on 6 February 2009; EUR 1,034,299.54 paid on 6 February 2009)	100%
Total paid	EUR 3,134,299.54 (US$4,063,807.18) USD28,426,140.67 = USD32.5 million of total claims of USD78,914,402.20.	

Solvency of the 2X Fund on 12 January 2009

33. The parties agree that at this time the 2X Fund had a liability to pay the seven December redeemers USD79 million and that, other than the 2X Fund's interest in the Master Fund, the 2X Fund had no assets of any value with which to meet this liability [SOAF ¶29]. The JOLs say that while RMF refuses to accept that the 2X Fund's interest in the Master Fund was of zero value by the end of December 2008 (notwithstanding that there is agreement that the Master Fund itself had no assets of any clear value at this time - [SOAF ¶29]), RMF is compelled to accept that the 2X Fund was insolvent at this time.

34. The JOLs say that RMF's refusal to admit that the 2X Fund's interest in the Master Fund on 31 December 2008 was zero, flies in the face of the parties' separate agreement that the Master Fund's value on the same date was minus USD251 million (see ¶17 above). If the Master Fund had a negative value on 31 December 2008, the 2X Fund's interest in the Master Fund could not on any realistic view have had a positive value, say the JOLs. And even if some argument could be found for the 2X Fund's interest in the Master Fund having a positive value, it does not help RMF, say the JOLs, unless RMF shows that the interest was sufficient to pay the entire USD79 million of redemptions which it is agreed were due – because if it was not sufficient, the 2X Fund must be held to be insolvent at that time, viz: 12 January 2009.

35. Moreover, say the JOLs, whatever the balance sheet position, the 2X Fund was undoubtedly cash flow insolvent on 12 January 2009, because it had liabilities that the parties agree amounted to USD79 million which it was clearly unable to meet in full

(or anything like in full) on that date (or at any time subsequently) from any of its realisable assets.

36. The JOLs drew to the Court's attention and seek to emphasise the following:

(1) All of the payments to RMF from the 2X Fund came from funds paid to the 2X Fund by the Master Fund [SOAF ¶41];

(2) Prior to the various receipts of these funds from the Master Fund (and even following receipt of those funds), the 2X Fund did not have sufficient cash to pay the outstanding redemption requests [SOAF ¶¶42, 46, 51, 54, 56, 61, 64 and 68].

37. It is also agreed that (apart from the value of its interest in the Master Fund) on 31 December 2008 the 2X Fund had no assets [SOAF ¶29]. Other than that interest it had no cash and had no receivables. So when the 2X Fund received a payment of USD14 million from the Master Fund on 9 January 2009, this was the only asset that the 2X Fund had available to pay its creditors. Those creditors included the December redeemers (including RMF), who were, as agreed, entitled to be paid some USD79 million. The USD14 million was on any view not sufficient to pay them. Instead of dividing the USD14 million rateably between the December redeemers, the 2X Fund simply paid the bulk of it (USD12.5 million) to RMF. No other redeemer received any payment on 12 January 2009, (see table at ¶32 above). There appears to have been no justification, say the JOLs, for treating RMF on 12 January 2009 differently from the other six December redeemers, all of whom had equal standing as creditors.

38. The foregoing matters of emphasis are presented as important parts of the factual context asserted by the JOLs for my consideration of their fraudulent preference claim and to which I will return below.

Further payments to investors

39. On 16 and 20 January 2009, another of the December redeemers (Investor 4) received two payments amounting to USD5 million (see ¶32 above). USD1.022 million of this was derived from the USD14 million received from the Master Fund on 9 January 2009, the balance was met from a further sum received from the Master Fund. This investor was fully redeemed by these payments. Investor 4 was therefore paid 100 cents in the dollar at a time when RMF had not been fully paid (RMF had by then been paid about 20%) and the other five investors had received nothing.

40. On 26 January 2008, another of the December redeemers (Investor 12) received a payment of USD300,000 and was fully redeemed [see ¶32 above]. This investor, say the JOLs, therefore received preferential treatment over RMF and over other investors who had not been redeemed at this time. [The JOLs say that depending on the outcome of this action, they intend to pursue clawback claims against Investors 4, 12 and 13 as well].

41. As shown above at the table at ¶32, RMF itself received further payments as follows:

(i) USD5 million on 22 January 2009.

(ii) USD2.5 million on 30 January 2009.

(iii) USD3 million on 6 February 2009.

42. When added to USD12.5 million received on 12 January 2009, RMF received the aforementioned total of USD23 million (or 36.89% of the USD62 million that it was owed).

43. By 22 January Investors 13, 7, 10 and 11 had not been paid anything in respect of their redemption requests and RMF was therefore paid ahead of them.

44. On 30 January and 6 February 2009, Investor 13 received payments of about EUR 3 million, by which this investor too was fully redeemed. Investors 7, 10 and 11 were not so fortunate.

Unredeemed investors

45. Investors 7, 10 and 11 were all December redeemers who were paid nothing. So, says the JOLs, when RMF received payments of USD23 million between 12 January and 6 February, RMF was receiving preferential treatment over Investors 7, 10 and 11.

46. There was no change to the solvency of the 2X Fund between the first and last payments to RMF and the position is therefore that each of the payments to RMF was made at a time when the 2X Fund was both cash flow and balance sheet insolvent.

Summary

47. The JOLs say that none of the facts outlined above ought to be controversial. The 2X Fund's case on the facts is that RMF has received USD23 million from an insolvent company. The money should have been distributed to its creditors *pari passu* in accordance with Cayman insolvency rules and the 2X Fund seeks to have the money brought back into the liquidation estate so that it can be properly applied. That would mean RMF proving in the liquidation for what it is owed and receiving its proper

share and no more, say the JOLs. The 2X Fund relies on four independent causes of action, each of which it says leads to the same result.

48. The first is however pivotal to the others and so can properly be addressed first. Before turning to it, I must mention here an aspect of RMF's response to the JOLs' claims by way of identifying fully, what the disputed issues are. I begin by mentioning RMF's stance on the issue of the solvency of the 2X Fund at the relevant times in January to February 2009 when the redemption payments were made to RMF.

49. RMF's stance in not agreeing that the 2X Fund was insolvent at those times is explained on the basis that it was in no position to know that and proof of the 2X Fund's state of insolvency at that and any other material time, must be established by the JOLs who pursue the clawback claim .

50. While as a purely forensic proposition, RMF's stance is understandable, the obvious state of insolvency of the 2X Fund at the relevant times as revealed by the facts which are set out above from the SOAF, cannot be denied.

51. I express as my first conclusion then, that the 2X Fund was, at the relevant times of the payments to RMF, insolvent, both on the cash flow basis (as to which more below) and on the balance sheet basis; in this latter sense as the result of the catastrophic losses sustained by the Master Fund in 2008 and because the Asseterra bonds entered in the balance sheet to disguise those losses, were worthless.

52. Two fundamental questions arise immediately from this finding of insolvency. First, were the payments out to RMF therefore in breach of the Companies Law as being unlawful payments of capital? If so, the JOLs say that the pleaded causes of action

arise primarily from the unlawfulness of the payments and for their recovery to the 2X Fund. Second, even if the payments were not unlawful, as they were made while the 2X Fund was insolvent and within six months of its winding-up, are they liable nonetheless to being recovered as fraudulent preferences if the payments were made with a view to giving RMF preference over other creditors?

53. The first question is a pure matter of construction of the relevant provisions of the Companies Law and depending on the answer, some of the other pleaded causes of action (save for the fraudulent preference claim) may or may not arise.

54. The second question – whether the payments were fraudulent preferences – will require the proper construction of section 168(1) of the Companies Law but will also be fact dependent; viz: was RMF in fact given undue preference in the payments it received?

THE JOLs' CAUSES OF ACTION

55. Against that background, the JOLs rely now on three primary causes of action:

(1) A claim that the redemption payments to RMF were unlawful payments of capital to a shareholder because, contrary to the requirements of section 37(6)(a) of the Companies Law (2007 Revision) (the **2007 Law**); the 2X Fund was cash flow insolvent because it was not able to pay its debts immediately after the payments were made. As a matter of law, the JOLs maintain that these payments, because they were unlawful, can be recovered by the 2X Fund either through a claim in restitution[9] or on the basis that RMF is required

[9] Citing the line of cases culminating in ***Kiriri Cotton Co. Ltd. v Dewani*** [1960] A.C. 192 and ***Amar Singh v Kulubya*** [1964] A.C. 14

in equity to account to the 2X Fund as constructive trustee of the misapplied monies (**the "Section 37 Claim"**).

(2) A claim that there was a mistake as to fact or law (as to the state of solvency of the 2X Fund) that caused the payments to be made to RMF, leaving RMF unjustly enriched and liable to repay the monies to the 2X Fund (**the Mistake Claim**[10]).

(3) A claim that the payments were fraudulent preferences and invalid pursuant to section 168 of the 2007 Law (**the Preference Claim**); alternatively, and on the basis explained in (1) above, that RMF is liable to account as a constructive trustee because they were payments in breach of trust (**the Constructive Trust claim**[11]).

A fourth claim – that RMF is liable as a knowing recipient of the payments made in breach of the directors' duty – was not pursued at this hearing (**the Knowing Receipt Claim**). It appears to be acknowledged by the parties that such a claim would require a degree of factual enquiry going beyond the factual premises which could be agreed in the SOAF.

56. There were some concerns expressed, nonetheless, by Mr. Meeson on behalf of RMF, whether this Knowing Receipt Claim can be distinguished from the Constructive Trust Claim being pressed and which also depends on the allegation that RMF had actual or constructive notice of the 2X Fund's state of insolvency when it received the payments.

[10] Relying on ***Barclays Bank v Simms*** [1980] Q.B. 677; ***Kleinwort, Benson Ltd. V Lincoln City Council*** [1999] 2 A.C. 349 and ***Pitt v Holt*** [2013] UKSC 26.
[11] Relying on ***Belmont Finance v Williams Furniture Ltd***. (No. 2) [1980] 1 All E.R. 393.

57. The position though, is that pursuant to a consent order dated 18 December 2013 and a subsequent consent order dated 15 August 2014, the Knowing Receipt Claim was stayed while the Section 37 Claim, the Mistake Claim and the Preference Claim (with its alternative Constructive Trust Claim) were set down for trial. These three claims were addressed sequentially in detail by counsel for the JOLs but, in light of the decision I have reached on the first – the Section 37 Claim – it will be addressed first. Apart from the Preference Claim which, unlike the others, has a footing apart from the Section 37 Claim and so must also be fully addressed; the others will not need to be addressed further in this judgment, in light of the decision I have reached.

THE SECTION 37 CLAIM

58. The starting point for this claim is the common law rule against distribution of capital to a shareholder. That rule which has come also to be expressed as the "*capital preservation rule"*, is described in the judgment of Lord Walker given on behalf of the United Kingdom Supreme Court in *Progress Property Co Ltd v. Moore* [2010] UKSC 55, at ¶15 as follows:

> *"PPC's case … relied on … what Mummery L.J. [in the Court of Appeal] referred to, at para 23, as 'the common law rule':*
>
> *'The common law rule devised for the protection of the creditors of a company is well settled: a distribution of a company's assets to a shareholder, except in accordance with specific statutory procedures, such as a winding up of the company, is a return of capital, which is unlawful and ultra-vires the company.'*

The rule is essentially a judge-made rule, almost as old as company law itself, derived from the fundamental principles embodied in the statutes by which Parliament has permitted companies to be incorporated with limited liability. Mummery LJ's reference to ultra vires must be understood in the wider and looser sense of the term[12] *.....Whether a transaction infringes the common law rule is a matter of substance, not form. The label attached to the transaction by the parties is not decisive."*

59. I acknowledge and accept the fundamental premises of the capital preservation rule:

(1) It is devised for the protection of a particular class of persons, namely, the creditors of a company.

(2) The rule is that any distribution of the assets of a company to a shareholder except in accordance with specific statutory procedures is unlawful.

(3) However, the rule must not be too broadly stated. Lord Walker and Mummery LJ were clearly not including all forms of payments of dividends as prohibited distributions of a company's assets. At paras 24-25 of his judgment, Lord Walker rejected as unsound (in keeping with the Courts below) a proposition that "*there is an unlawful return of capital whenever a company has entered into a transaction with a shareholder which results in a transfer of value not covered by distributable profits, and regardless of the purpose of the transaction. A relentless objective rule of that sort would be oppressive and*

[12]This, explained Lord Walker, is as identified in ***Rolled Steel Products (Holdings) Ltd v British Steel Corporation*** [1986] Ch 246 at 276- 278 (Slade LJ) and 302 (Browne-Wilkinson LJ) thus: "*a transaction which is ultra vires in the wider sense may confer rights on a third party who can show that he dealt with the company in good faith and for valuable consideration and did not have notice of the fact that the transaction, while ostensibly within the powers, express or implied, of the company, was entered into in furtherance of a purpose which was not an authorised purpose."*

unworkable. It would tend to cast doubt on any transaction between a company and a shareholder, even if negotiated in good faith, whenever the company proved, with hindsight, to have got significantly the worse of the transaction." As Lord Walker further explained – whether a transaction infringes the rule is a matter of substance and not form.

60. That the asset preservation rule forms part of the law of the Cayman Islands is confirmed in the decision of the Privy Council in ***Culross v Strategic Turnaround*** (above).

61. In the report at [8], Lord Mance in delivering the unanimous judgment, recognised the capital preservation rule even while emphasising the importance of the articles for the authorisation of the use of a company's capital for the redemption of shares in circumstances permitted by section 37 (1) of the Companies Law:

> *"It is a basic principle of company law that capital subscribed to a company may not be returned to shareholders otherwise than as prescribed by statute. Section 37(1) of the Companies Law permits the issue by the company of shares liable to be redeemed at the option of the company or shareholder, and s. 37(3)(c) goes on to provide that "redemption of shares may be effected in such manner as may be authorised by or pursuant to the company's articles of association".*
>
> *It is uncontroversial that this means that the manner in which any redemption may be effected must be authorised by or pursuant to the articles of association. As observed in Gower & Davies, Principles of Modern Company Law, 7th Ed. At 248 (2003) in relation to similar*

albeit not identical, provisions in the English Companies Act 1985, S.160(3):

"In order to protect the shareholders whose shares are not to be redeemed, the terms and manner of the redemption must be set out in the company's articles.""

62. In addition to its recognition of the capital preservation rule existing as protection for creditors, at least two further principles of importance for present purposes are apparent from this passage from Lord Mance. First, where authorised both by the statute and by their articles, companies are allowed to purchase (redeem) their own shares by way of return of capital. This is an important basis upon which it has been possible to promote and operate investment fund companies from within the Cayman Islands (as, indeed, from within other jurisdictions having similar statutory regimes).

63. Second, the articles which authorize the redemption of shares by return of capital, exist, in the context of an investment fund, not only for the protection of outside creditors but also for the protection of shareholders who, unlike shareholders of fixed equity in other types of companies, are investors having a right to redeem their investments represented by their shares.

64. However, it must be emphasised here, that in this case there is no complaint by the JOLs of a breach of the Companies Law or of the articles (or OM) of the 2X Fund, so far as non-redeeming shareholders were concerned. The argument of the JOLs here is that the payments to some of the December redeemers, in this case RMF, were unlawful because the payments were returns of capital and the 2X Fund was insolvent when the payments were made; that is: it was unable to pay all of its debts then owed

to the December redeemers who had all become creditors. Thus, it is also said that the payments to RMF were in breach of the *pari passu* principle and were fraudulent preferences.

65. The Companies Law applicable to the transactions in question here was that which was in force at the date of the transactions in January -February 2009; that is: the 2007 Revision. The relevant provisions are not, (as the JOLs' arguments would suggest), only in section 37, but also as RMF argues, in section 34 as well, as I will come to explain below. All references subsequently herein to section numbers are to the numbered sections of the 2007 Revision of the Law, unless otherwise stated.

66. As Lord Mance observed in ***Culross v Strategic Turnaround*** (above) in his interpretation of the Law, section 37(1) and section 37(2)[13] permit the issue and repurchase of redeemable shares, subject to there being provisions in the articles of the company authorising this. There were indeed such provisions in the Articles of the 2X Fund and some of these are already described above (at para 25). More generally, Articles 66 to 76 deal with the procedure for voluntary redemption of shares, Articles 77 to 88 deal with the compulsory redemption of shares and Articles 89 to 92 deal with general provisions applicable to both. Article 91 provides that: "*The Company may make payment in respect of the redemption or repurchase of the Shares in any manner permitted by the Statute, including out of capital*." The position is therefore that the Law and the Articles contain the necessary provisions authorising what would otherwise be unlawful at common law, as Lord Walker explained in *Progress Property* (above). That, however, is just the beginning. There

[13] Construing the 2010 Revision of the Companies Law which was then in effect and in terms the same as the 2007 Law.

were a number of restrictions on the exercise of the right to redeem shares and it is the question of just how these restrictions applied to the redemption of its own shares by the 2X Fund in early 2009, that is at the heart of this dispute.

67. The restriction that the Court is called on by the JOLs to consider was in section 37(6)(a), which expressed (and in the current Law still expresses) the capital preservation rule in the following terms:

> "*A payment out of capital by a company for the redemption or purchase of its own shares is not lawful unless immediately following the date on which the payment out of capital is proposed to be made the company shall be able to pay its debts as they fall due in the ordinary course of business".*

68. Section 37(6)(b) goes on to attach sanction to non-compliant payments, by the imposition of a fine of up to fifteen thousand dollars and imprisonment for up to five years.

69. The JOLs by Mr. McMaster, make the following observations:

(1) The section directly reflects the common law prohibition, stating that the payment out of capital *is not lawful.*

(2) The requirement to be met for the payment to be lawful is cash flow solvency; that is: that the Company shall be "*able to pay its debts as they fall due in the ordinary course of business",* immediately following the payment.

Payments out of capital

70. The first question I must answer is whether section 37(6)(a) applies at all. RMF by Mr. Meeson, denies that the payments it received from the 2X Fund were paid out of capital.

71. As developed in argument by Mr. Meeson, RMF's response is that the payments it received were not capital but (i) return of share premium (apart from the *de minimis* portion that reflected the par value of the shares) and were, in effect, the return of RMF's investments and (ii) were, even if returns of capital, not only authorised by the 2X Fund's Articles and OM, but also by the 2007 Law, because the 2X Fund was able to pay its creditors who, as at the dates of payment to RMF, were only those shareholders who had redeemed their shares; that is: the December redeemers, and who were to that extent, creditors of the 2X Fund for the unpaid amounts of their redemptions.

72. He submitted further that the payment of such debts out of capital was allowed. They were not the same as payments for the redemption or purchase of the 2X Fund's own shares; they were payments of lawful debts, the shares having already been redeemed and the debts accrued by way of the operation of the Articles and OM. See Article 90 and pages 37, 39 and 41 of the OM.

73. It must, however, be acknowledged immediately that at least $12.5 million of the payments to RMF were payments out of money received by the 2X Fund from the Master Fund and the OM explains that the 2X Fund's investment in the Master Fund will be an investment of the 2X Fund's *"capital or assets"*. This can be seen in the OM at Bundle B/B/19, which states:

> "[the 2X Fund] *will invest substantially all of its capital through a "master-feeder" structure in the* [Master Fund] *which is also a Cayman Islands exempted company. The Fund intends to invest directly or indirectly in the Master Fund on a leveraged basis."*

74. Further at the same page the word "*assets*" is used instead of "*capital*", and "*assets*" again appears at B/B/57.

75. However, nothing in my view turns on this use of nomenclature: the citation from ***Progress Property*** (above) suggests that at common law, any distribution to a shareholder of the company's assets is prima facie a payment of capital. But one must look to the substance of the transaction and, as will be explained below, there is a real distinction to be observed in this case between assets/capital on the one hand, and share premium and the proceeds of fresh issues of shares, on the other.

76. The JOLs say that the fact the payments were from capital is also clear from the trial balances for 2008 produced by the Administrator PNC for the 2X Fund, for the purpose of calculating the overall NAV and NAV per share for the 2X Fund (Bundle B/G pages 420 to 489). An agreed summary of the trial balances for 2008 was presented to me and examined during the arguments. (the "**Trial Balances Summary**"). It can be seen from the Trial Balances Summary that as at 1 January 2008, the 2X Fund had a total investment in the Master Fund of $139,703,856.07. It had received income from the Master Fund of $9,528,672.76 and had other assets of $317,202.96. There were stated liabilities of $4,507,137.77. The 2X Fund therefore as at that date, had a total NAV (assets less liabilities) of $145,042,594.02. The Trial Balances Summary also records that this equated to $141,539,941.81 of "Partners'

Capital" and $3,502,652.21 of "Retained Earnings". The figure of Retained Earnings does not change throughout 2008 but the Partners' Capital fluctuates, depending upon the net subscriptions or redemptions.

77. This is important, say the JOLs, because it shows that redemptions were being made by subtraction from capital.

78. For each month, it can be seen that the net subscriptions or redemptions resulted in an increase or decrease to the Partners' Capital and a consequent increase or decrease in the 2X Fund's investment in the Master Fund. What this shows, say the JOLs, is that as a matter of the 2X Fund's own internal accounting, subscription and redemption payments were treated as accretions to and subtractions from capital. This means that the 2X Fund was treating payments to redeeming investors as payments from capital which reduce capital.

79. In analysing this argument I must, indeed, as advised by the dicta from ***Progress Property*** (above) and as already mentioned, examine the substance rather than the form of the transaction, to see whether, the 2X Fund's income was in reality made up of share capital, as the JOLs contend or share premium, as RMF contends.

80. The JOLs contend that the internal accounting treatment of income as capital by the 2X Fund Trial Balance Summary, is entirely consistent with the statutory deeming provision in section 37 itself.

The construction of section 37(6)(a)

81. As set out at paragraph 67 above, the restriction on use of capital that the Court is considering is in section 37(6)(a). But section 37(5)(b) contains a deeming provision for the purposes of section 37(6). The deeming provision as it stood in the 2007 Law

operated by reference to the terms of section 37(5)(a) and so the terms of section 37(5)(a) should be read first:

> "*(a) Subject to this section, a company limited by shares or limited by guarantee and having a share capital may, if so authorised by its articles of association, make a payment in respect of the redemption or purchase of its own shares otherwise than out of its profits or the proceeds of a fresh issue of shares* (emphasis added)*."*

82. This sub-section thus authorised a company to make payments to redeem shares from sources other than profits or the proceeds of a fresh issue of shares on two conditions: "if so authorised by its articles" (which the 2X Fund was) and "subject to this section" (so on condition say the JOLs, of complying with the capital preservation rule in section 37(6)(a) against payments from capital unless cash flow solvent following payment). And then, for the purposes of this rule, there is also the deeming provision at section 37(5)(b) in the following terms:

> "(b) *References in subsections (6) to (9) to payment out of capital are, subject to paragraph (f) [(which dealt, in conjunction with other sub-subsections, with the use of the proceeds of a fresh issue as payment for redemption of shares)], references to any payment so made, whether or not it would be regarded apart from this subsection as a payment out of capital"*

83. The reference to "any payment so made" is, submits Mr. McMaster, a reference to any payment made in accordance with subsection (5)(a) and, obviously he says, not

merely a tautologous reference to any "payment out of capital". "Obviously", he says, because that would be circular – "references to payment out of capital are references to payment out of capital".

84. It follows, says Mr. McMaster, that the effect of the deeming provision of subsection (5)(b) is that, for the purposes of the rule in section 37(6)(a) against payments from capital, any payment that is not funded from profits or the proceeds of a fresh issue of shares – per subsection (5)(a) – is deemed to be a payment from capital. The payments to RMF were self-evidently not from profits (on the contrary the 2X Fund had only catastrophic losses) and they certainly were not [(he argued in this context although contradictorily in another context of his fraudulent preference arguments)] from a fresh issue of shares. They were therefore from capital and any failure to comply with section 37(6)(a) would render them unlawful given the state of cash flow insolvency of the 2X Fund.

85. This construction by which the JOLs invite the Court to conclude that section 37(5)(b) impacted upon section 37(5)(a) so as to have rendered all payments in respect of the purchase of a company's shares "*otherwise than out of profits or the proceeds of a fresh issue of shares*" to have been payments made out of capital and so deemed to be unlawful under section 37(6)(a) if made when the company was cash flow insolvent, is, as I remarked during the arguments, a strained and tortuous construction.

86. Not only would it involve the statute operating in that way by implication and deduction of reasoning so as to have created criminal liability when non-compliant payments of capital were made, the construction would also require the term

"payment out of capital" to have been regarded as including not only the paid up par values of the share capital of a company but also as including all share premiums generated to the accounts of a company from the sale of its shares, over and above their par values. Thus, because payments from share premiums would have been otherwise than out of profits or the proceeds of a fresh issue of shares. And this would be so although, as sections 37(5)(a) and 37(5)(b) then stood in 2007, they made no express reference to share premiums.

87. I felt compelled during the hearing to underscore the implications of this argument because, as touched upon above and as will be discussed further below, the redemption of shares in the ordinary course of business by investment funds such as the 2X Fund, will usually involve payments out of share premiums, even where their internal accounts may treat share premiums as assets or capital. The fact of the matter is that the articles permit such payments.

88. In the case of the 2X Fund, the restrictions strictly imposed by the capital preservation rule are nonetheless recognised and reflected in the constitutional documents. First, in part, in the Articles in the definition of "*Ordinary Share"*:

> *"...means an ordinary share in the capital of the Company of par value US$0.001 or €0.001 which may be issued in classes and having the rights provided for under these Articles."*

89. Thus the shares were to be issued at a par value of one-thousandth of a United States dollar or one-thousandth of a Euro, depending on which of those two classes of denomination they were issued in.

90. The classes and capital structure of the 2X Fund are then explained in the OM in these further terms (at page 37):

"The Fund has an authorised share capital of €25,000 divided into 10 Founder Shares, par value €0.001, per share and 24,999,990 ordinary shares par value €0.001 per share which are available for issue as Euro Shares or Euro Management Shares and US$25,000 divided into 25,000,000 ordinary shares per value US$0.001 per share which are available for issue as US Dollar Shares or US Dollar Management Shares."

91. Thus, the total authorised share capital of 50,000,000 shares with par values of EUR25,000 and USD25,000.

92. At page 39 of the OM under the heading "Offering of Shares" the following appears:

"Shares are issued in registered, book-entry form (meaning that no share certificates will be issued). During the Initial Offer, Euro Shares will be available at a price of €100 per Euro Share and US Dollar Shares will be available at a price of USD100 per US Dollar Share. Thereafter, Shares will be available on each Subscription Day at the prevailing Net Asset Value per Share of the relevant class. Applicants for Shares may also be required to pay an Equalisation Credit in order properly to account for the Incentive Fee. The net amount will be applied in subscribing for Shares. Fractional shares may be issued."

93. Thus, a potential total share premium value (at the initial offering prices of EUR100 or USD100) of EUR2.499 billion (leaving aside the 10 Founder shares) and USD2.5 billion -less the par values of EUR25,000 and USD25,000. Accordingly, the

nominal par value capital of the 2X Fund, would be *de minimis* compared to the value of share premiums, even when calculated at the initial offering prices. In other words, when examined in substance rather than form, substantially the entire value of the 2X Fund was identifiable as share premiums, apart from the *de minimis* nominal par value of the shares in issue.

94. Also, of significance to the resolution of the problems presented by this case, are the further provisions of the OM (p.p. 41-42) dealing with redemption of shares and as explained at paragraph 25 above. As there explained, shares were to be redeemed as investors would expect, not at their nominal par values or even at their initial issue prices, but at a per share price based on the NAV relevant to the class on the Redemption Day (after payment of any Incentive Fee with respect to the redeemed shares). Thus, at a price that reflected the premiums paid for the shares plus any market appreciations, less only the *de minimis* amounts of nominal par value capital.

95. It will be seen therefore, that shares were to be sold to investors at an enormous premium over par – all but one thousandth of the initial offering price of USD100 or EUR100 (or prices dictated by subsequent NAV calculations), respectively.

96. This would have been understood alike by investors and outside creditors of the 2X Fund. It would have also been understood that there would be ongoing redemption of shares at whatever NAV was struck for the respective redemption days and so that investing shareholders would have their shares redeemed at those prices. As noted above, the published NAV for the redemption of the USD class shares in dispute here, was USD118.88 per share.

97. If shares were to be reissued and re-subscribed, then that would also have been at the prevailing NAV prices per share for the relevant class at the date of subscription.

98. Thus, where the 2X Fund (like the many other similar fund companies) was concerned, the state of its balance sheet would be very fluid as shares were expected to be redeemed or subscribed on the ongoing basis, and this was reflected in the 2X Fund investment policy which was one that required its investments to be highly liquid.

99. With all such considerations in mind, treating all payments made for the redemption of shares from share premium as payments from capital and unlawful the moment an investment company like the 2X Fund became cash flow insolvent, would carry far-reaching consequences.

100. In reality though as I am satisfied and as already noted, the treatment of share premium as available for the redemption of shares in the ordinary course of business, was (and is) what investors and third party creditors alike would expect in the case of a fund like the 2X Fund whose ordinary course of business would involve, not only the sale, but also the redemption of shares to take place at a premium on the ongoing basis.

101. I also recognise of course, that it might be said that a state of cash flow insolvency is not "in the ordinary course of business". But, where a company is a going concern and not in winding up, what is in its ordinary course of business will also be defined by its constitutional documents, in the case of a company like the 2X Fund, its Articles and OM. It was precisely for dealing with crises such as cash flow difficulties, that the constitutional documents of the 2X Fund enabled the directors to

suspend the calculation of NAV and suspend redemptions of shares. But no such measures were implemented before the impugned payments to RMF were made.

102. The examination of the foregoing practical and conceptual difficulties is, in my view, a legitimate exercise in seeking the proper construction of the 2007 Law. The manner in which an investment fund like the 2X Fund may be able to respond to such difficulties was brought into sharp focus by section 34 of the 2007 Law, the relevant provisions of which I must now also set out in some detail:

> *"34(1) Where a company issues shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount of the value of the premiums on those shares shall be transferred to an account called "the share premium account". Where a company issues shares without nominal or par value, the consideration received shall be paid up share capital of the company".*

103. I pause here to note two things. First, it is an agreed fact in this case that the 2X Fund did not maintain a share premium account. Instead, all of its assets were invested with the Master Fund, as the OM declared. In return, as already noted, the 2X Fund was not issued shares in the Master Fund and did not have shareholder rights in respect of the Master Fund. Instead, the 2X Fund had booked investments in the Master Fund and in the event of winding up of the Master Fund, had only a contractual recourse against Societe Generale[14], through which all the Fund investments were made as the controlling leveraged third party investor (see OM p. 23). Thus, despite the Trial Balances Summary of the 2X Fund appearing internally

[14] The well-known multi-national French banking and investment service company headquartered in Paris.

to treat investments as capital and redemption payments as payments out from capital, the nature of its investments with the Master Fund was such that those investments could hardly have been regarded as capital for the purposes of the capital preservation rule and so as available immediately to meet the demands of creditors in the event of insolvency. In substance, what the 2X Fund had, was a contractual claim to its return of investment, enforceable as against the Master Fund and/or Societe Generale and when that investment was returned, it consisted almost entirely of share premium and appreciations from investment of share premium.

104. The second thing to note *en ṕassant* from section 34(1), is that the consideration received when a company issued shares without nominal or par value is to be treated differently – not as in the case of shares issued at a premium over par value as share premium, but as paid up share capital of the company.

105. This difference of treatment suggests that share premiums were (and are) not regarded by section 34 as paid up share capital of a company. And this difference of treatment carried through into the next subsection in a way that is pivotal to the present debate:

> *"34(2) The share premium account may be applied by the company subject to the provisions, if any, of its memorandum or articles of association in such manner as the company may, from time to time, determine including, but without limitation –*
>
> *(a) Paying distributions, or dividends to members;*
>
> *(b) ....*
>
> *(c) In the manner provided in section 37;*
>
> *(d) ...*

(e) Writing off the expenses of, or the commissions paid or discount allowed on, any issue of shares or debentures of the company; and

(f) Providing for the premium payable on redemption or purchase of any shares or debentures of the company.

Provided that no distribution or dividend may be paid to members out of the share premium account unless, immediately following the date on which the distribution or dividend is proposed to be paid, the company shall be able to pay its debts as they fall due in the ordinary course of business: and the company and any director or manager thereof who knowingly and wilfully authorises or permits any distribution or dividend to be paid in contravention of the foregoing provision is guilty of an offence and liable on summary conviction to a fine of fifteen thousand dollars and to imprisonment for five years." (Emphases added.)

106. [(Subsection 34(3) is a deeming provision that does not apply for present purposes. Subsections 34(4) and (5) go on to provide for the treatment of shares issued at a premium and allotted in pursuance of any arrangement in consideration for the acquisition or cancellation of shares in any other company - factors which also do not arise for consideration here)].

107. What is plainly relevant though, is that on its face, subsection 34(2)(f) provided that share premiums could have been used for the redemption or purchase of the shares of

a company like the 2X Fund whose articles allowed for it. It must follow, to my mind, that where the articles allowed, share premiums were not to be regarded under the 2007 Law, as having become part of the paid-up share capital of the company for the purposes of the capital preservation rule as expressed in the prohibition on the use of capital for the redemption of shares in section 37(6)(a)[15].

108. Widening the prohibition in section 37(6)(a), as argued by Mr. McMaster, simply by the implication of regarding section 37(5)(a) as including a reference to share premiums when no such express words appeared either in section 37(6)(a) or in section 37(5)(a) itself, would be by implication to write into section 34(2) itself a similar prohibition, despite its clear wording that allowed for the use of share premiums for the redemption of shares. In my view that would be an impermissible interpretation of the two separate regimes as they stood under sections 34 and 37 of the 2007 Law.

109. That this interpretation at which I have arrived is the correct interpretation of the 2007 Law, is bolstered by the further provision in section 34(2)(c) which recognised that section 37 provides a separate "manner", one might say "regime", for the application of share premiums.

110. But one is mindful of course, of the well-known linguistic canon that a statute must be construed as a whole[16] and so I must turn to look more closely at section 37 itself.

111. I note here though that section 34(2) plainly was not (and still is not) oblivious to the cash flow solvency test required by section 37(6)(a). On the contrary, as shown

[15] This is different from use for payments of distributions and dividends to members when a company was insolvent, as that was in the 2007 Law (and remains) expressly prohibited by subsection 34(2), the proviso, as shown in emphasis above.
[16] *Bennion on Statutory Interpretation*, 6th Ed. P.163.

above at paragraph 105 in emphasis, section 34(2) itself imposed (and still in the current Law imposes) such a test but as also noted, in respect only of the use of share premiums for the payment of distributions and dividends (see the words also in emphasis at paragraph 105 above).

112. It must be emphasized that there were no express words in section 37 which appeared to limit the uses permitted by section 34(2) itself. Rather, the words "subject to this section" as they appeared in section 37(5)(a) to limit the permissive operation of that paragraph, are a reference only to section 37 itself, not to section 34.

113. To read section 37(6)(a) by implication of section 37(5)(a) (which itself makes no express reference to share premiums) as treating share premiums as capital and so prohibiting the use of them for the redemption of shares once a company became cash flow insolvent, would in my view, be contrary to section 34(2)(f) as it then stood and so also contrary to the scheme of the statute when read as a whole.

114. Finally, and in my view conclusively on this point, section 37(6)(a) of the Law as it now stands (as amended by Law 10 of 2011) can no longer be said by virtue of what I describe as the "strained and tortuous construction", to prohibit the use of share premiums for the redemption of shares in circumstances where a company has become cash flow insolvent.

115. That issue has been put to rest by section 37(5)(a) and (b) of the Law which now respectively provide (since amendment in 2011):

> *"(5)(a) Subject to this section, a company limited by shares or limited by guarantees and having a share capital may, if so authorised by its articles of association, make a payment in respect of the redemption*

or purchase of its own shares otherwise than out of its profits, share premium account, or the proceeds of a fresh issue of shares;

(b) Reference in subsections (6) to (9) to payment out of capital are, subject to paragraph (f), references to any payment so made, whether or not it would be regarded apart from this subsection as a payment out of capital. (Emphasis added to show the 2011 amendment.)

116. When read with section 37(6)(a) (as set out above at para. 67) , the introduction of the words "*share premium account*" into section 37(5)(a) means that even if, as the JOLs argue, the expression "references to any payment so made" as that expression appears in section 37(5)(b), means payments made pursuant to section 37(5)(a); a "payment out of capital" as that expression appears in section 37(6)(a) could no longer include share premiums because they are now included in section 37(5)(a) as a permitted source of payment.

117. In other words, a simplified reading of all the foregoing subsections together as the Law now stands, means that by virtue of section 37(5)(b) read with section 37(5)(a) and for the purposes of the capital preservation rule in section 37(6)(a) , a "*payment out of capital*" would be a payment made "*otherwise than out of profits, share premium account(s) or the proceeds of a fresh issue of shares*."

118. Thus, clearly now under the current Law, payments out of share premiums for the redemption of shares when a company has become cash flow insolvent, are not prohibited as being payments out of capital by section 37(6)(a) by dint of the operation of and by implication of section 37(5)(a) and section 27(5)(b); even if, as I have found to the contrary, they ever were.

119. I consider that it is important in arriving at the meaning of the 2007 Law, to note the current state of the Law because there is no apparent reason of policy - and none was advanced in the arguments - why payments for redemption of shares out of share premiums should have been prohibited under the 2007 Law but no longer prohibited by the Law as it has stood since amendment in 2011. For this and further reasons below, I regard as compelling, Mr. Meeson's argument that the 2011 Amendment served only to clarify the Law.

120. Section 34(2) of the 2007 Law in its plain terms as set out above, clearly pointed to the conclusion that the use of share premiums for the redemption of shares was not disallowed in a state of cash flow insolvency.

121. There are further indications that the amendments in 2011 as they relate to this issue, were meant only to clarify the Law. One such arises from the deletion of section 34(2)(f) as it appeared in the 2007 Law (and that provision which expressly allowed share premiums as a source of redemption payments) , and the insertion instead of the term "share premiums" into section 37(5)(a). Thus, serving to remove share premiums from a possible (albeit strained and tortuous) reading of the term "capital payments" in section 37(6)(a), as including payments from share premiums.

122. Another indication appears from the insertion by the 2011 amendment, of the term "share premiums" into section 37(5)(c) as set out below (with the 2011 amendment emphasized):

> "(c) *The amount of any payment which may be made by a company out of capital in respect of the redemption or purchase of its own shares is such an amount as, taken with –(i) any profits and share premium of*

the company being applied for the purposes of the redemption or purchase; and (ii) the proceeds of any fresh issue of shares made for the purpose of the redemption or purchase, is equal to the price of redemption or purchase, and the payment out of capital permitted under this paragraph is referred to in subsections (6) to (9) as the capital payment of the shares."

123. Thus, another clear distinction between the use of the capital of a company and the use of its profits, share premiums and the proceeds of a fresh issue of shares, for the purposes of payment for the redemption of its shares. This provision explains, among other things, that only to the extent that the payment involves the use of capital (as distinct from any of the other three sources) will the payment be caught by the capital preservation rule in section 37(6)(a).

124. Given the complexities of this exercise of construction seeking to unravel what may fairly be described as ambiguities or obscurities in the Law, I have had recourse to the Hansards for the debate on the passage of the 2011 amendments and they proved to be illucidatory[17].

125. On the second reading of the Amendment Bill, this is what the mover had to say relative to the present issue:

"Madam Speaker, the amendments proposed constitute those that were considered the most critical to the local industry… there are a number of provisions that this amendment seeks to address [which are] as follows:

[17] For Monday, 11th April 2011; relying on the rule in ***Pepper v Hart [1993]*** AC 593; and as explained in ***Bennion on Statutory Interpretation***, 6th Ed. LexisNexis, at Section 217, page 566.

....

(4) Share redemption and repurchases: Madam Speaker, current provisions relating to share redemptions and repurchases can be difficult to apply in practice. The proposed amendments provide greater certainty for companies' directors and advisors, by clarifying that that manner of repurchase can be determined by a board if authorised by the Articles, by defining "paid up by reference to par value", and permitting surrender of shares for zero consideration."

126. The Law was in my view "clarified", among other things, by the amendments which inserted the term "share premiums" into section 37(5)(a) while removing the term as it was expressed in section 34(2)(f); thus including share premiums with profits and the proceeds of fresh issues of shares, as sources for the redemption of shares without falling foul of the capital preservation rule of section 37(6)(a). With that clarification of the section 37 regime in place, there was no longer a need for similar provisions in section 34 and hence the repeal of section 34(2)(f) itself. This all makes more sense of the Law, when read as a whole and in which the regime for redemption and purchase of shares is now as exclusively set out in section 37.

127. Accordingly, I find that the 2007 Law did not prohibit the use of share premiums for the redemption of shares when permitted by the articles of a company, even where the company had become cash flow insolvent because, by operation of section 34(2)(f) as it then stood, payments out of share premiums were not to be regarded as payments out of capital for the purposes of section 37(6)(a), which was (and still is) the statutory expression of the capital preservation rule.

128. Nor should this interpretation of the 2007 Law be regarded as surprising. The 2X Fund would have been but one of many Cayman investment companies even before the 2011 amendments which allowed, in the ordinary course of business, for the redemption of shares by payments from profits, share premiums and the proceeds of fresh issues of shares. The constitutional documents of these companies then (as now), allowed for redemption on the "first come first served" basis, depending on when redemption requests were notified. This was on the understanding that investors were entitled to receive not other investors' money, but the return of their own investments in funds in which share redemption values were based on NAVs and so in which there was to be very little exposure to risk of liability to third party creditors whose interests would out-rank investors' in the event of insolvency.

129. Notice to all the world that this was how investment companies operate was provided in the constitutional documents and hence notice also of compliance with the statutory requirement which calls for authorization of share redemptions by the articles.

130. As Mr. McMaster acknowledged in his submissions, no authority should be needed to establish that redemptions of shareholders form part of the ordinary course of business of a Cayman Islands Hedge Fund, but authority to that effect can be found in ***JP Morgan Multi Strategy Fund v Macro Fund Limited*** 2002 CILR 569.

131. In practical terms, what happened in this case was that RMF duly served its requests for redemption ahead of all but the six other December redeemers and received payments which (but for the *de minimis* amounts of the nominal share capital) came from the share premiums or proceeds of fresh issues of shares held by the Master

Fund for the 2X Fund. Thus, in reality, the payments to RMF were the return of but a part of RMF's investments ostensibly calculated by reference to the 2X Fund's internal accounting for shareholders' investments and based upon the NAV which the 2X Fund had published for December 2008 and which are treated by its Articles as having binding effect for all the purposes of the valuation and redemption of shares.

132. That being the manner in which the business of the 2X Fund was conducted in the ordinary course, it does not seem to me that the JOLs can now be allowed to vitiate the redemption of RMF's shares by reliance on the capital preservation rule as the doctrine is to be properly understood and as it was expressed in section 37(6)(a) of the 2007 Law.

133. It is to be emphasized that properly understood, the rule at common law, developed for the protection of creditors (or here in the context of an investment fund, other investors[18] as well) is that distribution of a company's assets to a shareholder, except in accordance with specific statutory procedures is a return of capital, which is unlawful. (See per Lord Walker in ***Progress Property*** (above).

134. Accordingly, where the distribution of a company's assets to an investor is in keeping with the articles promulgated in keeping with the statute, there is no breach of the statute, nor is there a breach of the common law rule.

135. By virtue of the specific statutory procedure of section 34(2) of the Law as it stood in 2007 – and as it stands now in section 37(5)(a) - the redemption of shares by return of share premiums and the proceeds of fresh issues, was allowed if authorised by the articles, as they were by the Articles of the 2X Fund and the right to payment for redeemed shares was not contingent upon the ability of the 2X Fund to pay other

[18] See per Lord Mance: ***Culross*** (above).

redeemed shareholders, still less other shareholders who had not yet redeemed their shares.

136. This does not mean that the 2X Fund should not have taken other steps which might have proven more equitable or contractually fair to all shareholders. Mr. Micalizzi should certainly have suspended NAV calculations in keeping with the Articles and OM and disclosed the true state of hopeless insolvency, rather than perpetrate the fraudulent use of the Asseterra bonds.

137. It is also regrettable that by means of that fraud, it appears that late subscribers' funds (ie: the proceeds of fresh issues) became available and were used to pay dividends back to the 2X Fund from the Master Fund and those funds used to pay some of the December redeemers, including RMF[19].

138. In effect, Mr. Micalizzi had put into train, a fraudulent "Ponzi Scheme".

139. The results have been grossly unfair to those December redeemers who received nothing, and even more so to those shareholders who had not yet sought to redeem their shares in the 2X Fund.

140. The loss will be borne substantially by the unredeemed shareholders and all but three of the December redeemers[20], with RMF itself bearing proportionately, the most substantial loss among the latter, and still further significant loss involving those 168,834.016 shares in respect of which redemptions were suspended.

141. As I will come to examine below[21], such are the unfortunate consequences when an investment fund becomes a Ponzi Scheme.

[19] More on this below when I come to deal with the Fraudulent Preference claim.
[20] Investors 4, 12, and 13 who received 100% of their redemption claims.
[21] When considering the dictum of Lord Sumption on behalf of the Privy Council in ***Fairfield Sentry Limited (in liquidation) v Migani and Others*** [2014] UKPC 9

142. In light of the construction of the Law at which I have arrived, RMF's primary contention is correct: the payments it received were lawful payments out of share premiums or out of the proceeds of fresh issues.

143. I need deal only briefly therefore with Mr. Meeson's secondary submission (as set out at paragraphs 71-72 above).

144. It has two premises, with both of which Mr. McMaster disagrees.

145. The first is that as the payments to RMF were paid to it qua redeemed shareholder and creditor, the payments out of capital were allowed. And so, even if the payments are to be regarded as made from capital (rather than from share premiums or proceeds of fresh issues), they were lawful and allowed.

146. To the contrary, Mr. McMaster says that these were payments for shares to a shareholder and so were unlawful when made from capital while the 2X Fund was insolvent.

147. This debate identifies a dichotomy that is perhaps unique to investment funds like the 2X Fund: are payments made to redeemed shareholders for the redemption of their shares to be regarded as payments for the purchase of their shares or as payments for debts owed to them as creditors?

148. If one looks to the form of the transaction, then the payments would be regarded as payments for shares. But if one looks to the Law and constitutional documents of the company as defining the substance of the transaction, the redeemed shareholder is a creditor and the payment is the payment of a lawful debt: see ***Culross v Strategic Turnaround*** (above).

149. In substance, if not in form then, payments from capital would not be unlawful, albeit the Law in its prohibition of fraudulent preferences may be engaged.

150. The second premise of Mr. Meeson's secondary submission depends on the 2X Fund having been solvent at the time of the payments to RMF. He contends for this on the basis that its only creditors were the December redeemers with a combined debt of USD79 million and that there was no conclusive evidence that the 2X Fund was unable to raise that amount. So, even if the payments to RMF are deemed to be payments for its shares from capital, they were allowed while the 2X Fund was solvent.

151. This is not an argument that I can accept in light of my finding that the 2X Fund (and the Master Fund) were insolvent. And this finding must be correct: at no time after 1st January 2008 were they able, from any source, to fully pay the debt of USD79 million owed to the December redeemers.

152. But there is, it must be noted, an air of unreality about this case instilled by the fact that the NAV per share of USD118.880 itself had no basis in reality. The Master Fund and the 2X Fund had no assets to justify that NAV or anything like it. This case has not, however, been presented on the basis of any other NAV per share. I am not asked to consider, for instance, whether, had a realistic NAV per share been applied to arrive at the debt owed to the December redeemers, the 2X Fund would have been deemed solvent on the cash flow basis and on that basis, whether over-payments were made to RMF and to the three other December redeemers who received payments. Here the clawback claim of the JOLs has not been presented on the basis that the NAV per share should have been correctly calculated at a much smaller sum, it is

presented on the basis that the December redeemers were all owed sums as creditors correctly calculated at NAV per share of USD118.880 but some (including RMF) were unlawfully paid from capital because the 2X Fund was insolvent. Otherwise, that the payments were fraudulent preferences.

153. I now turn to deal with that head of claim.

THE PREFERENCE CLAIM

154. As mentioned above, in this case, a basis of the JOLs' clawback claim is fraudulent preference, as that principle has come to be defined by statute and explained at common law.

155. The claim is presented on the basis that transactions taking place before the winding up of a limited company were liable to be treated as invalid pursuant to section 168(1) of the 2007 Law where they were made by way of "undue or fraudulent preference".

156. Section 168(1) of the 2007 Law provided:

> *"Any such conveyance, mortgage, delivery of goods, payment execution or other act relating to property as would, if made or done by or against any individual trader, be deemed in the event of his bankruptcy to have been made or done by way of undue or fraudulent preference of the creditors of such trader, shall if made or done by or against any company, be deemed in the event of such company being wound up under this Law to have been made or done by way of undue or fraudulent preference of the creditors of such company, and shall be invalid accordingly."*

157. That cross-reference in section 168(1) to "undue or fraudulent preferences of the creditors of a (bankrupt) trader" means that one must look to the Bankruptcy Law (1997 Revision) for the applicable corresponding test; in particular section 111(1) of the Bankruptcy Law which follows:

> *"Every conveyance or transfer of property, or charge thereon, and every payment, obligation and judicial proceedings, made, incurred, taken or suffered by any person unable to pay his debts as they become due from his own moneys, in favour of any creditor or any person in trust for any creditor, with a view to giving such creditor a preference over the other creditors, shall, if a provisional order takes effect against the person making, taking, paying or suffering the same within six months after the date of making, taking, paying or suffering the same, be deemed fraudulent and void as against the Trustee." (Emphasis added.)*

158. Mr. McMaster's submissions as to the corresponding test, set out following, are uncontroversial and are accepted.

159. A provisional order in bankruptcy is deemed to take effect at the time of the act of bankruptcy that gives rise to the provisional order. See the Bankruptcy Law, Section 35[22].

[22] Section 35 provides: The effect of the provisional order shall be deemed to have relation back to and to commence at the time of the act of bankruptcy being completed on which the provisional order is made, hereinafter referred to as "the commencement of the bankruptcy", or, if the debtor is proved to have committed more acts of bankruptcy than one, to have relation back and to commence at the time of the first of the acts of bankruptcy proved to have been committed by the debtor within six months next preceding the date of the presentment of the petition; but the effect of the provisional order shall not relate to any act of bankruptcy prior to the one on which such order is made, unless at the time of committing such prior act the debtor was indebted to some creator or creditors in a sum or sums sufficient to support a petition, and unless such debt or debts are still remaining due at the date of the provisional order.

160. Accordingly, the preference provisions under the Bankruptcy Law relate to relevant transactions within six months before the "act of bankruptcy".

161. Under section 168(2) of the 2007 Law, in a corporate insolvency, the presentation of a winding up petition (which, if successful is deemed the commencement of the winding up – see section 98) corresponds to the "act of bankruptcy" and therefore the relevant period is six months prior to the presentation date of any successful petition for the winding up of the company.

162. In this case, it is an agreed fact that all the payments to RMF were made within the six month period prior to the presentation of the petition to wind up the 2X Fund; which was presented on 18th March 2009.

163. On the basis of my earlier findings above, the 2X Fund was insolvent before any of the payments were made to RMF (or to any of the other December redeemers). On that basis, then any payment to RMF will have been rendered void under section 168(1) as an undue or fraudulent payment, if the payment was made with a view of giving RMF a preference over other creditors.

164. It is accepted that for the purpose of this inquiry, the state of mind in question here was that of Mr. Micalizzi, as the person who took the decision to make the payments in question.

165. As the principles emerge from the case law to be discussed below, the question is whether he was aware that the 2X Fund was insolvent at the time he made or directed the making of the payments and if so, whether he was aware that the payments were an undue or fraudulent preference within the meaning of the Law.

166. There is Cayman Islands authority for this test as explained in ***Segoes Services Limited (in Liquidation) v Oeoka, Kaweski and Highland Consulting Limited***[23]. There, in applying the English case law, it was held in the circumstances there presented that it was difficult to resist the inference of a fraudulent preference where the director of the insolvent company, being aware of the company's insolvency and of the demands of other creditors not yet satisfied, preferred his wife as a creditor of the company.

167. This was notwithstanding that the onus was on the liquidator to satisfy the court that the dominant intention of the debtor (per the directors of the debtor company), in allowing a particular creditor to be paid out ahead of other creditors, was to prefer that creditor, that is: to prove that the directors had the requisite state of mind – citing among other cases, ***In re M. Kushler Ltd***. (below).

168. Reference was made to the English case law as similar words were used in the Bankruptcy Act 1914, section 44, which deemed there to have been a fraudulent preference whenever a payment was made:

> *"…by any person unable to pay his debts as they become due from his own money in favour of any creditor… with a view of giving such creditor …preference over the other creditors…."*

169. English case law on the joint operation of the Companies Act and the Bankruptcy Act 1914 on this test, shows that the Court must determine the intention behind the payment, but in seeking to do so is entitled to draw inferences from the circumstances.

170. I accept that the following propositions can be distilled from the authorities:

[23] 2006 CILR Note 1; Cause 319 of 2005; para. 51-54

(1) The mere fact of a preference, that is: the consequence that one creditor gets paid ahead of others, is not on its own enough. For that approach would give no effect to the requirement that the payment is made with a view of giving a preference. The requirement is that the dominant intention is to prefer the creditor who receives payment. See ***In re M Kushler***[24] where both Lord Greane MR and Goddard LJ in their respective judgments on behalf of the Court of Appeal, explained that the statute is directing the court to ascertain the state of mind of the payer in relation to the particular transaction or transactions (at pp252 and 255 respectively).

Before the inference can be drawn that the payment was a fraudulent preference "*the court must be satisfied that the dominant motive was to prefer the particular creditor*" (emphasis added) (per Goddard LJ at p.255).

(2) The court can infer an intention to prefer from the circumstances of the case; there is no requirement that the intention can only be established by direct evidence. An inference of an intention to prefer can be supported by evidence like that suggesting an inference of any other fact. However, the burden of proof, to the civil standard, will be upon the person alleging the intention to prefer: ***In re Kushler***.

(3) Nor is it necessary to show an intention to disturb the operation of the bankruptcy laws in the sense of intending to avoid an equal distribution of the company's assets to the company's creditors. So,

[24] [1943] 1 Ch. 248

considerations as to whether the payer contemplated whether he would be able to pay his debts at some future time were irrelevant, once he was aware that the company could not pay its debts as they fell due at the moment when he made the particular payment. See ***In re Matthews Ltd.*** (in Liquidation)[25].

Speaking on behalf of the Court of Appeal Lawton LJ declared (at 265 D-E):

> *"What the court has to do is to construe the statute and it does not seem to us that the statute directs any inquiry whether the debtor's purpose was to disturb the operation of the bankruptcy law. The question under the statute is whether the payment was made "with a view of" giving the creditor preference over the other creditors."*

Lawton LJ addressed the dicta from In ***Re Kushler Ltd*** (above). In this way:

> *"It is said that the mere fact that a preference is shown is not sufficient to enable the court to draw the conclusion that the payment was fraudulent within the meaning of the statute, the court must be satisfied that the dominant motive of the debtor was to prefer the particular creditor…. No such motive can be inferred it is said, where the debtor honestly believed that all the*

[25] [1982] 1 Ch 257.

creditors would be paid within a period of three to six months. ([As was proposed in that case to have been the state of mind of the debtor, Mr. Matthews who caused the bank to be paid off with the available money thereby releasing his personal guarantees of the bank's loans to the company]).”

In conclusion, Lawton LJ explained the outcome thus:

“The result in our view, is that if the debtor, at the time when he makes the payment, genuinely believes that he can then pay his debts as they fall due there can be no intention on his part to prefer; there is then no knowledge on his part of insufficiency of assets which could indicate any intention to prefer. But that is not the present case. Mr. Matthews was aware that the company could not pay its debts as they arose. The preference that he gave the bank was that he deliberately paid it ahead of the other creditors and put upon them the whole risk of insufficiency of assets.

In our judgment, the payments were fraudulent preferences within section 44.”

I do not read this case as detracting in any way from the rule explained in ***In re Kushler*** (above).

Rather, it seems to me that Lawton LJ was here concerned to explain the importance of the debtor being actually aware of its state of insolvency at the time of making the preferential payment. There is no basis for reading his judgment as saying that the very fact of making the payment being aware of the state of insolvency was sufficient to make it a fraudulent preference, although, on the facts of the case then before the Court of Appeal, that might have been sufficient: Mr. Matthews being aware of the state of insolvency sought to prefer the bank because by so doing he would have been relieved of his personal guarantees given to the bank in respect of the company's indebtedness.

(4) It will also be sometimes necessary, as I find to be the case here, to distinguish between the motive of the debtor being something other than an actual intention to prefer when making the payment.

171. As Lord Evershed MR observed in ***Cutts (A Bankrupt) ex parte Bognor Mutual Building Society v Trustees of T.W. Cutts***[26]: "*…it is notorious that human beings are by no means single-minded, the intention to prefer, which must be proved, is the principal or dominant intention. There may also be a valid distinction…between an intention to prefer and the reason for forming and executing that intention.*"

172. Indeed, it is important to understand that that distinction is not a mere subtlety. A creditor who is given a payment which is otherwise lawfully due to him, cannot be required to surrender it back to the insolvent debtor's estate simply on the basis that the intention was to pay him what was due to him. It is that requisite intention to

[26] [1956] 1 WLR 728 at

prefer him as "*the principal or dominant intention*" that makes the payment an undue or fraudulent preference.

173. Lord Evershed recognised the importance of this distinction where he continued in ***Re Cutts*** in terms, which, although discursive, are fully worth reciting:

> *"It is at this point that the greatest difficulty, as it seems to me, arises, the difficulty being as often as not one of definition of the words used. If a debtor, knowing himself to be insolvent and knowing, also, that bankruptcy is imminent, deliberately elects to pay his oldest friend or his closest relative and to leave his other creditors unpaid or with little chance of being paid, it would appear to me to be irrelevant that he made the selection because of the love he bore for his friend or relative or because of his hopes for general but unspecified favours from them in the future. I am therefore not prepared to accept Mr. Raeburn's submission that a deliberate choice in the present case by the debtor of the Building Society for payment, because the society was the most important of his clients could not for that reason constitute a fraudulent preference. For if a debtor deliberately selects for payment A in preference to all his other creditors, it cannot, to my mind, matter, in the absence of other relevant circumstances, whether A is the debtor's oldest friend, closest relative or best client. On the other hand, where a debtor, owing money in all directions, has also robbed his employer's till, he may, knowing himself to be insolvent, elect to reimburse the till in order that, when the crash comes, the damaging*

fact of his robbery may not be discovered. Or a debtor may elect to make a particular payment under pressure of some threat, or to obtain for himself some immediate and material benefit or to fulfill some particular obligation. In these cases the reason for the payment affects, essentially, the intention in making it. In the instances given the intention, that is the real or dominant intention, will no longer be to "prefer" (that is to pay, as it were, out of turn) but will be to avoid the detection of a criminal act; to relieve the threat; to get the benefit and postpone the evil day; or to satisfy the particular obligation. Though the question of pressure in some form or another has, in the reported cases, often been the crux of the matter, it is plain that an inference of intention to prefer may be displaced in many other ways than by showing that the debtor acted under pressure. Examples are indeed legion. But in the present case the examples that I have given provide the closest analogies to the suggestions on the Society's side; and the real question before us is whether, upon the evidence and the findings of the county court judge, the true inference is intention to prefer or whether an inference of some other kind similar to those in the examples given is, at the least, not equally legitimate."

174. It emerges from that very careful analysis, that one is obliged in considering all the circumstances under which an impugned payment was made, to discern whether the dominant intention was to prefer (in the sense of deliberately paying out of turn being aware of the consequences for those creditors not paid) or whether the payment may

have been motivated by other concerns typically of the debtor himself, which are not impelled predominantly by an intention to prefer the creditor, even if preference is the consequence of payment.

175. A summary of the principles taken up in the foregoing discussion appears in the headnote of the judgment in ***Re Cutts*** itself and which is helpful, for my examination of the facts and circumstances of the payments to RMF in this case:

> *"(1) The onus is on the person alleging a fraudulent preference to prove to the satisfaction of the court that the payment impugned was made by the bankrupt with the intention of preferring the payee over his other creditors;*
>
> (2) *It is competent for the court to draw the inference of an intention to prefer from all the facts of the case;*
>
> (3) *The intention to prefer, which must be proved, must be the principal or dominant intention; there might however, be a valid distinction between an intention to prefer and the motive for that intention."*

176. Mr. Meeson for RMF argued that the correct analogy to draw would no longer be with the old bankruptcy regime of the Cayman law by way of joint operation with the Companies Law but with the Insolvency Act 1986 of England and Wales.

177. Section 229 (5) of the Insolvency Act 1986 provides that:

> *"The Court shall not make an order under this section (restoring the position to what it would have been] in respect of a preference given to any person unless the company which gave the preference was influenced in deciding to give it by a desire to produce in relation to that person the effect mentioned in subsection (4)(b) [that is: to put*

that person in a better position than he would have been in, in the event of the company going into insolvent liquidation].

178. Presented by Mr. Meeson as the leading English authority on these provisions is ***Re Mc Bacon*** [1990] BLCL 324 in which it was held that there must be a desire to produce the effect mentioned in section 229 and that the decision to make the preference payment must have been influenced by that desire.

179. Mr. Meeson submits that I should be guided by that dictum in my assessment of the circumstances here as to whether the payment to RMF were voidable preferences.

180. While it may seem simplistically attractive to find assimilation of expression between the new provision "*with a view to giving such creditor…a preference over the other creditors*" and being "*influenced by a desire to put (such creditor) in a better position than he would have been in in the event of insolvent liquidation*"; that manner of construction is not permissible. There is significant difference of wording as between the New English and old legislation (on which the Cayman law is based).

181. As Millet J (as he then was) emphasized in ***Re Mc Bacon*** (at p.335 d-f)

> *"I therefore emphatically protest against the citation of cases decided under the old law. They cannot be of any assistance when the language of the statute has been so completely and deliberately changed. It may be that many of the cases which will come before the Courts in future will be decided in the same way that they would have been decided under the old law. That may be so, but the grounds of decision will be different. What the Court has to do is to interpret the language of the statute and apply it. It will no longer inquire whether*

there was "a dominant intention to prefer" the creditor, but whether the company's intention was "influenced by a desire to produce the effect mentioned in section (4)(b)."

This is a completely different test. It involves at least two radical departures from the old law. It is no longer necessary to establish a dominant intention to prefer. It is sufficient that the decision was influenced by the requisite desire.

That is the first change. The second is that it is no longer sufficient to establish an intention to prefer. There must be a desire to produce the effect mentioned in the subsection."

182. So the difference between the old and new wording is not merely semantics and is especially important to note here, as even the amended provision in the 2013 Revision of the Cayman Companies Law[27] has retained the words "*with a view of giving such creditor preference over the other creditors*" and with them, the "*dominant intention*" test ascribed by the common law.

The Evidence relating to the payments

183. Against that background of the legal requirements, the JOLs and RMF have raised for my consideration a significant body of emails and other communications between RMF and the 2X Fund relating to the impugned payments and for which they respectively contend as showing that the payments were or were not fraudulent preferences.

[27] Section 145.

184. It is agreed that all the payments to RMF had originated from the funds paid to the 2X Fund by the Master Fund. And, prior to the various receipts of these funds from the Master Fund (and even following receipt of those funds), the 2X Fund did not have sufficient cash to pay all the outstanding redemption requests.

185. It seems also to be agreed and must be inferred and I so hold, that the person who decided upon and directed the payments to RMF (as indeed those to other December Redeemers) was Mr. Micalizzi. As noted above, it is an agreed fact that he was on the boards of both the 2X Fund and the Master Fund and was the key directing mind. He would have been aware that, as I have found, the 2X Fund was hopelessly insolvent as at end of December 2008 and when the impugned payments were made. Other figures of note on the 2X Fund side during the events surrounding the payments were Niall MacDougall (the Chief Operating Officer), Marta Renzitti, DD Growth's Chief Financial Officer and Sandradee Joseph (Compliance Officer). Their names also recur throughout the documented evidence which I will examine below. The object of the exercise is however, primarily to discern the intention of Mr. Micalizzi when directing the payments to RMF.

186. This evidence is best understood if set out in its chronological context and is unavoidably extensive.

DATE	EVIDENCE	SOAF or TRIAL BUNDLE REFERENCE
4/12/2008 (3 days after the December redemption	Being already concerned about the 3 days delay in payment, RMF by Gregor Gaurron make an onsite visit to the 2X Fund office in London where he meets Niall MacDougall and Marta Renzetti. The RMF Communications Journal	B/G1/58

date)	Log ("CJL") records that they were assured that the Fund is continuing to deliver strong performance. The Assets Under Management ("AUM") had grown to USD440 million, approached 13% YTD and that there were then no other redemptions apart from RMF's for year end.	
18/12/2008	An internal email at RMF's Pfaeffikon Switzerland office, records "DD Growth have not paid so far, so this money will not be in our accounts as scheduled…. However, we need to make sure that especially the DD Growth money….hit our accounts in the next days in order to be able to pay the money for the FX payments…could you please check with them whether they have already paid and if not ask them to pay asap (maybe they could do a prepayment in case NAV is not final yet)".	B/G1/80-82
19/12/2008	Entry in RMF's CJL of a communication between Michael Buerer of their Pfaeffikon office and someone at their Dublin office speaking of a phone call with PNC (the 2X Fund Administrator) "OPDD called Niall Whelan/PNC in order to investigate when they expect to finalise November NAV; Niall explained that they are awaiting "certain information". When we asked what information is pending, he was not in a position to specify further due to confidentiality. He suggested that we should send him an email so that he could refer our request to the right people."	BG1/92
22/12/2008	Another RMF CJL entry records that RMF "visited the manager of the DD Growth Funds office in London unannounced as we were concerned about the late redemption payment. RMF's redemption payment of approximately USD60 million with dealing date of 1 December 2008 did not arrive by the deadline of 19 December 2008 as stated in the OM. During the visit I (Phillippe Benedetti of Pfaeffikon) found out that the payment was not processed as the November NAV was not final yet. Main reason	B/G1/95

	for this delay was an unconfirmed existence of physical securities to the administrator by the new custodian (switch from MS to BNP[28] in November 2008) and a late broker quote." "I emphasized" writes Benedetti "that the late payment is of critical concern for RMF. Niall and Sandradee promised to speed up the process as much as possible. Unfortunately they were not able to agree on a specific time schedule." … "I asked them why they did not distribute a portion of the amount based on a late estimate (i.e: 90%). They both stated that this would be an exceptional action and that they have to threat (sic) all investors fairly and equally. Furthermore, Sandradee stated that according to the OM, distributions cannot be made as long as the NAV is not final. Additionally, she did not feel a two days delay is such an issue. …I highlighted that the delay is a major concern a critical (sic) for RMF. Both promised to do everything possible to speed up the process."	
24/12/2008	An email from Michael Buerer of RMF's Pfaeffikon office to Mr. Micalizzi and Ms. Renzitti of DD Growth: "I am writing to you because we are concerned about the continued delay of the November NAV and the continued delay of the payment of RMF's redemption as of December 1, 2008. Our analysts Gregor and Phillippe have been in continuous contact with you and your staff; but we keep on getting vague and unspecific information as to what exactly the reasons for the delay are. Either Dynamic Decisions cannot or does not want to provide specific details – both of which is (sic) not comforting for us as an investor and business partner. May I ask that you provide a specific explanation…also please provide us with a clear timeline when the payment will be executed….I have copied our Chief Risk Officer Serge Cadelli and our Head of Edge Fund Research Jaime Cartan. Please include them in your answer.	B/G1/100

[28] References to the investment banks Morgan Stanley and Banc National du Paris, respectively.

24/12/2008	There seems not to have been a direct response to this from Mr. Micalizzi himself. Instead, there are email exchanges between Niall MacDougall of DD Growth London and Phillippe Benedetti of RMF Plaeffiken: *"Phillippe* *Sorry I missed you again as I was on another call to Alberto (Micalizzi). He has informed me that he is in contact with Michael Buerer and Serge Cadelli on the matter of the redemption. This situation has not moved much this week unfortunately since we spoke, but I am being advised that we may be able to move some funds in advance of the redemption being finalized next week…this we would expedite and payments to yourself. This will be clearer on the 29th, however I realize that this may not give you the clarity you need right now. I will be in office next week, cancelling my holiday, to try and manage this process.* *Regards* *Niall"* *"Niall* *This does definitely not clear up the situation! Furthermore, I didn't get the point why it is not possible to get a clear information from your administrator as per when NAV is finalized and/or as per when BNP can confirm the existence of the physical instruments to the admin…. At least I see that you have risen priority of this matter. Thanks!* *Phillippe".* *Mr. Micalizzi and others are copied in.*	B/G1/101
28/12/2008	A lengthy but important email from Mr. Micalizzi to Michael Buerer, responding to his three points "in detail" under the heads (1) Delays in Finalizing NAV with PNC; (2) Non-Execution of Redemption and (3) Timeline (for payment). Here I will extract only the most telling aspects under each head.	

	"(1) *Delays in Finalizing NAV* *In the current market conditions, and over the last six months in particular, PNC has been taking more time to release the NAV. For example, last October's NAV was released at the beginning of December (almost 40 calendar days later) due to discussions and decisions over how to account for the Lehman exposure and set up a side pocket*[29]*. In general the 14 business day limit has rarely been observed due to the several entities in our funds…* *We also took two actions in November, meant to strengthen our ability to serve our investors which unfortunately are causing a onetime delay.* *(i) In early November, the Board approved my pre-active recommendation that any fair value calculation at month end…be provided by a third party auditor independent of the Fund's parties. The Board appointed KPMG to do this work, and they only delivered their result at close of business on Dec 19th.* *(ii) In November we decided to simplify our prime broker relationships, terminate Morgan Stanley and focus on BNP and JPM*[30] *….All of this took until December 19th ….PNC has requested that all bookings in the Nov. (brokerage accounts) be completed before the NAV is finalized.* *Non Execution of Redemption* *In Dec. we received USD155m worth of subscriptions from two large investors (please find attached confidential information about the largest (sic) of the two subscription forms, ie, 80 m the other one of 75m is available but I do not have*	

[29] I gather this is a reference to an accounting technique by which distressed or illiquid or hard to value assets are segregated from the remainder of a fund's portfolio to allow the fund to continue offering investors redeemable shares while preserving the value of the side-pocketed assets.
[30] JP Morgan Chase & Co.

	with me the scan version at the moment…. *At the end of November we got the EuroHedge nomination for an award at EuroHedge best market neutral fund for 2008 (please see below email from Nick Evans. Our strongest contender is GLC Diversified fund…Since Eurohedge awards depends on the risk-adjusted performance, we could still make it if we had a strong December (something around 2-3% MTD and hence 15-16% YTD).* *With that in mind, I expected to be able to manage your USD60m redemption very easily with a combination of new subscriptions and unencumbered cash totalling approximately 190m, a more than 3:1 coverage ratio.* *Unfortunately, the Madoff scandal broke a couple of days before the above-mentioned investors wired their monies. The panic situation that resulted led them and their banks to suspend subscriptions but not immediately, rather at the end of a back-forth process that end right before Christmas. The investors are still doing their best to re-activate subscriptions despite the negative …… However, it is unlikely this will all come through in the next two days.* (2) *As you understand, we are now going to liquidate our portfolio and generate enough cash to meet your redemption. Clearly the market situation does not help since liquidity is low these days.* *By Monday evening, however, I will give you a precise schedule of the steps we will take to meet your redemption. As I have already mentioned, one of the steps is to pay as much as possible by Wednesday.*	

	I keenly understand that RMF has the instruments to punish DD for any delay in completing redemption. I can only offer my sincere apology and express my disappointment that after successfully managing Bear Sterns transition, lenders' risk, the Lehman bankruptcy, the redemption of $90m in October and Madoff's scandal in December, we are causing such inconvenience to our best-class investor and business partner, right at the end of this turbulent year. Other much larger and well-known funds have chosen to manage similar disruptions by putting up gates on customer redemptions. We have chosen instead to stand behind our operational strength. This is a choice *I continue to believe is correct. Even if our redemption comes a few days later than anticipated, I hope you can come around to seeing there is an acceptable result given the year that has been.* *DD has an excellent chance of winning the EuroHedge best market neutral fund award for 2008. I am asking you to weigh the strong results we have delivered for you this year against a delay for a few days. RMF has been extremely important to our success. I continue to devote my full effort to managing the details of the redemption for the parent, and hold out hope that we will continue to work together in the future.* *Kind regards.* *Alberto"* There followed the referenced email from Nick Evans, editor of EuroHedge. *"Dear Alberto* *I just want to let you know that Dynamic Decisions Growth Premium has been*	

	provisionally nominated, under the category of Equity Market Neutral & Quant Strategies, for an award at the EuroHedge Awards taking place on 29 January 2009 at the Grovesnor House Hotel, Park Lane London. *This provisional nomination recognises the fund's excellent performance in an extremely difficult year in terms of delivering strong risk-adjusted returns to investors. A full list of the provisional nominations is published in the November/December issue of EuroHedge which is out this week….* *Nick Evans* *Editor, EuroHedge"*	
29/12/2008	One then sees an entry in RMF's CJL of this email exchange with Mr. Micalizzi created presumably by Michael Buerer: "*As RMF was provided only vague and unspecific information as to what exactly the reasons for the delays are, OPDD requested a specific explanation why the fund administrator PNC is not in a position to finalize the NAV, and why Dynamic Decisions CM was (sic) so far not been in a position to execute the payment, despite several indications that they expected to execute payment before Christmas. We also asked for a clear timeline when the payment would be executed. Alberto provided a number of explanations and indicated to provide a timetable until (sic) Dec 29, 2008. Note that he did not manage to deliver a specific timeline by then.*	
30/12/2008	*Micalizzi to Buerer* *"Dear Michael* *I am putting together the payment plan. Please allow few more hours and I will come back in*	B/G1/115

	details."	
31/12/2008	Buerer to Macalizzi *"Dear Alberto* *...have you had a chance to finalize the payment schedule by now? Also, would you be available for a call early next week? I have a number of follow-up questions with regards to the detailed answer you provided recently. The morning of Jan 5 or Jan 6, 2009 would be preferred."* Micalizzi to Buerer "*Dear Michael* *The 6th Jan is fine with me. Please let me know what time you prefer. Meantime, let me give you an update on where we stand. I got the official non-levered NAV from the administrator right yesterday evening and after a standard check that we are doing right now we will approve it; afterwards the 2X Levered NAV and the Luxembourg feeder NAV will be finalized by them, approved accordingly and communicated to our investors. We expect the whole process to be finalized by Tuesday 6th Jan and I anticipate no discrepancies with our estimated NAV. Sooner after, we will execute the liquidation of your redemption that will be finalized in the following 2/3 business days (please note that the first 5 calendar days in January included just 1 business day)."*	B/G1/114
Jan. 2009	In the evidence there appears a circular letter dated "January 2009" on Dynamic Decisions letterhead, addressed *"Dear Investors and Friends of Dynamic Decisions"* over Mr. Micalizzi's signature. It would have been sent to all investors, including RMF. I need quote only the beginning and end: *"Despite the exceptional market conditions of*	

	2008 Dynamic Decisions enjoyed continued success and the DD Growth Premium Fund achieved our target annual return across all share classes. This has been recognised by our nomination for the EuroHedge Awards 2008 in the category of "Equity Market Neutral and Quant Strategies…. *In closing, I feel each of the shocks from 2008 strengthened our organization. Many of you have already shared with us what we need to do to continue to earn your trust. Please let me or one of the senior team know if there is anything else we can be doing along with the all-important dimension of keeping your trust."*	
6/01/2009	RMF CJL records an *"update with Alberto Micalizzi on the status of the redemption and next steps. Alberto confirmed that the NAV calculation process is on schedule as outlined earlier (e-mail dated Dec 31, 2008) and he expects the NAV of the 2XL Feeder fund to be finalized by January 7, 2009….Alberto also indicated that the situation will be resolved within 2-3 days; reportedly 50% of the cash to satisfy the redemption is available and 50% readily available in the form of bonds and equities that need to be deposited first."* (Referencing an agreement with Micalizzi that RMF should be compensated for the delay)…. *"RMF will closely monitor progress and provide the manager with a draft agreement to recoup opportunity costs of a delayed payment."* This entry ends "*We will follow up on this with a separate legal review once more details and documentation are available, <u>but RMF is also considering a full redemption</u>."* The following pages in the evidence binder set out Michael Buerer's agenda of the issues he intended to raise with Alberto Micalizzi in that telecom and responses which formed the Log entry last described above. The agenda items	

	such as "*what exactly does KPMG deliver and for what instruments?* – referencing the alleged KPMG audit – and *"Specify the physical securities that needed to be transferred from MS to BNP"* – referring to the purported change of broker to BNP – are clear indications of a growing sense of concern on the part of RMF to verify Micalizzi's reports.	
6-7/1/2009	Further email exchanges between Buerer and Micalizzi follow on the telecom with Micalizzi ending: *"Perhaps in future RMF will not longer be an investor in our company but I wish you know that your words at the end of the call were extremely important to me and I will keep as a strong incentive for the future to do more and to do better.* To which Buerer replied: *"Dear Alberto* *Thank you for your kind words. I did not want to leave you under the impression that we are ungrateful for the results that you produced for your investors in the extremely difficult environment that all of us currently have to deal with. Let's try to get this situation behind us and have the issue resolved once and for all by the end of the week.* *Regards, Michael."*	
7/01/2009	There is a further email from Micalizzi in which he advises Buerer: "*Meanwhile I have instructed Sandradee to contact you (or to be ready to receive your communication) in regards to the compensation of the delayed payment that is occurring. As I said, we find it completely fair and we are ready to apply it to your case and to the case of the other investor that is redeeming with you in December. Would you please provide us with the*	B/G1/125

	draft of the agreement so that we can move forward accordingly."	
8/1/2009	Email Buerer to Micalizzi: "*Good evening Alberto* *Can you please provide us with a quick status update on where you stand in the redemption process? Are the monies going to hit our account tomorrow as planned?"* *"Dear Michael* *…. Yes, monies will start hitting your account tomorrow morning. I expect not less than 20 % of the redemption to be paid early in the morning. We started the operations of unwinding 2 days later and for this reason the redemptions will be fully paid in 2-3 days time. Tomorrow…I will give you another update and confirmation on the exact timing of the final payments. Kind regards, Alberto."* Also on this date an entry in the CJL of RMF shows growing concern at this change of tact by Micalizzi's concluding, *"It is clear that the manager impairs his credibility by providing this type of inconsistent information."*	
9/1/2009	And early the next morning the following exchange between Buerer and Micalizzi: *"Good morning Alberto* *….<u>At this point I am at a loss to understand what caused this new delay;</u> in your update later today can you please specify what caused the difficulties in raising the cash? <u>When we spoke on Jan. 6 2009 you mentioned that you have 50% of the cash available in the form of equities and bonds you need to dispose.</u> Clearly this does not reconcile to the 20% indication (in your email of last night)."*	B/G1/129

	"Dear Michael: *It is mainly due to the administrative aspects related to the internal approval required in these cases. Formally speaking, the NAV has not been ready (until today) as hence in order to avoid further delays we had to implement the procedure for partial payment (that we are doing for the first time). In terms of asset liquidation, we are just a bit more conservative in disposing some fixed income securities, that is it. Meantime, I have another update for you: an addition 40% of redemptions will be wired on Monday afternoon. As promised, later on today I will confirm the timing of the residual 40%. My apologies and best regards.* *Alberto."*	
12/1/2009	Email from Niall MacDougall to Michael Buerer "*Michael* *PNC have confirmed that they have instructed the 1st payment to you for 20% of the redemption in DDGP and I will forward the swift as soon as they provide it to me. I will advise you on the further payments when I have confirmed information.* *Regards, Niall"* To this Phillippe Benedetti of RMF's Pfaeffikon office replied: *"Hi Niall* *Thank you for the update! Alberto announced another 27m this Monday (please see attached email). Can you give us an update on that cash flow as well please?* *Furthermore, a swift confirmation from the administrator's account to ours would be very helpful….."*	B/G1/133
12/1/2009	*Email form Niall Macdougall to Phillippe*	

	Benedetti of RMF's Pfaeffikon office copied to Michael Buerer, Alberto Micalizzi and others: *"Phillippe* *I am waiting on Alberto's final instructions regarding the second staged payment, but please see the swifts below for today's two amounts…USD2085716.76 .... USD10428583.91.* [Hence the USD12.5 million paid on 12 January 2009.]	
13/1/2009	Benedetti replies the next morning: *"Hi Niall* *Thank you for the (last email)* *Could you gather more information from Alberto regarding the other 40%? Can you please tell me if the NAV is finalized in the meantime?* *...Phillippe"* There was no immediate response, so there was a further email two hours later: *Hi Niall* *I would appreciate any feedback!"*	
	Four hours later: *"Phillippe* *Many apologies for the delay, but I wanted to come back with concrete information to you. I have been waiting for an updated <u>cash flow statement to be provided to us, but it looks like it won't arrive before cut off for us to make payments out.</u> Unfortunately BNP still have a pretty early 3:30 pm cut off for USD payments in*	B/G1/133

	place and I was hanging on to see if we could turn the funds around. As things stand we plan to move the $27 m to PNC early tomorrow and they will pay you the next instalment as soon as possible....I hope the same day if we get the payment details quickly enough. I will send the swifts asap. *Regards, Niall"* To which Benedetti replies: "*Thanks for the update Niall. Please keep me posted once you know more. What about the NAV?*	
13/1/2009	In a letter to RMF, written in his capacity of chairman of DDCM, Mr. Micalizzi summarises the background of failure to pay RMF's redemptions in full and sets out the offer to pay interest in these terms: "*DDCM <u>acknowledge that as a result of the aforementioned matters there has been a severe delay of the payment of the redemption proceeds as set out in the OM and have offered to compensate RMF for the costs this has caused. Thus DDCM agree to pay RMF interest on the unreturned cash and will procure that the Fund returns the cash owed to RMF as soon as possible.</u> The interest will be charged at a rate of LIBOR (3 month USD) plus 5 per cent per annum and been (sic) deemed to have started accruing on a daily basis from 22 December 2008. A 3 month USD LIBOR rate of 1.46625 per cent per annum shall be used which results in a total interest rate of 6.46625 per cent per annum.* *We look forward to your acknowledgement that these terms are acceptable.* *Yours faithfully,* *Alberto Micalizzi"* There is no reply to this until 28 January 2009, as	

	to which see in turn below.	
14/1/2009	While insights into the thinking of those responsible for RMF would be less relevant than the thinking within DD Growth on the issue of voidable preference, the decision of RMF OpDD (Operation Due Diligence) to advise the RMF Board to seek the full redemption of all of RMF's shares in the 2X Fund is indicative of the relationships at this stage: "*We propose to fully redeem from the DD Growth Premium 2X Fund due to operational risk concerns in the context of the continued delay of the payment of the proceeds of RMF's redemption of USD60 million as of December 1, 2008….We acknowledge that various issues with external service providers seem to have contributed to the delay of the payment and notwithstanding that the manager has agreed to pay interest on the unreturned cash…we are under the impression that we are not given the full picture of the situation, and hence we believe that the manager's credibility has suffered to a point where we see no basis for a future business relationship in the context of institutional money management."*	
14/1/2009	Niall MacDougall to Benedetti and Buerer: "*Phillippe* *I just wanted to inform you that the November NAVs have been approved and after PNC go through their usual process will be released to investors. Please see below the 2X USD Class which will be confirmed to you:* *NAV USD Class: 118.880* *…if you need further clarification please refer to Alberto…regards, Niall."*	
	To which Benedetti replies *"Thank you for your update Niall!*	B/G1/140

	Can we expect the remaining 80% on Friday or will you further split amounts? *Regards* *Phillippe"*	
14/1/2009	Only some hours later on 14 January 2009, Michael Buerer, not being placated by Niall Dougall's notification of the NAV at 118.880 wrote to Micalizzi: "*Alberto* *Can you please elaborate on the reason for the continued delay of the payments of the redemption proceeds. I am sure you know that this case has gotten a lot of attention in the firm, and senior management expects an update. Thank you and regards,* *Michael."*	
15/1/2009	Micalizzi replies to Michael Buerer "*Dear Michael* *We have just approved the official NAV and hence the normal procedure for payment is going to start and I am going to make sure we have sufficient unencumbered cash to complete the rest of the payment. If I envisage any further delay I will (let) you know by today. I am aware of the internal escalation of this matter and conscious of the negative consequences that are likely to be produced in terms of our reputation at RMF. I am doing all my best to diminish such consequences and it is out of discussion that RMF will get 100% of its investment fully paid very shortly."* Buerer replies: *"Dear Alberto* *Thank you for the update. Once this is settled, maybe we find some time to recap the recent*	

	events in an informal discussion. *Regards* *M."*	
19/1/2009	RMF's CJL Records a report of a telecom between RMF's Pfaeffikon office (Buerer, Benedetti et al) and 2X Fund's London Office (Alberto Micalizzi which is telling: "*Update call on status of redemption. Alberto is still in the process of disposing assets to generate the cash to satisfy our redemption, in particular of a AA-rated bond issued by sovereign wealth fund.* *Reportedly he traded a tranche of USD10m on Friday, and will try to sell another USD20mn today, and the balance of USD16mn should be settled until Friday, January 23, 2009.* *…In order to further increase the pressure to resolve the situation, we made clear that the next step would be to involve the FSA.* *Obviously he prefers to refrain from selling equity positions in order to protect his track record as far as possible. We made clear that this is unacceptable to us, and that we expect him to put his clients' interest first."* [A further note explains RMF's understanding that the reference to the sovereign bonds must have been the understanding (falsely) Micalizzi had given them of the nature of the Asseterra Bonds. In this CJL entry, RMF notes its concerns about the prudence of the acquisition said to have been purchased "on margin".]	
21/1/2009	Concerns within RMF and the resolve to apply pressure on the 2X Fund escalate with a further unannounced onsite visit to the 2X Fund's Milan office. The report on that visit appears from RMF's Communication Journal Log: *"We decided to do an urgent onsite in Milan to get an update on payments related to our $60mn December 1 redemption and to hear DD's story about the continuous delay directly from Alberto.*	B/G1/167

	A new schedule has been proposed to us in which we should get 80% within a week. All in all, we still feel uncomfortable and have the impression that we are still not getting the full story behind the delays. [The Note continues to comment on Micalizzi's explanation that the investment in sovereign bonds on margin had been prompted by the collapse of Lehman Bros.] "*Following this development he didn't sell the bond immediately because the NAV was not final. This is a very cheap excuse blaming on the administrator as the strategy trades only very liquid large cap equities and the delay in NAV calculation is on DD's side as he was holding on information to the administrator, selling the whole bond position turned (out) to be a difficult task during the Christmas period as spreads became very wide. Actually in the Austria bond he holds about 53% of the issue! Instead he decided to sell the bond in small pieces without harming the track record of the fund. RMF's initial 20% payment (is) supposed to be proceeds from the first chunk sold. Today Jan 21 another $20mn shall be sold and $15mn was sold yesterday. There are far too many question marks in this story and we always get something new to digest….In early Jan. conf. call he claimed having 50% cash already. The situation is not pleasant and we will propose a full redemption on the earliest bond meeting. It is also very disappointing as Alberto was always very responsive and communicative but now delays with answers and looks for new excuses….."*	
22/1/2009	Following that on site visit Micalizzi writes: *"Dear Gregor and Andreas* *Thank you for taking time to come to our office and analyse the situation with me. I have made further inquiries with our counter-parties in order to ascertain the most feasible scenarios of*	B/G1/177

	inflows. *As a recap, I would like to share with you two case(s), where deadlines mean swift confirmation to you.* (Then follow his two "best case" and "worst case" scenarios.) Best case "*USD34m between today and Monday. Balance (approximately 12m) between Tuesday and Wednesday next week"* Worst Case "*USD20m between today and Monday. Balance (approx.. 25m) between Tuesday and Friday next week.* *As explained we will make payment to you of any amount coming to us during the day since the partial settlements on our side are occurring from various counter-parties and they can list our accounts at different times during each of the following days….* *Alberto"* Also on 22 January 2009 there RMF CJL entry by Michael Buerer at the Pfaeffikon office which states tersely as regards the investment in 2X Fund and Micalizzi himself being blacklisted: "*Manager Board decision* *Redeem; the Board also decided that the manager will be put on status "refused".*	
26/1/2009	The following exchange of note takes place between Phillippe Benedetti and Niall MacDougall: "*Hi Niall* *I have a question regarding the first redemption*	B/G1/180-181

	tranche for 12 January 09. You transferred a total of $14mln to the administrator's account. We finally received approximately $12.5m only. Do you know the reason for that difference?" *"Phillippe* *You are correct that we moved $14mn to PNC and our plan was to pay approximately 20% of the redemption requests at that point as per the Fund Directors' resolution. In trying to treat all redeeming investors fairly they paid out the difference ($1.5m) on the same basis to another investor who was redeeming a smaller amount for November.* *Regards, Niall."* *"Ok, that makes sense.* *Thanks for the explanation,* *Regards Phillippe."*	
26/1/2009	A further USD5 million was received following that meeting as evidenced by this email from Buerer to Micalizzi et al. *"Dear Alberto* *We would like to follow up on the status of the outstanding payments as outlined below. We can confirm that we have received the USD5mn you wired to PNC last week, and we expect a swift confirmation for the balance of the USD29mn (best case) or USD15mn (worst case) of the first instalment today. Please note that the timelines were reported to senior management on the occasion of a manager board meeting last Thursday afternoon and it is important that this timeline is met under all circumstances. Please keep us posted….* *Michael"*	B/G1/183

26/1/2009	Following a further email from Micalizzi to Buerer and Gregor Gawron (Pfaeffikon) there appears the following entry in the RMF CJL. "*Status update on redemption* *Giv(en) the fact that only 5 mln has been paid from the best/worst case scenario proposed to us last week we stressed for explanation. Apparently only $12 mln has been sold and not the $15 - $20 mln as communicated to us during the onsite last week. <u>The latest liquidation news is that the whole bond position will be settled as a swap versus a bank guarantee releasing 70% cash. Our next step will be to contact directors of the fund and proceed with legal actions should the payment not arrive within four days."</u>*	
27/1/2009	RMF's CJL records per Gawron (Pfaeffikon) "*Status update on redemption* *As still no money is flowing in <u>we have now officially informed the manager that we will proceed with legal actions as well as contact funds board of directors."</u>*	B/G1/187
	And an email of the same date from Buerer to Micalizzi: "*Dear Alberto*" [After setting out the most recent history of delay in the promised payments]…. *"Under these circumstances, we have no other choice but to proceed as discussed during our conference call on January 19, 2009. <u>We will take up the situation with our in-house legal counsel to draft a formal letter to the fund's Board of Directors of the DD Growth Premium 2X Fund, who bear the ultimate responsibility for the fund in general and this situation in particular.</u>* *RMF prepares this case for further escalation*	B/G1/188

	and explains all options available to enforce its investor rights. *Please keep us informed about the status of today's payment and future payments (including supporting evidence such as SWIFT confirmation). Thank you and regards.* *Michael"*	
28/1/2009	RMF writes to the 2X Fund "*to convey its dissatisfaction and concern regarding the current operation of the Fund, including the failure of the Fund and the investment manager, DDCM, to liquidate positions in the Funds portfolio to meet its redemption requests….* *RMF have expressed their frustration at the Fund (and DDCM's) failure to pay the redemption monies as set out in the OM. [*And by way of response to the offer to pay interest] *(DDCM) have acknowledged the Fund's failure to pay these monies on the terms set out in the OM, and in a letter dated 13 January 2009, agreed to pay RMF interest on the unpaid monies in order to compensate them for the cost loss* caused. *RMF requests that, in accordance with the fiduciary obligations owed by the Fund directors to all shareholders, you procure that (DDCM) liquidation sufficient positions to pay RMF in full, and that RMF receives this money (plus the interest that has accrued) within three business days from the date of this letter."*	
30/1/2009	Micalizzi responds in an email to Martin Glyn Jones (RMF's Lawyer, Investments Group Pfaeffikon) et al: "*Dear Martin* *I refer to our conference call today and your letter dated 28 January. I can assure you that we are taking this matter very seriously and we are*	B/G1/221

	doing our best to settle the payment of your redemption proceeds. As an act of good faith and to show you that we are committed to settling our obligations to you, we are paying USD2.5m today. Unfortunately, we have a temporary liquidity problem and we would ask you to grant us 5 business days to complete the payment to you. *I understand that my credibility is negligible at the moment with respect to this matter and hence on Monday I will provide you with third party evidence of the process that I have put in place in order to release the required cash to satisfy your redemption.* *Regards, Alberto."*	
	RMF's CJL records the internal views of this email: *"Status update on redemption* *Alberto confirmed the receipt of fax addressed to Fund's board of directors* [*i.e: the letter of 28 January 2009*]. *The directors are supposed to meet on Saturday. Further $25mln expected to be wired today. This is still just a fraction of the remaining $42.5 mln expected to hit our account today (30 Jan.) at latest according to the worst case scenario presented to us on Jan 22.* [The SOAF recognises that USD2.5 million. was paid on 30 January bringing the total by then to USD23 million paid.] *During the call Alberto said that he is working on the bank guarantee that would release 70% cash from the bond position held. This is again another "gaining time" statement as early this week (Monday Jan 26) it was communicated to us that the bank guarantee was about to be completed within 48 hours.* *Next step is to have DD issue an authorisation for RMF to gain a confirmation from fund's*	223

	administrator about the assets held, and as a last step to contact FSA."	
4/2/2009	Martin Glyn Jones writes to Alberto Micalizzi and other 2X Fund directors (Humphrey Polanan and Michael Nobel), a letter that aims to and appears to serve to widen the circle of concern within the 2X Fund, beyond just Alberto Micalizzi (and those answerable to him). *"Dear Directors* *Yesterday we finally received a statement from the 2X Fund administrator PNC, but to our disappointment found that it was nearly three weeks old and broke the portfolio down into style buckets, rather than providing positional information we had hoped for. We were particularly concerned that the statement showed $446,000,000 of outstanding fixed income receivables, something that would not be expected of a fund that was sold as following an equity market neutral strategy. We discussed this on a call with Humphrey Polanan last night and he explained that this entry related to a large position of corporate bonds that have been sold and for which the Fund is awaiting payment. RMF had previously been told that the fixed income securities held by the Fund were sovereign debt, not corporate debt, and this has just added to our concerns as to how the Fund is being managed. We urgently require third party confirmation from ONC as to the current composition of the portfolio, including details of individual positions, and requests that you, the Fund Directors, authorise PNC to provide RMF with this information. Please note that we are not seeking any preferential treatment, but ask that this information be provided to all investors.* *We look forward to your prompt response, best regards.* *Martin Glyn Jones.* *Lawyer Investment Structures Group"*	229

6/2/2009	A reply comes by email from Humphrey Polanan jointly with Alberto Micalizzi: This requires to be set out in full for the insight it affords into the thinking of the 2X Fund and its representations as at this date: *"Dear Martin and Gregor* *The Directors of the Fund have concluded our meeting, and have taken your concerns very seriously. We have raised a number of issues with the Investment Manager, the Fund staff and their lawyer.* *I felt it was important to keep you informed of the status of our discussions. And on behalf of the Directors, I am reaching out to you in that spirit.* *The directors would like to communicate to you that we understand your concerns that the redemption has only been partially paid by the fund. We believe that (an) urgent solution must be found so that the balance of your redemption can be paid promptly. Accordingly, we have instructed the Investment Manager to work with the utmost speed to find a solution to their liquidity issue.* *During the meeting we were briefed extensively by the Investment Manager and staff on the pending sale of the bonds held by the Fund. The settlement of these bonds is expected to provide the liquidity necessary to complete RMF's redemption request. We have been furnished information indicating that, while settlement has not yet taken place, it is imminent. We feel reassured that the Investment Manager is close to resolving this matter.* *Even as this resolution is being actively pursued, which it is not a full redemption, as a matter of good faith, the Investment Manager has made an additional payment of $3m to RMF today, with fuller payments expected early next week.*	B/G1/231

	A formal communication on the above, will be made to RMF on Monday. *This is indeed a difficult situation for all involved. I can reassure you that the Board and management of Dynamic Decisions is doing all that is possible to resolve this matter in a mutually satisfactory manner. Again, we have taken your concerns seriously, and appreciate your understanding. I look forward to remaining in touch.* *With kind regards.* *Humphrey Polanan, Director"*	

187. There was in fact that payment of USD3 million made on 6 February 2009; bringing the total to five payments to RMF in the amount of USD23 million or 36.89% of the total debt due to RMF in the amount of USD62 million.

188. The enquiry into the state of mind of the directing minds of 2X Fund can therefore proceed, based on the foregoing narrative, up to the time of that last payment on 6th February 2009.

189. What followed after that date in the chronology was, as shown in the email disclosure of 9th February 2009; RMF's decision having been taken on 7th February 2009 to refer the matter to the FSA and another email, also of 9th February 2009, internally between the RMF London office to RMF Pfaeffikon and RMF New York, confirming that the matter had indeed been referred to the FSA; "out of *grave concerns regarding the manner in which (DD Growth 2X Fund) is operating*".

Analysis

190. I have taken the trouble of setting out the narrative in full chronological detail because it virtually speaks for itself. It reveals a picture of unrelenting and escalating

pressure being applied by RMF and an equally consistent effort at prevarication and evasiveness on the part of Mr. Micalizzi (I make no observation about the states of minds of those answerable to him or those who were the other members of the Board of the DD Growth companies). Mr. Micalizzi was, as discussed above, the directing mind taking the decisions on redemption payments at all material times, both on behalf of the 2X Fund and the Master Fund.

191. In my view, the only reasonable inference to draw from the narrative in its entirety, is that in making the payments to RMF, Mr. Micalizzi was responding to pressure and out of concern that absent the payments, RMF would doubtless be able to and would insist upon regulatory intervention by the FSA and ultimately, take legal action.

192. There is no reasonable basis for a conclusion that his dominant intention was to prefer RMF. Rather, there is clear basis for concluding that, but for RMF's persistence and undoubted ability to compel, RMF might have received significantly lesser payments or no payments at all.

193. Apart from hoping to postpone or avoid the evil day, Mr. Micalizzi had no demonstrated motive for wishing to pay RMF ahead of any other of the December redeemers.

194. Having papered over the catastrophic losses with the Asseterra bonds, it appears he was stalling for time in the futile hope that the Funds under his management could recover. This may well have been a function of his failing to appreciate the true magnitude and effects of the Lehman Brothers collapse up to that point in time in early 2009.

195. I recognize that I am not privy to whatever exchanges there may have been between the 2X Fund and the other December redeemers for insight into Mr. Micalizzi's thinking vis-à-vis them. But that fact does not assist the JOLs. They have the burden of proving the dominant intention to prefer RMF. They have failed to do so in my judgment.

196. While, as I have noted, the narrative virtually speaks for itself, there are those aspects which I have emphasized which invite further comment.

197. Some of the more stark examples of the pressure applied by RMF should be noted:

- The unannounced visit to DD Growth Office in London on 22 December 2008, three days after the payments were due. Then the RMF CJL entry notes that DD Growth intended to "treat all investors fairly and equally".

  Later, on 7 January 2009 Micalizzi emails to Michael Buerer in similar terms in regards to the proposed compensation for late payment: "*we find it completely fair and we are ready to apply to your case and to the case of the other investor that is redeeming with you in December."*

  There is every reason to regard this as mere platitude: sop to cerberus to deflect RMF's concerns and it actions that would otherwise be taken. This was not, in any sense, an indication of willingness to give RMF preference. Indeed the language used, although now known to be insincere, was antithetical to preferential treatment.

  Despite the platitude, RMF was relentless: the entries for the 24 December 2008 show that they chased the 2X Fund virtually all day by telephone and email, pressing for a "clear timeline" for payment.

PNC, the Administrator, was also called. The pressure was continuously applied daily until receipt of the first and second payments on 12th January 2009.

Then came the worthless offer to pay interest for the costs of delay.

- Another stark example of pressure was the second unannounced visit to the 2X Fund Milan office on 21 January 2009. By this time Mr. Micalizzi had deployed the illusion of the Asseterra bonds (described as Austrian bonds) but RMF's representatives were sceptical: the 2X Fund was meant to invest in liquid large cap equities, not sovereign debt. Nonetheless, the illusion worked until it became clear to RMF that the excuses for not liquidating the bonds were yet another "gaining time" ploy and RMF's legal department were then called in.

  The letter of 6th February 2009 from lawyer Martin Glyn Jones to the Directors of the 2X Fund, made it plain that the game was up with the Asseterra bonds. (See entries above at 27th January to 4th February 2009).

  In the meantime, it stands to reason that the payments to RMF, including the latter two "good faith" payments of USD2.5 million and USD3 million, were timely and strategic payments aimed at appeasing RMF to avoid legal action and/or the threatened report to the FSA, not in my view, at preferring RMF in any sense.

- This is all the more so the only reasonable conclusion when it is borne in mind that the latter payments came only after RMF staff had referred the matter to the RMF Board and the threat of legal action or complaint to the FSA would

likely follow after. See entries at 19th (RMF CJL); and 27th January 2009 above from Buerer to Micalizzi from which it also appears (ie: in response to the 26th January email) that the third payment in the amount of USD5 million had been received only after the unannounced visit by RMF to Mr. Micalizzi in Milan.

198. The notion of preferential treatment also requires me to examine motive, as the case law explains. In other words, what reason would the 2X Fund have had for seeking to prefer RMF? This too invites an examination of Mr. Micalizzi's frame of mind and such utterances that were made by him capable of disclosing his motives are at best equivocal, when viewed from the point of view of the JOLs' case here. When viewed from RMF's point of view, they confirm that he was merely responding to pressure.

199. In his lengthy email of 28 December 2008 to Michael Buerer, Mr. Micalizzi states: "*I keenly understand that RMF has the instruments to punish DD for any delay in completing redemption.*"

200. In his 7th January 2009 email exchange with Michael Buerer he admits to recognising that "*Perhaps in future RMF will not longer be an investor in our company…".*

201. In his 15th January 2009 email to Buerer he admits: *"I am aware of the internal escalation of this matter and conscious of the negative consequences that are likely to be produced in terms of our reputation…"* And, in the same light, Micalizzi's email of 30th January to Martin Glyn Jones: *"I understand that my credibility is negligible at the moment with respect to this matter….".*

202. These utterances are not consistent with an active expectation or hope for an ongoing client relationship with RMF in the future. They were an admission to the contrary

and when viewed in the context of what had actually transpired in the wake of the Lehman Brothers collapse, Mr. Micalizzi could have entertained no realistic hope of keeping RMF as a client once his deception was revealed, as it must inevitably have been seen to be, by him.

203. Knowing the true position with the Asseterra bonds and the state of hopeless insolvency as only he was positioned to know, it would be illogical to infer that he was motivated by the hope of keeping RMF as a client. He therefore can only be inferred, in my view, to have been seeking to postpone the inevitable revelation of the true state of affairs.

204. On behalf of the JOL's it is submitted that the inference of fraudulent preference arises from other utterances by Mr. Micalizzi, and that RMF were moreover aware that they were being preferred.

205. I will now examine those further utterances. In his lengthy email of 28th December 2008 to Michael Buerer, Mr. Micalizzi refers to RMF as "*our best class investor and business partner*" and advises of the intention to "*manage your USD60 million redemption very easily with a combination of new subscriptions and unencumbered cash totalling approximately 190m., a more than 3:1 coverage ratio*". It was in this email that he also recognised that "*RMF had the instrument to punish DD".*

206. But these too were at their highest equivocal utterances: they could just as readily be revealing of a mind-set to string RMF along, as of an intention to prefer RMF with the motive of placating a favoured client.

207. When viewed in the full context of all that the extensive narrative of communications reveal, the former motive – that of seeking to postpone the disclosure of the

catastrophic losses and the hopeless insolvency of the 2X Fund, is the only reasonable inference to draw.

208. And I should emphasise that the expressed willingness on Mr. Micalizzi's part to make redemption payments from new subscription monies does not, by itself, strengthen an inference of an intention to prefer RMF, even where the monies available at the time were actually used to pay RMF alone: as in the case of the last two payments of USD2.5 and USD3 million.

209. Nor, in relative terms, was RMF actually given a preference. Having regard to the figures already examined above from the SOAF, the total payment to December redeemers amounted to USD32.5 million compared to redemption requests of December redeemers of USD79 million (USD32.5 million/USD79 million) or 41%, (using the then prevailing foreign exchange rates as per SOAF ¶24).

210. The total payments made by the 2X Fund to RMF were USD23 million and therefore 36.89% of the total of USD 62 million owed to RMF.(USD23/USD62 million).

211. Nor would Mr. Micalizzi have had reason to think that RMF would regard payments to it by use of new subscription monies as preferential treatment. This, because redemption of shares from the proceeds of new subscriptions happened and would be expected to happen, in the ordinary course of business of an investment fund like the 2X Fund.

212. As discussed above, in dealing with the section 37 claim, it was at that time (and still is) permissible by the Companies Law and the constitutional documents of the 2X

Fund, to use new subscription monies in this way[31]. Neither counsel before me argued to the contrary.

213. This issue would also have gone to the question not only of undue or fraudulent preference, but also to whether RMF had become a constructive trustee with an obligation to make restitution of the payments, being on notice that late investors' money had been used to make the redemption payments in a state of cash flow insolvency; that is: that the 2X Fund had become a Ponzi Scheme.

214. It is in this sense, as I understand it, that Justice Sumption spoke of it being "*inherent in a Ponzi Scheme that those who withdraw their funds before the scheme collapses escape without loss, and quite possibly with substantial fictitious profits. The loss falls entirely on those investors whose funds are still invested when the money runs out and the scheme fails*[32]."

215. This becomes the unfortunate reality when an investment fund like the 2X Fund becomes a Ponzi Scheme because it is on the basis of the constitutional documents of investment funds that investors will know (and those redeeming will expect) that not only profits and share premiums, but also the proceeds of new subscriptions, may be used to pay out redeeming shareholders. Having had their redemptions paid on the basis of NAVs which are also published in keeping with the constitutional documents of the fund, those who have redeemed, would not expect that there could be recourse against them by those who were still members of the fund when it collapsed[33].

[31] See section 37(5)(a) above
[32] Fairfield Sentry (above at [3]).
[33] Fairfield Sentry (ibid)

216. Here it is said by the JOLs that the recourse is sought not on behalf of the many unredeemed shareholders who suffered the brunt of the catastrophic losses, but only on behalf of those three December redeemers who were paid nothing. That they had become creditors like RMF and so although having suffered a much smaller loss than the bulk of the unredeemed shareholders (and perhaps than RMF itself), deserve to be dealt with on the *pari passu* basis along with RMF, as creditors.

217. It is on this basis that the fraudulent preference claim is presented but as I have found that there was no dominant intention on the part of 2X Fund to prefer RMF over them (or over any other December redeemer), in the end they can fare no better than any of the many other shareholders who had not managed to redeem their investment.

218. I conclude that there was a breach of neither section 37 nor section 168 of the 2007 Companies Law.

219. It follows that there is no need to consider RMF's change of position defence[34]; in which it claims that it changed its position in good faith – first by redeeming part of its shares in the 2X Fund and then by relying on the 2X Fund's stated NAV to redeem some of its shareholders.

220. Nor is there need to consider the JOLs' claims in restitution, constructive trust or mistake, each of which depends on the payments to RMF being declared to have been unlawful.

[34] Relying on Lord Goff's dictum in ***Lipkin Gorman (a firm) v Karpnale*** [1991] 2 A.C. 548, and ***Scottish Equitable LLC v Derby*** [2001] 3 All E.R. 369 as a bar to RMF's restitution claim.

221. The JOLs' claims which are based on the alleged breaches of the provision of the 2007 Law are accordingly dismissed.

Hon. Anthony Smellie
Chief Justice

17th November, 2014