IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

CAUSE NO: FSD0166 OF 2019 (ASCJ)

IN THE MATTER OF THE COMPANIES LAW (2018 REVISION)

AND IN THE MATTER OF ONETRADEX LTD (IN OFFICIAL LIQUIDATION) ("OTX" or "the Company")

Before: **The Honourable Chief Justice Smellie**

Appearances: **Malenik Miller Legal Counsel for and on behalf of the Cayman Islands Monetary Authority ("the Authority").**

Christopher Harlowe and Sarah Lewis of Mourant Ozannes on 27 November 2019; Barry Issacs QC instructed by Christopher Harlowe and Sarah Lewis on 25 June 2020, for the Ad Hoc Liquidation Committee.

Graeme Halkerston instructed by Niall Hanna of Walkers for the Controllers/Joint Provisional Liquidators of OTX

Hearing Dates: **27 November 2019, 25 June 2020 and application on the papers on 1 September 2020**

Written reasons: **1 October 2020.**

REASONS FOR RULINGS

Securities Investment Business- report by its auditor of improprieties- appointment of controllers by the Monetary Authority over its affairs- controllers application for their appointment as provisional liquidators- basis for appointment of provisional liquidators- payment of liquidation costs from assets of clients held on trust –Berkeley Applegate principle- distribution of assets in satisfaction of claims while disputed claims unresolved- jurisdiction to allow – setting of liquidation reserve to meet costs and unresolved claims while allowing for return of assets- principle for setting of such a reserve- whether provisional liquidators might be allowed interim payment on costs- jurisdiction to allow interim payments.

1. OTX was incorporated in the Cayman Islands on 19 September 2012 and was granted a Securities Investment Business-Full Licence (Broker Dealer), by the Cayman Islands Monetary Authority ('the Authority"), on 4 December 2013.

2. By its Petition filed on 29 August 2019, the Authority, acting in its regulatory capacity, petitioned for the winding up of OTX and the appointment of Kenneth Krys and Angela Barkhouse of KrysGlobal (Cayman) Ltd, as the joint official liquidators. Mr Krys and Ms Barkhouse had earlier been appointed as Controllers of OTX by the Authority, ("the Controllers") in circumstances to be described below.

3. On 27 September 2019, the Authority's Petition was, with the agreement of the Authority, stayed by order of the Court in deference to an Ex Parte Summons filed on 30 August 2019 by the Controllers which sought their immediate appointment as joint provisional liquidators of OTX ("JPLs"), under section 104(3) of the Companies Law.

4. In bringing this application for what was in effect, a stay of its winding up to allow OTX the opportunity to reconcile and resolve its obligations owed primarily to investor-clients, the Controllers asserted that this, in their considered view as those then in charge of OTX, would be in the best interests of its investor-clients and creditors. They relied upon the case law as explained in ***In Re Caledonian Bank Limited (in voluntary liquidation)*** 2015 (1) CILR 143, where it was held that the effect of the appointment of controllers at the instance of the Authority over a regulated entity was that the "*controllers have effectively assumed control of the*

licensee's affairs to the exclusion of the [joint voluntary liquidators], the directors and the shareholders, and anyone else who may claim any aspect of control. [subject of course to their duty to report to the Authority]"

5. Thus, the rational for their appointment as JPLs instead of as official liquidators was, as Mr Krys explained in his second affidavit[1], on the grounds that although the Authority may be able to establish that OTX was unable to pay its debts within the meaning of section 93(c)[2] of the Companies Law (2018 Revision), OTX intended to present a compromise or arrangement to its creditors and investor-clients - persons who are more accurately described as "trust beneficiaries" because of the relationship of trust upon which their investments are held by OTX (hereinafter simply "clients").

6. As was then argued on behalf of the Controllers and accepted by the Court, in this case the Court was not required to find that OTX was then presently, within the meaning of section 93(c), unable to pay its debts because section 104(3) of the Companies Law specifically introduces the words "*likely to become*" so as to qualify the test "*unable to pay its debts*" prescribed by section 93(c). Thus, while the words of section 93(c) themselves do not, unlike their English equivalent, include "*an*

[1] Sworn and filed on 30 August 2019, at [4].

[2] The test for inability to pay debts under section 93(c) is a cash flow test although it is concerned also with debts falling due from time-to-time: see ***Skandinaviska Enskilda Bavken AB (PUBL) v Simon Conway and David Walker (Weavering Macro Fixed Income Fund Limited (in liq)*** (unreported, CICA, 18 November 2016) citing with approval at [39] ***BNY Corporate Trustee Services Ltd*** v ***Eurosail-UK*** 2007-3BL plc [2013] 1 WLR 1408.

element of futurity" (per Martin JA in ***Skandinaviska,*** above at [38]), the additional phrase in section 104(3) carries a distinct meaning in the context of section 104(3).

7. The words "*likely to become*" are derived from the UK Insolvency Act 1986 (the "1986 Act"). The meaning and purpose of the words are explained in the English case law. In ***Re Primlaks*** [1989] BCLC 734, Vinelott J, in the context of placing a company into administration for the purpose, inter alia, of allowing it to seek an arrangement with its creditors, said (at 741[f]-[g]):

> *"Paragraph (a) of section 8(1) [of the 1986 Act] sets out a condition that must be met before the court can enter into an inquiry as to whether an administration order would serve any useful purpose. The court must be satisfied that the company is or is likely to become unable to pay its debts. Clearly in this context, the test prescribed must be whether a company currently able to pay its debts as they fall due will probably be unable to pay them in the future. It would be unjust to a company's creditors to impose on them the regime of an administration order so as to improve and perhaps expand the company's business if the probability is that the company will be able to pay its debts as they fall due*".

8. I accept that for the purposes of deciding whether or not the jurisdiction vested by section 104(3) of the Companies Law should be exercised, the language of section 104(3) imposes a jurisdictional pre-condition which is similar in effect as that for the opening of an administration proceeding and, importantly, it serves much the same purpose as a substitute, in this jurisdiction, for the administration procedure, as this Court first stated in ***Re Fruit of the Loom***[3]***:***

[3]2000 CILR Note 7 and Written Judgment delivered on 26 September 2000 pp 8-9 beginning at line 20. There the Court adopted and applied the similar approach taken by the English High Court in the application of the equivalent pre-administration provisions of English Companies Act 1948: see ***Re Highfield Commodities*** [1985] 1 W.L.R. 149, at 159, per Megarry V.C.- and ***Re Esal (Commodities) Ltd*** [1985] BCLC 450 at 460 per Harman J. Several subsequent decisions of this Court applying ***Re Fruit of the Loom*** can be found in ***Re Trident Microsystems (Far East) Ltd (unreported, Cresswell J, 1 June 2012); Re CW Group Holdings Limited (unreported, Parker J, 3 August 2018) Abraaj***

> *"The discretionary power vested in the Court by section 99[which became section 104] of the Companies Law is very wide. As the orders already made recognize, the power admits of a discretion which the Court will be prepared to use to appoint provisional liquidators as the basis for the rescue of a company. This is subject to the Court being satisfied that such appointment would be for the benefit of those having the financial interests in the company to be rescued. The Court must be satisfied that the order would be for the general benefit of creditors and subject to creditors' prior interests, the benefit of shareholders.*
> *In the absence (of) jurisdiction given by specific statutory powers in the Courts for the making of administration orders over the affairs of companies, it is apt that the flexible discretionary power given in Section 99 for the appointment of provisional liquidators be used to enable the rescue of a company where it is just to do so..."*

9. Here, the pre-condition to the appointment of the JPLs and the appropriateness of their appointment was satisfied, as it appeared from the evidence that OTX was or was likely to become unable to pay its debts as they fall due and a provisional rather than outright liquidation, would best serve the interests of investor-clients and creditors.

10. As mentioned above, the order appointing the JPLs as well as further orders for the interim management of the provisional liquidation were made on 27 September 2019 and still further orders were granted upon an application of the JPLs on 27 November 2019. I come below also to explain the reasons for the making of the orders on the 27 November 2019 but before so doing, the troubling background to the Authority's Petition, to the JPLs' Ex Parte Summons and subsequent

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Holdings *(unreported McMillan J, Cause No: FSD 95 of 2018);* ***Mongolian Mining Corporation*** *(unreported McMillan J, Cause No: FSD 99 of 2016)and implicit in orders appointing Provisional Liquidators in* ***Arcapita Investment Holdings Limited*** *(FSD Cause 45 of 2012, 19 March 2012) and* ***Suntech Power Holdings Co, Ltd*** *(FSD Cause 143 of 2013, 7 November 2013)*

applications, comes from the affidavit of Audrey Roe, the Head of the Compliance Division of the Authority:

> **"*Background***
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> 1. *OTX was incorporated as an ordinary resident Cayman Islands company on 19 September 2012 (Registration No: 271824) and was issued a Securities Investment Business (full licence) to conduct the activity of Broker/Dealer by the Authority on 4 December 2013, pursuant to section 6 of the then Securities Investment Business Law (2011 Revision).*
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> 2. *The Authority's records show that OTX acts as its own registered office from the physical address of their business at 5th Floor, Anderson Square, Shedden Road, George Town, Grand Cayman. Baker Tilly (Cayman) Ltd. ("Baker Tilly" or "the auditors") are the external auditors of the Company.*
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> 3. *The Authority's records further show that on the date of OTX's incorporation Mr. Colin Ian Methven Wilson ("Mr. Wilson") and Mr. Jamal Young were appointed as directors, with Mr. Wilson also appointed to act as the Company secretary. On the date of incorporation one share was issued to MG Management Ltd. representing 100% of the issued share capital of the Company.*
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> 4. *Currently, the Company is owned by Mr. Richard Lawrence Ellison ("Mr. Ellison") 51% (510 ordinary voting shares) and Mr. Wilson 49% (490 ordinary voting shares). Mr. Ellison and Mr. Wilson are also the only directors of the Company as well as full-time employees involved and responsible for the day-to-day operations of the Company.*
>
> 5. *At the time of licensing, the Authority had been informed by OTX that it had been established to provide broker / dealer services to a range of clients. OTX's website onetradex.com, states that they are the Cayman Islands' only fully-licensed broker / dealer that offers online discount trading services to individual investors, traders, hedge fund managers and family offices. 64% of the Company's clients are resident in the Cayman Islands.*

6. *The Company was until 22 July 2019 a broker member of the Cayman Islands Stock Exchange.*

7. *The Company's primary custodian for its clients' assets is Interactive Brokers LLC. ("Interactive Brokers" or "IBKR") who are headquartered in Greenwich, Connecticut. Interactive Brokers is regulated by the U.S. Securities and Exchange Commission ("SEC"), the US Financial Industry Regulatory Authority ("FINRA"), the New York Stock Exchange ('NYSE"), US Commodity Futures Trading Commission ("CFTC") and other regulatory agencies around the world. Interactive Brokers as part of its broker dealer agency business provides direct access ('on line') trade execution and clearing services to the Company's clients.*

Triggers to the Authority's Regulatory Concerns and Regulatory Enforcement Action Failure to File Audited Financial Statements

8. *OTX had a history of failing to file audited financial statements ("AFS") as part of the Company's annual return to the Authority going back to 2015 and as a result on 30 January 2019, the Authority exercised its enforcement powers and imposed further conditions on OTX's licence pursuant to section 17(2)(ii) of the Securities Investment Business Law (2019 revision) ("SIBL"). The following further conditions were imposed on OTX's Licence:*

   (a) ONETRADEX LTD shall not undertake any new business for any new clients until further notice from the Authority; and

   (b) ONETRADEX LTD shall, within 60 days, submit its audited financial statements for the financial years 2015, 2016, 2017 and 2018.

The Decision Notice and Schedule of Imposition of Conditions ("the Notice") was served on the Company on 1 February 2019.

Onsite Inspection Findings and Regulatory Breaches of the SIBL, SIBL Regulations & Anti-Money Laundering Regulations (2018 Revision) ("AMLRs")

9. Immediately following the issuance of the Notice, the Authority conducted an on-site inspection of the Company between the 4 to 8 February 2019, (the "Inspection"). The Inspection resulted in a number of material findings.

10. The Inspection identified contraventions of the SIBL, SIBL regulations and the AMLRs, by the Company which included breaches of:

(a) sections 13(1) and 13(2) of SIBL for not submitting its audited financial statements for the financial years ended 30 June 2015, 2016, 2017 and 2018, resulting in the Authority's decision notice of 1 February 2019;

(b) section 13(2){b) of SIBL for failing to submit a Certificate of Compliance for 30 June2018;

(c) section 6(2)(b) of the SIBL for having contravened a condition of its licence for not submitting adequate Summaries of Operations on an annual basis for the years ended 30 June 2015, 2016, 2017 and 2018;

(d) regulation 8(1)(b) of the Securities Investment Business (Financial Requirements and Standards Regulation 2003) ("SIB Requirements and Standards Regulations") for failing to submit statements for 03 and 04 of2018;

(e) regulations 5(a)(ix), 12(1)(e)(i) and 12(1)(e)(ii) of the AMLRs for having deficiencies with its ongoing monitoring program including the conduct of ongoing due diligence of business relationships.

External Auditors Findings

11. On 7 March 2019 pursuant to its reporting obligations under section 19 of the SIBL, the Company's auditors issued a letter to the Authority advising of a potential breach of regulation 40 of the Securities Investment Business (Conduct of Business)

Regulations 2003 ("SIB COB Regulations."). The auditor stated that as part of their testing of the Company's financial period ending 30 June 2015, they had uncovered evidence that the Company had used a client's funds to facilitate stock loan transactions with other parties unrelated to the client whose funds were used and without the said client's knowledge or approval. The client's funds were loaned to the other parties and stocks were taken as collateral by the Company to secure the loans. The auditor further stated that the Company had advised them that the transaction in question: (i) was an oversight; (ii) had not resulted in any losses to the client and; (iii) all funds had been returned to the same client. In communications with the Authority on the 1 August 2019, the Company also subsequently advised that at the time of this stock loan transaction, "...the Licensee did not realize the use of the funds in its client account was a potential breach of Securities Investment Business Law, Securities Investment Business (Conduct of Business) Regulations 2003, Section 40 - Client Bank Accounts. Instead, the Licensees concentration was focused on the potential for loss of funds and the collateral that was being deposited..." and that, "No money was lost on this transaction however the Directors accept that this mitigates rather than cures this breach of the regulations."

12. *On 29 March 2019 the Authority was further advised by the Company that they had contacted the client whose funds had been used in the transaction outlined above in paragraph 11 and notified him of the unauthorized use of his funds.*

13. *On 26 April 2019 the Authority received the Audited Financial Statements (AFS) of OTX for the period ending 30 June 2015. Of note:*

    (a) *The audit opinion was qualified with respect to the potential breach of the SIB COB Regulations relating to the unauthorized use of client funds as outlined in paragraph 16 (sic) above.*

    (b) *The auditor's report contained the following "Emphasis of Matters"*

        i. *The Company has been subjected to a potential loss of funds (approximately GBP 57,000) arising*

from the placing of Beaufort Securities Ltd. into administration in the UK;

ii. *The Company was at risk of losing its licence issued by the Authority; contents of the Authority's Decision Notice were outlined. The auditor's report further outlined that the Company's management made representations to the auditor that in the event its licence is revoked they planned to continue operations "in other lines of business".*

(c) *The notes accompanying the AFS that were submitted to the Authority also revealed that a potential dispute existed regarding the true legal and beneficial ownership of certain stocks held by the Company on behalf of a client.*

14. *The auditors also advised the Authority that audits for the years ended 2016, 2017 and 2018 were still in progress, however the information requested from the Company was being produced very slowly as a direct result of the Company's lack of an adequate internal book-keeping and record keeping system.*

15. *The Company failed to comply with the imposition of the Further Conditions imposed by the Authority on 30 January 2019, in that it failed to file its AFS within 60 days as required; in fact only AFS for the period ending June 2015 were filed sometime after the 60 day deadline and the AFS for the years 2016, 2017 and 2018 remain outstanding at the date of this affidavit.*

Appointment of the Controllers

16. *The appointment of controllers was seen by the Authority as the most appropriate regulatory enforcement action to protect the interests of the public, OTX's clients and its creditors. As such on 12 July 2019 the Authority exercised its powers pursuant to section 17(2A)(h) of the SIBL and resolved to appoint, at the expense of OTX, persons to assume control of the Company's affairs. Pursuant to sections*

17(2),(a),(b),(c),(d) and (e) of the SIBL, the Authority was of the view that there were reasonable grounds to believe that the Company:- (i) was unable or appeared likely to become unable to meet its obligations as they fall due; (ii) was carrying on business fraudulently or otherwise in a manner detrimental to the public interest, to the interest of its clients or to the interest of its creditors; (iii) had contravened the SIBL, SIBL regulations, and the AMLRs; (iv) had failed to comply with a condition of its licence; and (v) the directors had failed to conduct the direction and management of OTX's business in a fit and proper manner.

17. *On the 18 July 2019 Mr. Kenneth Krys and Ms. Angela Barkhouse of the firm Krys Global (Cayman) were appointed by the Authority as Joint Controllers ("the Controllers") of OTX. The Controllers were granted the powers to:*

    (a) *assume control of the affairs of OTX and, to the exclusion of any operator, to administer the affairs of OTX in the best interests of the clients, and creditors of OTX;*

    (b) *assess whether any applications should be made to the Grand Court of the Cayman Islands to protect the interests of the clients and creditors of OTX;*

    (c) *prepare and furnish a report in accordance with Section 17(5) of the SIBL to the Authority regarding the affairs of OTX and of their recommendations thereon. The report was to be furnished as soon as possible, but no later than three months from the date of the Controllers' appointment.*

The First Interim Controllers' Report- 30 July 2019 ("the First Controllers' Report')

18. *On the 18 July 2019 the Controllers attended the premises of OTX, immediately took control of the affairs of OTX and began their investigations and the preparation of the First Controllers' Report.*

19. *On 30 July 2019 the Controllers filed their First Controllers'*

Report, the salient points within it are summarised below along with the main regulatory breaches uncovered by the Controllers which are also outlined in further detail below.

Breaches of SIBL and related regulations

20. *OTX was in serious breach of the SIBL and SIBL regulations. The breaches identified at the time of the First Controllers' Report were:*

    (a) Section 7(4) of SIBL for failing to advise the Authority of changes to information provided to the Authority pursuant to section 6(4) within 7 days after the change of information;

    (b) Section 13(2) of SIBL for failing to file audited accounts for the years ended 30 June 2016, 2017 and 2018 and certificates of compliance;

    (c) Regulation 4(1) of SIB COB Regulations for failing to maintain adequate professional indemnity, professional liability and business disruption insurance in an amount appropriate to the size, complexity and nature of the business;

    (d) Regulation 10 of SIB COB Regulations for using misleading statements in its advertising;

    (e) Regulation 26 of SIB COB Regulations for failing to implement proper controls for managing client monies;

    (f) Regulation 27 of SIB COB Regulations for failing to safeguard client assets;

    (g) Regulation 29 of SIB COB Regulations for failing to ensure client assets are properly segregated;

    (h) Regulations 33 and 34 of SIB COB Regulations for failing to perform reconciliations of client accounts;

    (i) Regulation 40 of SIB COB Regulations for failing to ensure that client money is held at all times in a client bank

account;

(j) Regulation 6 SIB Requirements and Standards Regulations for failing to maintain adequate accounting records and internal controls; and

(k) Regulation 7 of SIB Requirements and Standards Regulations for failing to perform reconciliations of the Company's accounts.

Unauthorised Use of Client Funds

21. OTX had engaged in various share loan transactions for which client funds were used without the client's knowledge or permission, the details of which are set out in the First Controllers' Report at 5.07 to 5.38. As a result, the Controllers have identified potential exposure to liability that OTX faces arising from the share loan transactions in the table within the First Controllers' Report at section 5.39.

Misleading information

22. The Controllers at section 4.20 and 4.21 of the First Controllers' Report have identified through a review of OTX's website and promotional material that OTX was purporting to have been in some way vetted by the FINRA and CFTC. Searches of FINRA and CFTC and other regulatory bodies within the USA were conducted by the Controllers' U.S. legal counsel ("US Counsel") and did not reveal any references of any kind that OTX, its directors or employees had been vetted by these regulatory bodies.

23. The US Counsel having also reviewed the Interactive Brokers Consolidated Account Agreement (which governs OTX's accounts with Interactive Brokers) and concluded that the Securities Investor Protection Corporation's ("SIPC") protection for a maximum coverage of US $500,000 "for each client securities account" referenced on the Company's website and promotional material was misleading. Although the introducing agreement between Interactive Brokers and OTX is not consistent with the securities industry standard "fully disclosed clearing agreement," the underlying clients of OTX are not "disclosed" to Interactive Brokers and their securities

are, for all relevant purposes, comingled with the securities of all other customers of OTX. Even to the extent that separate sub accounts may have been established for each client, the Interactive Brokers Agreement clearly provides that they are maintained for "convenience" only. For this reason, there is the possibility that the relevant SIPC protection provided is a grand total of US $500,000 and not US $500,000 for each client.

Inadequate Professional Indemnity and Liability Coverage

24. *OTX currently holds professional indemnity and professional liability insurance coverage to a limit of at least KYD $1,000,000 for any one claim and in aggregate. The Controllers observed that this is less than the minimum that is required as the Authority expects its licensees to obtain and maintain at a minimum "professional indemnity insurance of at least KYD $1,000,000 for any one claim and KYD $1,500,000 in aggregate. The Controllers have noted that this coverage appears insufficient, given the assets under management, which are reported as not less than $80 million.*

Management Accounts, Solvency and OTX's Current Financial Position

25. *The Auditors have advised the Controllers that they are not in a position to issue audited accounts for the financial years ended of June 2016, June 2017, and June 2018.*

26. *Based on information provided by OTX, the Controllers attempted to prepare a summary of the management accounts for the years ended 30 June 2016 and 2017, however a number of issues were encountered and are summarized below:*

    (a) the trial balance provided for 2015 had amounts that could not be easily reconciled to the figures appearing in the 2015 Audited Financial Statements;

    (b) the capital accounts reflected in the 2016 and 2017 management accounts did not appear to reconcile to the 2015 Audited Financial Statements; and

(c) *the amounts for capital contribution are different in all three years.*

27. *Management accounts for the period ended 30 June 2018 and 2019 have not been received.*

28. *Based on information provided by the Directors on the expected costs of operations up to 25 August 2019, the Controllers propose to set up a provision for the operating costs of $13,433.*

29. *Based on contingent liabilities stemming from the share loan transactions (referred to above), the Controllers have restated the assets and liabilities of OTX which they believe represents the financial position of OTX as at 25 July 2019 in a table at section 6.30 of the First Controllers' Report.*

30. *The total current deficit of OTX is shown as US $885,471 within section 6.30 the First Controllers' Report.*

Other Findings within the Controllers' Report

31. *The Company has not established and maintained adequate records or internal controls in relation to their clients' or their own assets or liabilities.*

32. *The Controllers' Report provided information on the demographics of OTX's 299 clients as follows:*

(a) *The clients have addresses from 51 countries;*

(b) *The largest client base is 192 clients who are resident in the Cayman Islands, the second largest client base is Belize with 12 (4%), and the third largest is Panama with 8 (3%);*

(c) *Individual or joint holders comprise 226 clients (76%), corporate clients comprise 64 and the remaining 9 are trust or LLC clients;*

(d) *There are 19 clients that hold balances with a value in excess of $1,000,000 with the largest account holder holding $16.7 million;*

(e) *66 clients have balances with values in the range of $100,000 to $1,000,000 and the remaining 214 clients have balances less than $100,000.*

The Controllers ' Recommendations

33. *Upon an interim assessment of the financial position of OTX, the Controllers have recommended that the Authority present a petition to wind up OTX, and at the same time the Controllers, in conjunction with the Authority, apply for the appointment of Joint Provisional Liquidators ("JPLs") over OTX for the following reasons:*

34. ***There is a substantial risk that OTX is or will soon become insolvent.*** *The Controllers' review of the assets and liabilities, including potential liabilities that arise from certain share loan transactions that OTX entered into and for which it used client funds without their authority, projects a net deficit of US$885,471.*

(a) ***The threat of litigation dissipating the assets of OTX.*** *The Controllers have identified a number of instances, in particular involving certain clients, where they have indicated or threatened that they are engaging legal counsel to advise them on obtaining their assets. In the circumstances, the Controllers consider that there is a real and imminent risk of a client bringing a claim against OTX whether in the Cayman Islands or in the United States to have its investments returned to it, or petitioning in either jurisdiction for the appointment of a liquidator/trustee over OTX. There is a risk that the clients could claim to be creditors of OTX with standing to wind up OTX or bring claims for return of funds, and a real risk that a claim or application may be made in either the Cayman Islands or the United States, where the Interactive Brokers are located, for their assets or for the winding up of the Company. As a result of the potential exposure to litigation, the immediate appointment of the Controllers as Joint Provisional Liquidators has also been recommended within the First Controllers' Report, in order to create a moratorium on claims at least in the Cayman Islands and better manage any litigation in the United States.*

(b) ***Sale of Assets.*** *To assist in the sale of all or part of the Company's business.*

(c) ***There is a need for further regulatory investigation of OTX.*** *The Controllers have provided their first interim report, but do require further investigation to more accurately assess the exact position of OTX.*

Steps Taken by the Authority

35. *On the advice of the Legal Division of the Authority, the Authority has demonstrated through its own findings and the subsequent findings of the Controllers (that it appointed) that there are sufficient grounds for the use of its enforcement powers to bring the Petition for the liquidation of OTX.*

36. *On 7 August 2019, the Executive Committee of the Board of Directors of the Authority, after due consideration and having passed the necessary resolutions, invoked their power under section 17(6)(d) of the SIBL to revoke the Licence and apply to the Court for the winding up of the Company. The effective date for the revocation of the Licence will be the date of the appointment of the Joint Official Liquidators of OTX ("JOLs").*

37. *The Company has been provided with ample opportunity to rectify the regulatory breaches of the SIBL, its related regulations and the AMLRs, and has been kept apprised of the Authority's intention to revoke the Licence and to bring the Petition.*

38. *In an effort to notify the management, the directors, the shareholders or any related party to OTX of the actions and intended actions to be taken by the Authority, all documents filed in support of the Petition were delivered to the Registered Office of OTX at their Company's offices and duplicate copies were sent to the Joint Controllers. An affidavit of service was filed with the court once service of the pleadings and all supporting documents had been executed upon the company and its directors.*

Nomination of Joint Official Liquidators:

39. Given their prior involvement as Controllers, Mr. Kenneth Krys and Ms. Angela Barkhouse of Krys & Associates Cayman Ltd (t/a KRYS Global), insolvency practitioners and accountants at Governors Square, Grand Cayman, Cayman Islands were nominated by the Authority to be appointed as JOLs having expressed their willingness and consent to act in offering their services as qualified insolvency practitioners, as evidenced by their affidavits, filed in accordance with the CWR.

40. Having been appointed Controllers since 18 July 2019, Mr Krys and Ms Barkhouse both have already expended considerable time and incurred costs in familiarizing themselves with and acquiring knowledge of the affairs of OTX, its custodians, bankers and clients. In addition, both nominees have been directly liaising with many of the Company's clients and have carried out extensive preliminary investigations as evidenced by their report and various updates to the Authority. Both nominees are best placed to assume control over the affairs of OTX in liquidation as further evidenced by their affidavits and are adequately equipped to offer their services as qualified insolvency practitioners in compliance with the Insolvency Practitioners Rules (IPRs) and are thus able to progress the winding-up in a timely and effective manner."

The hearing of 26 and 27 November 2019

11. Against that background from Audrey Roe's Affidavit, and having appointed the JPLs on the 27 September 2019 (with the Authority's Petition deferred by its consent), two months later, on the 27 November 2019, I heard an application brought on behalf of the JPLs. There were two main aspects to this application. The first sought directions on the filing and adjudication of claims and for the hearing of appeals against the rejection of claims. Claims were to be categorized as "Proprietary Claims" (as claims based on ownership of assets held by or on behalf

of OTX for clients) and as "Creditor Claims" (where the claim related to debts said to be owed by the Company to clients or third parties, such as trade creditors or service providers).

12. The second aspect of the JPLs' application itself involved two elements. The first was for orders allowing the JPLs to be paid their remuneration and to meet all expenses of the controllership and of the provisional liquidation, including but not limited to expenses incurred for the administration of assets (together "JPLs' expenses"), from out of the assets held by or on behalf of OTX on trust for any client ("Trust Assets") and/or creditors or otherwise within the control of the Company. The second element sought orders allowing the JPLs to release Trust Assets held on behalf of clients but in order to do so, to first set aside funds from the Trust Assets to meet JPLs' expenses or to satisfy possible unresolved claims, either Proprietary Claims or Creditor Claims. This setting aside of assets was proposed to be by way of a reserved fund ('the Reserve").

13. In order to deal fairly and effectively with the Trust Assets and any assets of OTX which may be recovered, the JPLs accepted and proposed that with the Reserve established, this would allow them not only to retain sufficient assets to meet the JPLs' expenses and unresolved claims but also to return or allow for the return of the bulk of the Trust Assets, as soon as possible, to the clients in respect of whose accounts confirmations had been received from the sub-custodian IBKR ("Confirmed Clients").

14. Recognizing that the implementation of the second aspect of the orders sought would not be straightforward but potentially controversial, the JPLs also sought liberty to apply to the Court for the determination of:

(a) the method of apportionment of any sums payable by recourse to the Trust Assets pursuant to the orders sought, as between the clients; ("**apportionment orders**").

(b) the quantum of any sums payable by recourse to the Trust Assets pursuant to the orders sought ("**quantum orders**").

15. While the first aspect of the application for directions proved to be uncontroversial, the latter aspect for orders allowing the JPLs to apply Trust Assets as proposed for meeting JPLs expenses and unresolved claims, became controversial.

16. The primary position taken in this respect by the Ad Hoc Liquidation Committee ("the Ad Hoc Committee"), was that Trust Assets could not be used in the manner proposed but could only be held strictly in trust for the respective clients and returned to them accordingly, free from any charge of JPLs' expenses or claims related to the controllership or the provisional liquidation (or even ultimately the winding up) of the Company. Their position was that Trust Assets belonged to the clients, they were not assets of OTX as the entity in controllership or liquidation and so could not be used to meet the expenses of OTX or to meet creditor claims against OTX.

17. In response, on behalf of the JPLs, it was stressed that significant indispensable work had already been done during the controllership and still needed to be done to

unravel the accounting and other record keeping systems of OTX and to enable the resolution and settlement of Proprietary Claims and Creditor Claims. This work had to be paid for and as OTX itself did not have the funds to do so, the clients for whose benefit it had to be done were obliged to provide for it. While their assets were properly to be regarded as Trust Assets, provision had to be made from them because there was no other source of funding.

18. While IBKR had given the confirmations that most of the client accounts were properly segregated and held on behalf of the respective clients, irregularities with the accounts and other records of OTX of the kind mentioned above from Audrey Roe's Affidavit as cause for the Authority's concerns, had already been confirmed by the JPLs. The JPLs had also identified irregularities in relation to certain client accounts.

19. For instance, IBKR had identified an account held on behalf of 11 clients into which funds had been commingled such that IBKR itself had no visibility as to what assets belonged to which of the 11 clients. This account, called the "**DAS account**", gave rise to the difficult issues mentioned below and discussed by Mr Krys in the excerpts from his 4th Affidavit.

20. There were also difficulties in relation to an account held with Linear Investments Limited, ("**Linear**") a third party sub-custodian with whom the management of OTX had taken positions in the name of OTX using assets from the DAS Account and assets of a certain client ("**Client X**") without, it appeared, the knowledge or consent either of the DAS Account clients or Client X. The Linear position is also,

along with the DAS Account, the subject of further discussion in Mr Kyrs' 4th Affidavit:

> ""**DAS Account"**
>
> (a) *The "DAS Account" is an account held by the Company with the sub- custodian "Interactive Brokers" **("1B")** (the **"DAS Account").** As set out in Krys 3, the DAS Account is distinguishable from the other accounts held with **1B** which appear to have maintained segregation of the Client's assets' because the DAS Accounts holds the commingled assets of around eleven Clients (the **"DAS Clients").** Due to the manner in which the DAS Account operated, **IB** had no visibility on the identities of the DAS Clients and their assets were not segregated. Similarly, although the DAS Clients were able to provide instructions to **1B** regarding the treatment of their assets (using a different type of software to the other Clients sub-custodied with **1B),** the DAS Clients were not aware that their assets were commingled. This arrangement appears to have given rise to a potentially significant amount of cross-subsidisation of gains and losses as between DAS Clients, without the knowledge of those DAS Clients…*
>
> **"Linear Account and US Trusts"**
>
> (b) *As set out in Krys 3, the Company holds an account with the sub-custodian "Linear Investments Limited" **("Linear')** in its own name. Though the account with Linear is held in the Company's name, the assets in Linear include commingled Client assets.*
>
> (c) *The JPLs have received notification from Linear of its intention to make a margin call of USD 556,762 (the **"Linear Margin Call"),** which Linear will meet via recourse to the Clients' cash as well as other of the Clients' assets (i.e. securities) that are under its custody.*
>
> (d) *The JPLs understand that, **in** connection with and for the purposes of calculating the amount subject to the Linear Margin Call, Linear proposes to use cash balances held in various currencies to settle negative cash balances in other currencies, in each case forming part of the Linear*

account. Consequently, it appears unavoidable that Clients' assets (i.e. securities) must be realised ***in*** *order to satisfy the Linear Margin Call. An anonymised spreadsheet indicating the balances across the Linear cash accounts (segregated by currency) is exhibited at* ***page 1 of Exhibit KMK-4.***

(e) *Based on the JPLs' current understanding of the assets held at Linear, this liability has the potential to significantly impact upon one individual Client* ***("Client X")*** *and the DAS Clients (as will be explained further below). The JPLs have corresponded and held conversations with Client X regarding this exposure (but not the other DAS Clients) and are in ongoing discussions with Linear and the Committee regarding the genesis of this potential exposure and the equitability of it being disproportionately borne by Client X and the DAS Clients, to whom the liabilities which gave rise to the margin call appear not to relate.*

(f) *The liability at Linear (which exposes the cash and other assets of Client X and the DAS Clients discussed above) is a result of an arrangement involving the Company, Linear, and a Client (comprised by six trust structures (the* ***"US Trusts"****) pursuant to which the US Trusts sought to profit from rights attributable to Dutch Withholding Tax Refunds* ***("DWTR").*** *As matters stand, this arrangement has contributed significantly to a net liability in the Company's name of EUR3,329,329, the majority of which appears to be attributable to the US Trusts. This liability continues to grow, and it includes the legal fees paid by the Company to date to the Dutch attorneys engaged to pursue claims against the Dutch tax authority (in respect of which the litigation is at an appeal stage)."*

21. In light of that description of the problems with the DAS Accounts and that of Client X, and in recognition of the work then already done and anticipated to be done to unravel the commingled accounts and to resolve unresolved claims (which may be made not only against OTX itself but also in the form of proprietary claims against

the assets of clients "Proprietary Claims/ Claimants"), the arguments on behalf of the JPLs for the setting of the Reserve to enable return of assets to Confirmed Clients, was based on established principle from the case law, which also explains the jurisdiction of the Court for the making of such orders.

22. In granting the orders sought, in particular for the ***Berkley Applegate*** relief[4] and for the setting of the Reserve, I then (on 27 November 2019) expressed my findings *ex tempore* and on the "in principle basis", in terms which I now revise and clarify, as follows:

"I am satisfied that on the basis of a reserve being set to meet any Proprietary Claims which may be established against any of the clients' Trust Assets held at IBKR (i.e.: the Reserve), it is appropriate that those clients should be allowed now to have access to the value of the assets held within their accounts. These are accounts for which prima facie confirmations of ownership have been provided by the clients and acknowledged by the JPLs as well as by IBKR itself as the relevant sub-custodian, and are accounts which are identified in the order made today at paragraph 1 and deemed accordingly to be "Confirmed Clients' accounts"[5]. It follows that the assets in the Confirmed Clients' accounts are strictly to be regarded as assets held on trust by OTX, not the assets of the Company itself. This carries important ramifications for the treatment of the Reserve, which are to be addressed now on the *prima facie* basis, and as discussed below.

[4] ***Berkeley Applegate (Investment Consultants) Ltd, In Re***, [1989] Ch 32.
[5] These accounts have also been referred to as "U Accounts"

The primary question for today is what should be the amount of the Reserve expressed as a percentage of the value of the assets in the Confirmed Clients' accounts and for what purpose may the Reserve be applied?

In the course of arguments today, it came to be accepted between the parties, (and notwithstanding the Ad Hoc Committee's initial objections) that the Reserve could be applied to cover the JPLs' reasonable costs and expenses of the provisional liquidation, as well as the earlier costs and expenses of the Controllership, as well as any future costs of the provisional liquidation, on the basis of the ***Berkeley Applegate*** principle, as that principle was applied recently by this court in ***Re Caledonian Securities Limited (in off. Liq.)***[6]. That, in part, will therefore be the effect of the order made today.

The Confirmed Clients and other creditors who are represented by the Ad Hoc Committee through Mr Harlowe, also accept in principle, that the Reserve could be available, on an appropriate basis to be defined, to meet the claims of clients who may have proprietary claims, but who, unlike the Confirmed Clients, have not yet had their claims admitted ("Proprietary Claimants"). This was on the basis also established in the case law, that although assets held by an investment company like OTX will be held for clients on trust, the Court's inherent jurisdiction to supervise

[6] 2016 (1) CILR 309, where it was held (following also the earlier decision of this court in ***AHAB v Saad Invs. Co. Ltd*** 2010 (1) 553) that the Court has an inherent equitable jurisdiction to order liquidators' fees and expenses to be paid from trust property held by a company in liquidation provided that such fees and expenses were reasonably incurred in returning the trust property to those beneficially entitled to it. This recognizes the principle stated by Deputy Judge Edward Nugee in ***Berkeley Applegate*** (at p.50) that *"... the court has a discretion to require as a condition of giving effect to (the) equitable interest that an allowance be made for costs incurred and for skill and labour expended in connection with the administration of the property"*

and, if appropriate, intervene in the administration of a trust, while not enabling it to vary beneficial interests in trust property, permitted the Court to give directions to trustees to distribute trust property on particular bases when the Court was satisfied it was just and expedient to do so. This jurisdiction extended to making orders permitting a trustee to distribute trust property, notwithstanding the existence of claims or potential claims from third parties to trust property or of rejected claims to a beneficial interest; and accordingly, since (as in this case) it was in the best interest of the clients and of the proper administration of the assets held in trust, a trustee (here the JPLs) could be permitted to distribute the Trust Assets in accordance with a procedure approved by the Court - a procedure which properly balanced the interests of established clients to a timely return of their money with the interests of persons with serious but unresolved claims: see ***In re Global UK Ltd (No. 3)***(Ch. D) [2013] 1 WLR 3874[7]

There is however, a remaining concern which is two-fold and which is reflected in the Confirmed Clients' concern mentioned above, that an appropriate basis is defined for resolving any outstanding proprietary or other claims. More particularly, it is whether any such claim should be satisfied against the Reserve even if it turns out to be provable, as a strict matter of tracing, as against a particular Confirmed Client's account or whether it should be met from the Reserve on the

[7] Following and applying ***In re Benjamin*** [1902] 1 Ch 723, dictum of Lord Walker of Gestingthorpe in ***Schmidt v Rosewood Trust Ltd*** [2003] 2 AC 709, at [36] and ***Finers v Miro*** [1991] 1 WLR 35, CA. ***Finers v Miro*** and ***In Re MF Global UK Ltd (No.3)*** have both been followed and applied by this Court: see ***In Re SICL (in off. Liq.)*** written ruling delivered on 1 October 2019 in FSD Cause 15 of 2010 (ASCJ) at [79] to [84].(unreported).

pro rata, pari passu basis, to the extent that it is provable generally in the liquidation of the Company as a liability, not of any particular Confirmed Client or Clients, but as a liability of the Company itself.

The latter premise would involve the Reserve being set and the liabilities of the Company being identified and resolved on the "pooling" basis, whereas the former premise would involve the Reserve being held to meet only those claims which are proven respectively as against any particular Confirmed Client's account, with all remaining balances being respectively returned to Confirmed Clients (both premises together, "the pooling issue").

On the basis that this Court will direct which of those two premises will apply for resolution of the pooling issue after claims are filed, and subject to further observations below, I am content to leave the pooling issue open now. The Confirmed Clients will however understand, that it will be for the Court to resolve the pooling issue once the claims are in and can be assessed by the JPLs and ultimately if necessary, by the Court.

As to the amount of the Reserve, I am satisfied that US$12.75m[8] is sufficient to meet all claims which can reasonably foreseeably arise and so as to avoid any risk of irremediable prejudice to a claimant[9], and while including the provision for the JPLs' expenses. This amount represents approximately 15% of the valuation at today's date of the Confirmed Clients' accounts and any other assets held by OTX

[8] By the time the order was settled calculated at US$15m based on the value then of the Trust Assets.

[9] Applying the test as developed and applied for the setting of liquidation reserves in ***In Re Sphinx Group of Companies***, 2010 (1) CILR 234.

and my decision is taken relying primarily on the following factual position presented on behalf of the JPLs by counsel at today's hearing (from paragraph 7 of the JPLs' written submissions):

> *"The JPLs have now obtained a clearer picture of the assets held by the Company for Clients, how these assets were and are held, and, crucially, the liabilities to which those assets are or may be exposed because of the mismanagement of the Company. The Company holds assets of approximately US$85m, the vast majority of which are Client monies. Crucially however, those assets are exposed to liabilities of up to approximately US$5m arising as a result of losses incurred on positions in the third party accounts into which Client assets were transferred."*

This statement is important for three main reasons. First, it acknowledges that the "vast majority" of the US$85 million are Confirmed Clients' monies, a proposition which is consistent with the *prima facie* confirmations which have been given to the Confirmed Clients in respect of their accounts held at IBKR. Second, the stated possible exposure of the assets in their accounts to liabilities being confined to the sum of approximately US$5 million for losses incurred in third party accounts into which some client assets were transferred. Thus, the exposure of the Confirmed Clients' accounts to potential liabilities can be regarded as limited to that amount if any claims can ultimately be established against their accounts on the pooling basis (plus, of course, with the JLPs' expenses to be allowed in keeping with ***Berkeley Applegate*** (above)). Third, the recognition that there is as yet no determination of the allocation of the losses of approximately US$5 million – whether they are to be allocated to a particular client's account, to a specific number of client accounts or

more generally to all clients' accounts. This will depend on the JPL's investigations as to the source of funding for the positions taken in the mismanaged [DAS or Linear] accounts and whether the losses incurred on the positions must be allocated respectively to those accounts or, in the distinct alternative, more broadly across client accounts. If the former proposition is established and so no tracing claim can be proven against specific Confirmed Clients' accounts, the owner of a particular mismanaged account in question (such the DAS Account clients or Client X) would likely have a claim only against OTX itself and/or those officers of OTX who were responsible for using that client's assets for funding the loss sustaining positions.

If the latter proposition is established so that the losses must be allocated more broadly against client accounts, then there may be a case for the pooling of the Reserves (i.e.: net of the JPL's expenses reasonably incurred) to meet the client's claim on the *pro rata pari passu* basis, with any of the Reserves remaining to be returned to the Confirmed Clients on the same basis."

The application by the PL[10] for orders entitling him to payment of Costs on the interim basis, taken on 25 June 2020.

23. By his summons dated 13 May 2020 (the PL's summons), the PL applied for orders that:

> "*1. The PL be entitled to draw from Client's assets ("Trust Assets"), by way of interim payment on account the sum of US$913,414.19 (the "Interim Payment"), representing 80% of the Costs (as defined in the Order of 27 November 2019 and in Mr Krys' 5th Affidavit filed in*

[10] By this time Ms Barkhouse having resigned on 22 April 2020, Mr Krys continued and applied as the sole provisional liquidator.

support of this summons) [11] *incurred between 4 September 2019 and 30 November 2019.*

2. *The Interim Payment shall be allocated between all Clients in an amount proportionate to the value (in cash) of each Client's total Trust Assets.*

3. *The PL will repay and/or reallocate amounts drawn from the Trust Assets in respect of the Interim Payment if necessary, following the determination of the Quantum Apportionment Application (as defined above at [14] and further explained in Krys 5 and as incorporated as part of the Order of 27 November explained above).*

4. *The PL's costs of and occasioned in connection with the summons be paid out of the available assets of the Company on an indemnity basis as an expense of the provisional liquidation (without prejudice to the PL's entitlement to* ***Berkeley Applegate*** *relief in respect of all Costs (as defined in the Order of 27 November and in Krys 5)."*

24. Notwithstanding the approval in principle on the ***Berkeley Applegate*** basis, for the PLs' Expenses to be paid from the Reserve, the Ad Hoc Committee objected to the grant of the PL's summons. Their objections were stated on two bases: (i) that the Court lacked jurisdiction to grant an interim payment and (ii) even if the Court had jurisdiction, as such an order would be discretionary, it should not in the attendant circumstances grant the relief sought.

25. The Ad Hoc Committee's arguments were as follows (as taken from their written submissions):

"*<u>Jurisdiction</u>*

41. The only provisions which enable the court to make orders for interim payments or payments on account are Order 29 rules

[11] Stated as *"all fees, expenses, costs, disbursements and liabilities incurred by the JPLs (and formerly, in their capacities as Controllers…) … in connection with the performance of their duties (including, but not limited to, the administration of the Trust Assets)"*

*10 and 11 of the Grand Court Rules, and Regulation 10(2) of the Insolvency Practitioners' Regulations 2018 ("**IPR**"). The court has no inherent jurisdiction to make such an order.*[12]*

Walkers' letter to Mourant dated 7 May 2020, which asked whether the Committee would be willing to approve the making of an interim payment, stated that:

> *"In the usual course of a liquidation, it is customary for a liquidator to receive a payment on account in an amount not exceeding 80% of the remuneration sought (see regulation 10(2) of the [IPR]."*

42. *Contrary to the implication in this letter, the IPR do not apply in the present case.*

43. *Regulation 2(3) of the IPR provides (so far as relevant) as follows:*

> *"Part III of these Regulations shall apply to every application made to the Court by an official liquidator ... for an order approving payment of his remuneration out of the assets of a company in provisional or compulsory liquidation ..."*

44. *Part III of the IPR includes Regulation 10(2), which provides:*

> *"An official liquidator may receive a payment on account, the amount of which shall not exceed eighty percent of the remuneration sought in the report and accounts prepared in accordance with Regulation 12(2)."*

45. *It follows from Regulation 2(3) that Regulation 10(2) only applies to an application by an official liquidator for a payment on account if the order sought approves:*

> *"payment of his remuneration out of the assets of a company in provisional or compulsory liquidation ..."*

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[12] Cf ***Moore v Assignment Courier Ltd*** [1977] 1 WLR 638 (section 20 of the (UK) Administration of Justice Act 1969, referred to in ***Moore*** at pages 643 and 645, is analogous to section20(1) of the Grand Court Law allowing for rules of court for interim payments on claims for damages, debt or other sum); ***Algosaibi v Saad Investments Co Ltd*** [2013(2) CILR 344- where it was held that this Court, in party and party litigation did not have jurisdiction to award an interim payment of costs].

46. *The May Summons seeks an order that the JPLs are entitled to payment out of the assets of the Clients. It does not seek an order that the JPLs are entitled to payment out of the assets of the Company.*

47. *The May Summons is therefore outwith the IPR, and the Court has no jurisdiction to make the order sought.*

48. *Further or alternatively, the IPR are (as Regulation 2(3) makes clear) concerned solely with the remuneration of the official liquidator. The Costs which are the subject of the May Summons fall outwith the IPR.*

49. *As stated above, paragraph 6 of the Order provided (so far as relevant) as follows*:

> *"The JPLs be entitled to be paid by way of remuneration and to meet all fees, expenses, costs, disbursements and liabilities incurred by the JPLs (and formerly, in their capacities as Controllers...) ... in connection with the performance of their duties (including, but not limited to, the administration of the Trust Assets..."*

50. *Costs are defined in the May Summons by reference to paragraph 88 of Krys 5, which states that:*

> *"The Order defines Costs as 'all fees, expenses, costs, disbursements and liabilities incurred by the JPLs (and formerly, in their capacities as Controllers...) ... in connection with the performance of their duties (including, but not limited to, the administration of the Trust Assets...' (the "**Costs**").*"

51. *The JPLs seek to draw by way of Interim Payment a sum representing 80% of Costs. In other words, the amount sought to be drawn by way of Interim Payment relates to Costs. Most of the Interim Payment sought relates to legal expenses.*[3]

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[3] See paragraph 90 of Krys 5. Of the sum of US$913,414.19 sought by way of interim payment, US$647,605.51 represents legal fees (of which 80% or US$518,084.29 is sought by way of interim payments).

52. *Costs (whether fees, expenses, costs, disbursements or liabilities) fall outside the IPR and the court has no jurisdiction to make the order sought in the May Summons for this reason also.*

Discretion

53. *If, contrary to the submission made above, the Court has jurisdiction to make the order sought in the May Summons, the Committee submits that the court should refuse to make the order in the exercise of its discretion.*

54. *The making of an interim payment is exceptional, because it is a general principle that a person has a right not to be held liable until their liability has been established by a final judgment (cf* ***Smuts*** *v* ***Pearson*** *[2010] EWHC 814 (QB) at [97], [99]). The Court should not depart from the general principle in the present case, for the reasons set out below.*

55. *The April Summons was issued on 28 April 2020 and is supported by Krys 5, which was sworn on 29 April 2020. Krys 5 is 70 pages (196 paragraphs) in length and has 340 pages of exhibits.*

56. *Since Krys 5 was served on the Committee, the JPLs have produced a substantial further amount of documentation relevant to the April Summons and the May Summons. In particular, the JPLs provided the Committee with a spreadsheet of more than 6,000 cost line items on 20 May 2020; in addition, numerous invoices in relation to legal fees were provided as recently as Friday 20 June 2020.*

57. *The Committee's principal response to the April Summons is likely to be that the sums claimed pursuant to paragraph 6 of the Order are neither fair nor reasonable in all the circumstances, having regard to (i) the amount of time worked; (ii) the complexity of the case; (iii) any exceptional responsibilities required; (iv) the effectiveness of the JPLs' operation; and (v) the value and nature of the value of the custody assets relative to the expense of the work undertaken. Thus a central issue for determination in relation to the April Summons will be the proportionality of the work done to the results achieved (cf* ***Re Caledonian Securities Ltd (in Official***

***Liquidation**) (above), Smellie CJ at paragraphs 78-81).*

58. *The Committee is in the process of undertaking the substantial task of responding to the voluminous evidence and further documentation provided by the JPLs in relation to the April Summons. The fact that the hearing of the April Summons is listed for two days gives an indication of the scale and complexity of this task and the likely dispute.*

59. *There is further work to be done before the Committee will be in a position to serve its evidence in answer to the April Summons. The parties have agreed a procedural timetable, pursuant to which the Committee will file and serve its evidence in answer by 4 August 2020. The hearing of the April Summons has been* fixed for 21 and 22 September 2020.

60. *A substantial part of the hearing of the April Summons will address the JPLs' costs incurred from 4 September to 30 November 2019, which is the subject matter of the May Summons. It follows that the May Summons has sought to put the Committee in the invidious position in which, in order to be able fully to respond thereto, it would have to file evidence addressing matters which will be the subject of the hearing of the April Summons.*

61. *This is unfair to the Committee, because the Committee was and is not in a position to file this evidence, and because it would force the Committee to reveal its position in relation to the May Summons before it has had a proper opportunity to finalise that position. This is evident from the fact that the parties have agreed that the Committee will serve its evidence in answer by 4 August 2020. In these circumstances, it would be unfair to order an interim payment.*

62. *The JPLs delayed for several months before issuing the May Summons for an interim payment in relation to Costs incurred between 4 September and 30 November 2019. However, the April Summons will be heard in September. This also militates against the making of the order sought at this late stage.*

63. *For the reasons given above, the Court is respectfully invited to dismiss the May Summons".*

26. The sheer technicality of the Ad Hoc Committee's objection on jurisdictional grounds to the orders allowing interim payment of the PL's costs is readily apparent. I was not persuaded by it.

27. My first reason is that by paragraph 7 of the 27 November Order, the PL is permitted to apply for approval of such Costs as those the subject of this summons on a "*final or interim basis*". The grant of this right to apply for interim costs was not opposed by the Ad Hoc Committee at the 27 November hearing. Such a right is an established one, even in more contentious cases involving ***Berkeley Applegate*** principles derived, not from the statutory rule-based jurisdiction of the Court, but from the equitable principles recognized and applied in that and the subsequent cases which follow it.

28. For example, in ***Finers v Miro*** (above), the English Court of Appeal, in exercise of its equitable jurisdiction, allowed payment out of a disputed fund held by liquidators and which was potentially impressed with a constructive trust for the benefit of the plaintiffs, to enable the defendant, who had a competing legal claim to the funds, to engage legal representation. That was therefore, in the context of liquidation proceedings and without recourse to the Insolvency Rules, the discretionary grant of access to funds on the interim basis notwithstanding the competing proprietary (equitable and legal) claims to them.

29. In ***Katz and Alexander (as joint liquidators of MK Airlines Limited) v Bradney, Duncan, Oldham (as former Administrators of MK Airlines Limited) and others*** [2012] EWHC 1018 (Ch), the Chancellor of the High Court had to decide whether

the plaintiffs, as liquidators, should be allowed an interim payment (ie: "on account") of fees and costs in part out of pooled assets where the Insolvency Rules did not allow it but instead on the basis of the ***Berkeley Applegate*** principles.

30. In granting the application, the Chancellor (at [47]-[48]) noted the opposing arguments of the Respondents questioning why the Plaintiff/Liquidators in that case, should enjoy the "super-super-priority" that an interim payment would involve, as being "*formidable*" but noted that "*against that, I have to recognize that the Liquidators cannot be made to work for nothing. The delay and extra expense involved in removing these liquidators [(which, as it happens, is also proposed here by the Committee in seeking to take the provisional liquidation to official liquidation and winding up)] and appointing the Official Receiver is likely to involve substantial delay and extra expense to all creditors. Authorising some payment so as to ensure the prompt completion of the liquidation appears to me to be the lesser of two evils*".

31. I was guided by similar considerations when assessing the PL's application here. In the exercise of discretion to grant the PL's application (having been satisfied that the jurisdiction exists) I was persuaded especially by the following averments from Mr Krys' 5th Affidavit and from the written submissions presented on his behalf:

> 5. *The JPLs understand that Clients may be unhappy with allocations of Costs in a collapse such as this when, through no fault of their own, they find themselves facing the diminution of the value of their investments with the Company however the Application will be determined. This affidavit explains the work that was done and how it was for the benefit of Clients. The steps the JPLs (and in their capacity as former Controllers) have taken since their appointment have provided benefits to Clients and the Trust Assets that simply would not*

have been possible if the JPLs had declined to assume responsibility for the safeguarding and return of Trust Assets and left each Client to resolve their own positions instead.

The collective process of the JPLs' involvement had efficiencies for the Client body as a whole. Given the extent of the mismanagement of the Company and the failure to keep basic records[3]*, had the JPLs not sought to reconcile the assets held by and for the Company, and resolve any competing claims made by Clients to Trust Assets, ii is difficult to conceive exactly how Clients would have recovered / dealt with their Trust Assets, without individually appointing receivers over their Trust Assets - though given the commingling that has occurred, the JPLs think that would have been fraught with complications and result in higher costs overall. Also, the extent to which Trust Assets were in jeopardy would not ever have become known until such time as some party was appointed to intervene in the manner the Controllers did. In the circumstances, that party was us and we have taken all reasonable steps since appointment to try to ensure that the work which has been undertaken has been reasonable, proportionate, and commensurate with the duties bestowed upon us by this Honourable Court.*

6. *Moreover, by way of example, with regards to the Client Accounts held with 1B (including the DAS Account) (and the related Trust Assets), all such 1B Client Accounts (including the DAS Account) were opened in the name of the Company (i.e. so far as IB was aware the Company was the 'client'). As such the involvement of the JPLs (and formerly the Controllers) was a necessary (and inevitable) consequence, without which* ***1B*** *Clients would not have the requisite power or authority to engage with 1B and/or to instruct* ***1B*** *to effect the transfer of Trust Assets held in the relevant Client's 1B Account. It is, I respectfully submit, appropriate for the JPLs (and the Controllers) to recover the Costs incurred in connection with dealing with such matters from the Trust Assets of Clients (in accordance with the principles more fully outlined below).*

32. While the Ad HoC Committee was unable to challenge the correctness of those averments, it was difficult to understand the basis upon which it could be just to deny the PL a reasonable amount of interim payment on his Costs.

33. The point was driven home by the written submissions (at[18]) on behalf of the PL referencing, by analogy, the quantum of interim payments allowed by application of the Insolvency Practitioners Regulations in liquidation proceedings from the assets of companies:

> *"It is submitted that the appropriate Interim Costs order is at the 80% level sought by the PL:*
>
> (a) *The application is sought at 80% of the Costs incurred in the Interim Costs Period. This is by analogy with the customary applications made in the jurisdiction pursuant to Regulation 10(2) of the Insolvency Practitioners' Regulations, 2018.*
>
> (b) *The PL has set out in detail the work that was done during the Interim Costs Period and confirmed it is his opinion that the sums claimed fall within the Costs as defined in the November Order.*
>
> (c) *The Ad Hoc Committee has not identified any specific basis to criticise the Interim Costs or the amount of Costs incurred in the Interim Costs Period. The Ad Hoc Committee has had the evidence identifying the basis for these costs since 29 April 2020. No evidence has been filed in opposition to this application by the Ad Hoc Committee. The Ad Hoc Committee's criticisms of the work of the PL have focused on the Costs incurred in connection with arranging the return of Trust Assets held in IB accounts, but no interim payment is sought today in respect of those Costs.*

(d) *The application is made on the basis that the PL would repay, or reallocate, any amounts paid by way of interim payment if, at the hearing of the Final Quantum and Apportionment Application on 21-22 September 2020, the quantum and/or apportionment method is ultimately approved in a lower quantum, or apportioned in a different manner, than that which is proposed by the PL under the Final Quantum and Apportionment Application (which is the same basis proposed in respect of the Interim Costs).*

(e) *There is no realistic prospect of the PL being required to engage the undertaking to repay the Interim Costs., because the Interim Costs represent 37% of the Costs incurred up to 31 March 2020 and 19% of the total Costs expected to the end of the liquidation process. Notwithstanding, the PL has agreed to the Ad Hoc Committee's request that such an undertaking be given.*

(f) *The Interim Costs represent approximately 1% of the assets held by the Company at the time of the Controllership.*

(g) *The Interim Costs represent work done by the PL and his advisers for which final payment will not be confirmed until after the Final Quantum and Apportionment Application in late September 2020. This would mean being out of funds for over a year for work done for the benefit of stakeholders of the Company".*

34. I was satisfied that it was within the equitable discretionary jurisdiction of the Court to do so and that it was just to grant the orders sought by the PL's (or May) Summons and granted those orders accordingly.

The application taken and granted "on the papers" on 1 September 2020.

35. On 1 September 2020, I considered the PL's application by summons dated 19 June 2020 for orders which, in effect, directed the PL to reduce the amount of the Reserve from 15% of the value of Confirmed Clients Accounts to 6.9% of that value. This application was obviously for the benefit of those clients, was unopposed by the Ad Hoc Committee and as such was amenable to being taken administratively "on the papers" as it was, and granted.

36. The Confirmed Clients having been entitled on the basis of the Reserve to early transfer of their accounts, they were described as "Early Transferors" in Mr Krys' 6th Affidavit filed in support of this application and in which he explained the rationale for the reduction of the Reserve in the following terms which I accepted:

"Early Transferor Reserve Reduction Application

1. *The purpose of the Early Transferor Reserve was to enable qualifying Clients (being – as described in the Order - certain Clients whose Trust Assets were custodied or 6 held in U-Accounts with IB) early access to their Trust Assets notwithstanding that certain matters relating to the liquidation of the Company, and thereby their Trust Assets, remained unresolved (for example, the adjudication of Proprietary Claims (if any) asserted by Clients resulting in claims against Trust Assets already transferred by as part of the Early Transfer Regime).*

2. *It was set out in the Order, and understood by Early Transferors, that if they elected to instruct the JPLs to effect the early return of their Trust Assets, an amount equal to 15% of the cash value of their Trust Assets (calculated as at the date they provided notice to the JPLs instructing them to execute the transfer) would be retained in their Client Account in order to meet certain potential other liabilities which may have arisen in the liquidation of the Company (including any Proprietary Claims asserted against the Early Transferors' Trust Assets).*

3. *The liquidation of the Company is now substantially more advanced. In particular, in respect of the Proprietary Claims:*

(a) *the deadline for Clients to submit Proprietary Claims (being 30 March 2020)*[1] *has passed, with thirteen Clients having submitted Proprietary Claims;*

(b) *upon adjudication of the Proprietary Claims, I have determined it possible and/or necessary to*[2]*:*

(i) *admit a number of Proprietary Claims*[3] *in respect of the securities element described in them, where I possess the securities and the records of the Company indicate they are held for the Client;*

(ii) *reject a number of Proprietary Claims in respect of the securities element described in them, where I do not possess the securities;*

(iii) *reject a number of Proprietary Claims in respect of the cash element described in them, in the absence of the successful articulation of any tracing claims by the relevant claimants; and*

(iv) *defer the full determination of one Client's Proprietary Claim where it appears that there are grounds for competing claims to the same Trust Assets. I have notified the affected parties that some or all of their Proprietary Claim is a competing claim and have offered mutual disclosure of each other's contact details in order to facilitate the potential for discussion and mutual resolution. This process is ongoing, and there may well be further developments*

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[1] As noted in paragraph 193 of Krys 5, pursuant to the terms of the Order, Clients were required to submit Proprietary Claims within 56 days of receipt of the Order (unless otherwise agreed by the JPLs), see paragraph 1 of the Order (being 16 March 2020). Following a number of requests and in view of the difficulties presented by the COVID-19 crisis, the JPLs extended the deadline for submission of Proprietary Claims to 30 March 2020.

[2] In each case, I have written to the affected Proprietary Claimants (or in some cases, their counsel) to give notice of my decision and of their further rights under the MF Global Process.

[3] Subject to receipt of a Proprietary Claim from another Client.

which may necessitate my involvement, or which the affected Clients may wish to pursue of their volition and in a manner of their own choosing. Should it become necessary, I propose to apprise this Honourable Court of any material developments and, potentially, seek further directions in due course; and

(c) *the Proprietary Claim referenced above at* ***paragraph 3(b)*** *has been asserted against Trust Assets held in the DAS Account*[4]*. Accordingly, it is now possible to say that there are no admitted Proprietary Claims over Early Transferors' Trust Assets. As such, it is no longer necessary for that element of Early Transfer Reserve, which was held to provide for such Proprietary Claims, to be retained*".

37. In his 6th Affidavit, Mr Krys then continued to explain the basis of the amount to be kept in the Reserve in order to fund the steps already taken and remaining steps to be taken, opining that US$4,959,628 (or 6.09% of Early Transferors' Assets) represented that sum. This allowed him to propose that 8.91% of Early Transferors' Assets be returned to them less the applicable direct costs incurred in respect of each Early Transferor in accordance with their directives.

38. It became necessary however, to establish a separate reserve to meet the claims of Later Transferors and this was also addressed by Mr Krys (as set out at [39] – [53] of his 6th Affidavit. At [47]- [53] and at [54]- [55] he addressed, respectively, the costs likely to be attendant upon the resolution of DAS Account Later Transferors (some DAS Account holders having had their assets returned) and Client X's proprietary claim, making provision for those as well.

39. Provisions were also to be made for an escrow account to hold the assets of unresponsive clients, less the costs attached with those accounts. With these factors in mind, as well as Mr Krys' further assessment that the entire liquidation process, including the resolution of all claims, could be completed by year end 2020, I granted the orders for the release of 8.91% of the Early Transferors' Assets and the commensurate reduction of the Reserve. Such an order was after all, a primary reason for the creation of the Reserve.

40. Having determined that the losses sustained in the DAS Account were to be allocated only as between the DAS Account clients, directions were also sought for the resolution of those claims within the DAS Accounts (as distinct from more widely as against Trust Assets). The only Proprietary Claim asserted currently was against assets held in the DAS Account and so Mr Krys avers here that there are no admitted Proprietary Claims over Confirmed Clients (ie: Early Transferors') Trust Assets.

41. Having granted the orders for the reduction of the Reserve and the commensurate return of Trust Assets to Confirmed Clients, the following issues and directions for dealing with DAS Account Clients and Client X remained to be resolved before OTX could be placed into official liquidation and finally dissolved (as taken for the Krys '6th Affidavit at [21]:

> *(i) any further application necessary to make further distributions of the residue of any Early Transferor's or Later Transferor's Trust Assets at the close-out of OTX, following determination and satisfaction of the final*

Direct Costs and Indirect Costs attributed to such Early Transferor or Later Transferor;

(ii) *the determination and effectuation of the appropriate treatment of Trust Assets belonging to the Lower Later Value Transferors and Unresponsive Clients;*

(iii) *the determination of the appropriate allocation of the DAS Account Loss between DAS Account clients;*

(iv) *any litigation proceedings arising out of the adjudication of the Client's Proprietary Claim which has been rejected, as outlined above.*

(v) *The determination of certain applications which are already pending before the Court including:*

(a) *the Apportionment and Quantum Applications (see [12] above, now to be confined to the PL's Costs or Expenses;*

(b) *the Authority's Winding Up Petition in respect of the Company;*

(c) *any application by the Ad Hoc Committee seeking an order that it too is entitled to* ***Berkeley Applegate*** *relief, as has been suggested by it in correspondence.*

GRAND COURT FINANCIAL SERVICES DIVISION CAYMAN ISLANDS

Hon. Anthony Smellie
Chief Justice

1 October 2020.