IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION
Hon Mr Justice Andrew J. Jones QC
1st April 2010, in Open Court

16/4/10

CAUSE NO. FSD 70 OF 2010 (AJJ)

IN THE MATTER OF PART 16 OF THE COMPANIES LAW

AND IN THE MATTER OF RESERVE INTERNATIONAL LIQUIDITY FUND LTD (IN LIQUIDATION)

Appearances: Mr Shaun Folpp, Ogier for the Petitioners
Mr Anthony Akiwumi, Stuarts for the directors of the Fund
Mr Hector Robinson, Mourant for Société Generalé

REASONS FOR JUDGMENT

INTRODUCTION

1 On 1 April 2010 I made a Declaration pursuant to Section 241(1)(a)of the Companies Law (2009 Revision) on the petition of Messrs Nicholas Carter and David Walker of PricewaterhouseCoopers ('the Official Liquidators"), by which I recognised their right and authority to act on behalf of Reserve International Liquidity Fund Ltd (In Liquidation) ("the Fund"), to the exclusion of its former directors and managers. The Court's Declaration is binding on all persons for all purposes in the Cayman Islands. I now give my reasons for making this Declaration.

FACTUAL BACKGROUND

2 The Fund was incorporated in the British Virgin Islands ("BVI") on 15 March 1990. It operated as an open-ended mutual fund under the BVI Mutual Funds Act 1996 (as amended) and is regulated by the Financial Services Commission. It carried on business as money market daily liquidity fund, aiming (but not guaranteeing) to maintain an NAV per share of US$1. It invested in fixed interest securities, including commercial paper and loan notes issued by Lehmann Brothers Holdings Inc ("Lehmann").

3 The Fund was a "sister" fund of a much larger American market fund known as the Reserve Primary Fund which had carried on business in New York since 1971 and was registered with the US Securities and Exchange Commission. The Fund was one of a "family" of funds, together known as the Reserve Group, which was operated from offices in New York. The Fund's investment management was conducted through Reserve Management Company Inc ("the Investment Manager") pursuant to the terms of an investment management agreement dated as of January 26, 2006 (Birch Affidavit, Exhibit CS3, tab 7). As a direct result of the Lehmann bankruptcy, the Fund ceased to be a viable business and its management have been attempting to wind down its affairs in an orderly manner since September 2008. In his first affidavit (§11), Mr Nicholas Carter states that, as at mid September 2009, the Fund had distributed some US$2.5 billion to its investors representing approximately 86% of its assets. He says (§18 & 19) that the Fund's remaining assets comprise some US$287 million deposited with State Street Bank, Boston and two amounts of US$10 million each deposited with the Cayman Islands branches of Branch Banking and Trust ("BB&T") and Société Generalé ("SocGen").

4 The Fund's directors attempted to wind up its affairs in an orderly manner without the benefit of commencing either a winding up proceeding in the BVI or a bankruptcy proceeding in New York. It seems to me that they were inherently unlikely to succeed, if only because the Fund has as many as 3000 investors/claimants, some of whom contend that they should be treated as creditors rather than shareholders. In these circumstances it is not surprising that the Fund has become the subject of a multiplicity of proceedings pending in both the US District Court for the Southern District of New York and the Supreme Court for the State of New York.

5 On 16 September 2009 an unpaid creditor commenced proceedings in the BVI High Court for an order that the Fund be wound up and that independent liquidators be appointed. On 27 October 2009 the Fund, acting by its Directors and Investment Manager, responded by commencing an

interpleader proceeding in the US District Court for the Southern District of New York by which the Fund seeks to be allowed to place all its assets in the custody of the court; to enjoin, once a final plan of distribution has been approved, all proceedings against the Fund or its directors; to obtain a discharge of the Fund and its directors from all liabilities to investors; and an order that investors interplead and settle between themselves their rights in the final distribution. The Fund has not made any filing under the US Bankruptcy Code.

6 On 18 January 2010 the BVI High Court made a winding up order in respect of the Fund and appointed Messrs Carter and Walker of PricewaterhouseCoopers as joint official liquidators (1st Carter Affidavit, Exhibit 'NC1'). It is common ground that, as a matter of BVI law the Fund's Official Liquidators are required to take possession of, protect and realise the Fund's assets and distribute those assets to its creditors and thereafter distribute the surplus assets, if any, to its shareholders. It is not in dispute that as a matter of BVI law the powers of the Fund's directors are automatically terminated (subject to very limited exceptions which are of no relevance to the issues raised on this petition) and that the Official Liquidators have full power and authority to act on behalf of the Fund, both in the BVI and elsewhere. On 28 January 2010 the Fund, acting by its directors, lodged an appeal against the winding up order. This appeal has not yet been heard and determined. On 30 March 2010 an application for a stay of all further proceedings under the winding up order was heard and rejected.

THE OFFICIAL LIQUIDATORS' PETITION

7 It is against this background that on 2 March 2010 the Fund's Official Liquidators presented a petition to this Court under section 241 of the Companies Law (2009 Revision) for a declaration that they be recognised as the only persons entitled to act on behalf of the Fund in this jurisdiction. The need for such a declaration arises because SocGen and BB&T have been given conflicting instructions. The Investment Manager (acting by or under authority of the Directors) has instructed the banks to transfer the two sums of US$10 million to a custody account with State Street Bank, Boston, where the money would become subject to the control of the US Court in the interpleader proceedings. The Joint Official Liquidators have given conflicting instructions that the funds be transferred to an account in the BVI where they would be subject to the control of the BVI High Court in the liquidation proceedings. Both banks responded, quite properly, by freezing the accounts pending determination of the issue whether, as a matter of Cayman Islands law, the Fund's Directors'/Investment Manager or its Official Liquidators are recognised as having authority to act on its behalf.

8 Section 241(1) provides that "Upon the application of a foreign representative the Court may make orders ancillary to a foreign bankruptcy proceeding for the purposes of – (a) recognising the right of a foreign representative to act in the Islands on behalf of or in the name of a debtor". Messrs Carter and Walker do not go on to seek any further ancillary relief under paragraphs (b) to (e) of section 241(1).

9 The expression "foreign representative" is defined to mean a trustee, liquidator or other official appointed in respect of a debtor for the purposes of a foreign bankruptcy proceeding. A "debtor" is defined to mean a foreign corporation or other foreign legal entity subject to a foreign bankruptcy proceeding in the country in which it is incorporated or established. It is not disputed that the Fund is a "debtor" which is the subject of a foreign bankruptcy proceeding and that Messrs Carter and Walker are "foreign representatives" within the meaning of section 241(1). Nor is it disputed that the effect of the winding up order, as a matter of BVI law, is that the powers of the Fund's former directors are terminated automatically and Messrs Carter and Walker are the only persons entitled to act on its behalf. Their powers and duties under the BVI Insolvency Act 2003 are very similar to those of an official liquidator appointed under Part V of the Companies Law (2009 Revision).

10 A declaration under section 241(1)(a) takes effect for all purposes and is binding upon all persons within the territorial jurisdiction of the Grand Court. For this reason, Rule 2(1) of the Foreign Bankruptcy Proceedings (International Cooperation) Rules 2008 provides that all such applications shall be made by petition, which means that they will be heard in open court and that any interested party may be heard. I first dealt with this matter in a case management conference on 25 March 2010 at which the Official Liquidators, the Fund's Directors, BB&T and SocGen were all represented by counsel. Although there was no evidence tending to suggest that any other party might in fact have an interest in this matter, I nevertheless directed that the hearing be advertised because any declaration made under section 241(1)(a) will be binding on all persons in this jurisdiction, whether or not they have actual notice of the petition.

APPLICABLE CONFLICT OF LAWS RULES

11 The applicable Cayman Islands conflict of laws rules are very well established. First, all matters concerning the constitution of a corporation are governed by the law of the place of incorporation, in this case the BVI. It follows that I must look to BVI law to determine who are the company's officials authorised to act on its behalf. It is not disputed that, as a matter of BVI law, the powers

of the directors have been displaced by the winding up order and that its Official Liquidators are the persons now authorised to act on its behalf. Second, the authority of a bankruptcy trustee or liquidator appointed under the law of the place of incorporation is recognised in the Cayman Islands. (Dicey and Morris, *The Conflict of Laws,* 10th Edition, Rule139(2) and Rule 143). The application of these legal principles led me to recognise, in *Re Bernard L. Madoff Investment Securities LLC (In Securities Investor Protection Act Liquidation)* (Cause FSD 47 of 2010), that the trustee appointed by the US Bankruptcy Court for the Southern District of New York be recognised as the only person entitled to act in this jurisdiction on behalf of that company.

12 I think that counsel for the Fund's Directors accepted that a proper application of the applicable Cayman Islands conflict of laws rules does inevitably lead to the conclusion that it is the Official Liquidators appointed by order of the BVI High Court who must be recognised as the persons entitled to act on behalf of the Fund in the Cayman Islands. As I understand it, Counsel's argument is that the grant of a declaration is a discretionary remedy and that I should exercise my discretion by (a) refusing to make any declaration; or (b) adjourning the petition pending the outcome of the directors appeal against the winding up order which is currently pending before BVI Court of Appeal; or (c) directing that the sums on deposit with BB&T and Soc Gen be paid into Court pending the outcome of the BVI appeal; or (d) ordering that the sums on deposit be paid into Court pending the outcome of actions (Cause Nos. FAD 83 and 84 of 2010) which were commenced against BB&T and SocGen on 29 March 2010 in the name of the Investment Manager. Counsel for the directors argues that I should exercise my discretion in one or other of these ways for the following reasons.

COUNSEL'S SUBMISSIONS ON BEHALF OF THE DIRECTORS

13 First, Counsel for the Directors argues that I should refuse to grant a declaration because, to do so will not lead to an economic and expeditious administration of the Fund's affairs. This submission is misconceived. I would only refuse to grant the declaration sought if it could be demonstrated that the law of the place of incorporation, pursuant to which a foreign representative has been appointed, is inherently inconsistent with Cayman Islands law in some material respect, such that recognition of the foreign representative's authority would be contrary to public policy. It cannot be suggested that the BVI Insolvency Act 2003 is inconsistent with the principles of Cayman Islands insolvency law. Nor for that matter could it be suggested that the US Bankruptcy Code or the Securities Investor Protection Act are inherently inconsistent with Cayman Islands principles. In effect, Counsel is asking this Court to look beyond the narrow

matter in issue, namely whether it is the Directors or the Official Liquidators who are entitled to act on behalf of the Fund, and to interfere in the substantive issues about the manner in which the Fund's assets should be distributed amongst its creditors and investors. These questions must be addressed to the BVI High Court and the US District Court in New York. I have recognised that Messrs Carter and Walker have the legal power to act on behalf of the Fund for all purposes in this jurisdiction. Unless and until the Fund becomes the subject of a winding up proceeding in this jurisdiction, it is a matter for the BVI High Court to give directions about the way in which its Official Liquidators exercise their powers.

14 Second, Counsel argues that I should refuse to grant a declaration because the Official Liquidators have entered into a protocol by which they are said to have agreed not to commence any proceedings in this jurisdiction. In my judgment there is, quite simply, no factual basis for this argument. I accept the Official Liquidators' evidence (Carter Affidavit §§24 & 25) that they have negotiated the outline terms of a protocol designed to facilitate the effective distribution of the Fund's assets, but I do not need to concern myself with the terms of this (draft) protocol for two reasons. First, the protocol will take effect only if it is approved by both the US District Court in New York and the BVI High Court. Court approval has not yet been obtained. Second, by an order made on 18 February 2010 (1st Carter Affidavit §23 and Exhibit NC1, page 76-77) the BVI High Court has specifically authorised and directed its Official Liquidators to present this petition. In the light of this evidence I cannot possibly conclude that the Official Liquidators have "agreed" not to seek recognition of their powers in this jurisdiction. Even if they had entered into any such agreement, I would still have to adjudicate the issue (in Cause Nos. FSD 83 and 84) on the application of BB&T and SocGen who are still faced with conflicting instructions from two different sources, both purporting to act for the Fund.

15 Third, Counsel for the directors asked me to adjourn the Official Liquidators' Petition or grant a stay (deferring the date upon which my declaration would take effect) pending the outcome of the Directors' appeal against the winding up order. The existence of the appeal has two potential consequences. First, because the Fund is incorporated in the BVI, I must look to BVI law to ascertain who is entitled to act on its behalf. If the BVI Court of Appeal were to grant a stay of the winding up order and that stay were to have the effect of re-instating the authority of the Directors, then application of the Cayman Islands' conflict of laws rules would lead to the conclusion that I should recognise the Directors as the persons currently entitled to act on behalf of the Fund. However, the evidence is that the Directors' application for a stay was heard and rejected by the BVI Court of Appeal on 30 March 2010. Second, I could adjourn the hearing of

the Official Liquidators' Petition pending the outcome of the appeal if I thought that it was convenient to do so on case management grounds. I considered this possibility at the case management conference held on 25 March 2010 and concluded that the matter was in fact urgent because BB&T and SocGen were faced with conflicting instructions. The matter became even more urgent a few days later when the Fund's Investment Manager issued proceedings (Cause Nos. FSD 83 and 84) against the two banks.

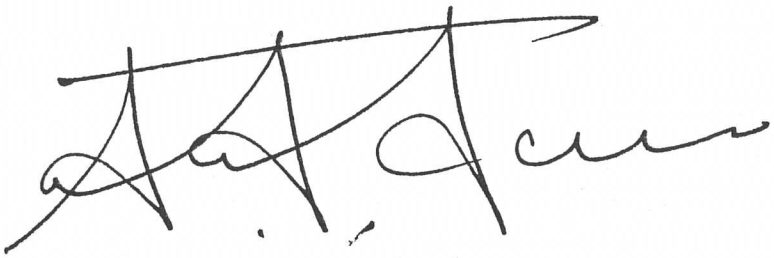
16 Fourthly, Counsel for the Directors submits that I should adjourn or stay this Petition on grounds of *forum non conveniens* and/or *lis alibi pendens.* With all due respect to Counsel, I think that this argument is also misconceived. The purpose of section 241(1)(a) is to provide foreign representatives with a convenient and expeditious method of establishing their credentials and right to act *in this jurisdiction* on behalf of or in the name of a debtor, in a way which will have universal effect against all persons in the Cayman Islands. By definition, a petition can only be presented under section 241 if there is a "foreign bankruptcy proceeding" pending before a foreign court (or possibly some governmental authority). The fact that such a proceeding is pending is a necessary pre-condition to the exercise of this Court's jurisdiction. It cannot constitute a reason for refusing a declaration. Furthermore, it is only this Court which can make declaration under section 241. The fact that the exercise of this Court's jurisdiction will necessarily involve having regard to some foreign law does not lead to the conclusion that this Court can in some way abrogate its responsibility to a foreign court.

CONCLUSIONS

17 I emphasise that this Court is merely being asked to determine whether the persons entitled to act on behalf of the Fund in this jurisdiction are (a) the Directors, either directly or indirectly in their capacity as the directors of the Investment Manager or (b) the Official Liquidators appointed by order of the BVI High Court. I am not concerned with issues about the way in the Fund's assets should be distributed. These issues will be determined in the liquidation proceedings pending before the BVI High Court and/or the interpleader proceedings pending before the US District Court in New York. To the extent that there is any jurisdictional overlap or conflict, this must be resolved by those courts, probably through the mechanism of an international protocol. It is not my function to interfere in this process in any way whatsoever. I have made a declaration recognising that the Official Liquidators are the only persons having authority to act on behalf of the Fund in this jurisdiction. How they exercise that authority is a matter for the BVI High Court.

18 Finally, I considered the question of costs. In my judgment it would serve no useful purpose to make an order for costs as between the Directors and the Official Liquidators. As regards, BB&T and SocGen, they are entitled to appear and be heard on the Petition if they wish to do so. Counsel for BB&T attended the case management conference but not the hearing itself. Counsel for SocGen appeared at both the case management conference and the substantive hearing. Affidavit evidence was also filed on its behalf. I concluded that the limited costs incurred by the banks in this proceeding should be treated as part of their "costs of doing business" and should not be passed on to the Fund's creditors and investors. For these reasons I made no order for costs.

DATED the 16th day of April 2010



The Honourable Mr Justice Andrew J. Jones QC