

English High Court recognizes winding-up of solvent Bermudian fund

Introduction

On 17 May 2019, judgment was handed down in the UK High Court by Mrs Justice Falk in a case where recognition of a winding-up of a foreign investment fund was granted under the Cross-Border Insolvency Regulations 2006 (CBIR).

This is the first time that a UK court has examined in detail the United Nations Commission on International Trade Law (UNCITRAL) Model Law on insolvency and the interplay with its Guides to Enactment, as well as case law from various jurisdictions concerning its application to solvent scenarios.

Mrs Justice Falk found that:

- ▶ Recognition under the CBIR was available for entities subject to just and equitable winding-up
- ▶ “Insolvency” was not a prerequisite for recognition under the CBIR
- ▶ The High Court was not required to, and should not, conduct a factual assessment of the solvency of a relevant entity as part of a recognition application

Background

Sturgeon Central Asia Balanced Fund Ltd. (the Fund) was a closed-ended investment fund incorporated in Bermuda.

A participating shareholder brought a winding-up petition against the Fund after it amended its bylaws in 2014, taking away participating shareholders' power to wind the Fund up as otherwise envisaged by them soon thereafter. The amendment to the bylaws was not subject to a vote of a meeting of the participating shareholders, even though they had already expressed their opposition to the amendment.

After protracted and contested winding-up proceedings, an order was made for the Fund to be wound up on just and equitable grounds by the Court of Appeal for Bermuda on 23 March 2018. Following an unsuccessful application by the Fund, seeking leave to appeal to the UK Privy Council, Roy Bailey and Keiran Hutchison of EY were appointed Joint Provisional Liquidators (JPLs) of the Fund on 22 January 2019.

There is currently no question that the Fund is solvent as far as the claims of creditors are concerned, and no finding of insolvency has been applied for nor made. The liquidation commenced on a just and equitable basis, and the liquidation of funds, which would often be solvent as far as the claims of creditors are concerned are a common feature of liquidations performed offshore. This case is not a traditional solvent liquidation where the directors would be required to swear a declaration of solvency prior to the commencement of the liquidation.

The JPLs made an application for recognition under the CBIR on 25 March 2019.

The issue

The issue confronting the UK High Court in this case was that the most recent Guide to the Enactment to the Model Law (2014) - which is designed to assist in its interpretation - provides that:

"...as used in the Model Law, the word 'insolvency' refers to various types of collective proceedings commenced with respect to debtors that are in severe financial distress or insolvent... . A judicial or administrative proceeding to wind up a solvent entity where the goal is to dissolve the entity and other foreign proceedings not falling within article 2 subparagraph (a) are not insolvency proceedings within the scope of the Model Law. Where a proceeding serves several purposes, including the winding up of a solvent entity, it falls under article 2, subparagraph (a) of the Model Law only if the debtor is insolvent or in severe financial distress".

The High Court's ruling on the issue

Despite the terms of the Guide to Enactment and further academic commentary, Mrs Justice Falk ordered that the CBIR and case law were clear in that recognition was available in instances of just and equitable winding-up, being a law relating to insolvency, but that insolvency was not a prerequisite for recognition. The determinative issue is whether the law of the foreign proceedings relates to insolvency, not whether the entity subject to those proceedings is insolvent.

Mrs Justice Falk also noted that to decide otherwise had the potential to open the Court to the requirement that it determines the financial status of a given entity on each recognition application when "it is wholly unclear how financial distress might be determined, or what the threshold is". This would go against the purpose of the CBIR "of allowing recognition on an efficient basis, because of the factual enquiry that would be required".

The JPLs were advised by Clyde & Co LLP who instructed Joe Curl of 9 Stone Buildings, and by Marshall Diel & Myers Limited on matters as they relate to Bermudian law.

Impact

The decision provides welcome clarification on the question of the applicability of the CBIR to just and equitable liquidations. This judgment paves the way for subsequent recognitions of this nature and brings needed certainty to the cross-border insolvency regime and industry.

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