THE EASTERN CARIBBEAN SUPREME COURT
TERRITORY OF THE VIRGIN ISLANDS

IN THE HIGH COURT OF JUSTICE

CLAIM NO. BVIHCV 2008/97

BETWEEN:

SOMERS DUBLIN LTD. A/C KBCS AND OTHERS

Applicants

And

MONARCH POINTE FUND LIMITED

Respondent

Appearances: Mr Barry Isaacs QC and Mr Oliver Clifton for the Liquidator
Mr Mark Phillips QC and Ms Claire Robey for the redeemed members

JUDGMENT

[2012: 16 November]

(Unpaid redeeming members of fund in liquidation claiming that their claims to redemption proceeds have priority to claims of continuing members – **Westford Special Situations Fund Ltd v Barfield Nominees** considered – sections 207 and 197, Insolvency Act, 2003 considered)

[1] **Bannister J [ag]:** Monarch Pointe Fund Limited ('the Company') was incorporated in the Virgin Islands on 29 December 2003. It carried on business as a mutual fund and operated under a Memorandum and Articles of Association in a form commonly adopted (broadly speaking) by institutions of this type. In particular, its Articles of Association provided for members to be able to redeem their shares in accordance with a set of regulations of the type which are frequently encountered in cases of this sort.

[2] On 17 August 2007 the Company suspended redemptions and some time in 2008 the High Court appointed a liquidator. The current Liquidator is Mr Stuart Mackellar. Although unsworn, material before the Court shows that when

redemptions were suspended seven redeemed members had yet to receive some $18 million between them of redemption proceeds to which they were entitled. Those amounts remained outstanding when the Company went into liquidation. Two of these redeeming members retained some of their shares and were thus and to that extent continuing members of the Company when it went into liquidation. The subscription price represented by their retained shares, together with the subscription price represented by the retained shares of the other eleven continuing members, is some $47 million in total. The total nominal value of unpaid redemption proceeds and retained capital subscriptions together is thus somewhere in the region of $65 million. After payment of all the Company's external creditors the Liquidator has available to satisfy these liabilities some $3.5 million. If he distributes this fund *pari passu*, without distinguishing between continuing and redeemed members, each will receive about five cents in the dollar. If he pays the redeemed members in priority to the continuing members, the redeemed members will receive about twenty cents in the dollar and the continuing members nothing. If he pays the fund to the continuing members without distributing anything to the redeemed members, each continuing member will receive, by reference to their initial subscriptions, just over seven cents in the dollar.

[3] In May 2012 the Liquidator sought directions, *ex parte*, that he be permitted to make an interim distribution of the fund to the redeemed members in priority to any rights of the continuing members. I refused to make such a direction and instead directed that the distribution be made rateably between the redeemed members (for the outstanding balance of their redemption proceeds) and the continuing members (for the subscription price paid for their shares). At the same time I directed that notice be given to all redeemed and continuing members and that any redeemed or continuing member wishing to apply to vary the direction should make an application to do so within 56 days of entry of the order. Four redeemed members did make such an application. I made a further direction on 30 July 2012 that any continuing member wishing to be represented on that application must give notice of its intention to do so by 14 September 2012 and that in default the Liquidator would represent the interests of the continuing members on the substantive hearing. That hearing took place on 6 November 2012, when the four redeeming members were represented by Mr Mark Phillips QC, who appeared together with Ms Claire Robey, and the continuing members' interests were looked after by Mr Barry Isaacs QC, who appeared together with Mr Oliver Clifton on behalf of the Liquidator.

The parties' submissions

[4] By agreement, Mr Isaacs QC went first. His primary contention was that the fund should be distributed to the continuing members in proportion to the number of shares retained by each of them when the company went into liquidation, to the exclusion of the redeemed members. Alternatively, he submitted that the fund should be distributed between the redeemed and the continuing members rateably in proportion to the number of shares held by each at the commencement of the winding up.

[5] Mr Isaacs QC, relying on section 197 of the Insolvency Act, 2003 ('section 197' 'IA, 2003') and **Westford Special Situations Fund Ltd v Barfield Nominees Ltd**[1], says that the claims of the redeeming members are not admissible as claims in the liquidation of the Company. The claims of the continuing members are self evidently not admissible as liquidation claims, either, and are covered by section 34(1) (c) of the Business Companies Act, 2004 ('BCA, 2004'), which provides that (subject to anything to the contrary in the company's memorandum) a share in a company confers on its holder the right to an equal share in the distribution of the surplus assets of a company. It follows, he submits, that neither the redeemed nor the continuing members have claims in the Company's liquidation.

[6] Mr Isaacs QC justifies this submission by reference to section 207 of IA, 2003 ('section 207'), which provides as follows:

> 207. (1) Unless and to the extent that this Act or any other enactment provides otherwise, the assets of a company in liquidation shall be applied
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> (a) in paying, in priority to all other claims, the costs and expenses properly incurred in the liquidation in accordance with the prescribed priority;
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> (b) after payment of the costs and expenses of the liquidation, in paying the preferential claims admitted by the liquidator in accordance with the provisions for the payment of preferential claims prescribed;
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> (c) after payment of the preferential claims, in paying all other claims admitted by the liquidator; and
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> (d) after paying all admitted claims, in paying any interest payable under section 215

[1] HCVAP 2010/014, 28 March 2011 (CA)

> (2) Subject to section 151, the claims referred to in subsection (1) (c) rank equally between themselves if the assets of the company are insufficient to meet the claims in full, they shall be paid rateably.
>
> (3) Any surplus assets remaining after payment of the costs, expenses and claims referred to in subsection (1) shall be distributed to the members in accordance with their rights and interests in the company.
>
> (4) For the purposes of this Act, assets held by a company in liquidation on trust for another person are not assets of the company.

[7] Mr. Isaacs QC submits that section 207 provides a complete code of priorities for the distribution of the assets of a company in its winding up; that, after payment of such preferential and non-preferential claims as the liquidator admits, any surplus assets must be distributed in accordance with section 207(3); and that the surplus so identified is distributable between the members in accordance with their rights and interests in the company. The redeemed members became past members when they exchanged their shares for the right to receive the redemption price upon the relevant Redemption Day with reference to which the redemption was sought. The redeemed members are therefore no longer members of the Company and are thus excluded from any participation in any distribution of surplus assets under section 207(3), which makes no mention of past members. IA, 2003 knows exactly when to distinguish between members and past members[2] so that the drafting of 207(3) so as to omit any mention of past members cannot have been accidental and must have been deliberate. It follows, Mr. Isaacs QC submits, that the claims of the redeemed members to the unpaid balances of their redemption proceeds fall outside section 207 altogether.

[8] Mr. Isaacs QC further submits that the redeemed members cannot show that they are entitled to any rights or interests *in* the Company [emphasis added]. They are instead creditors *of* the Company and section 197 shows, he submits, that they are creditors without claims in the liquidation. They therefore fall between two stools and must be sent away empty handed.

[9] Elegant as these submissions are, I cannot accept them. The scheme of distribution provided for by section 207 is expressed by its opening words to have effect only unless and to the extent that IA, 2003 or any other enactment otherwise

[2] Mr Isaacs points by way of example to sections 197, 200-202, 204-205 and paragraphs 9 and 10 of Schedule 2

provides. In my judgment, section 197 does provide otherwise. It is in the following terms:

> 197 A member, and a past member, of a company may not claim in the liquidation of the company for a sum due to him in his character as a member, whether by way of dividend, profits, redemption proceeds or otherwise, but such sum is to be taken into account for the purposes of the final adjustment of the rights of members and, if appropriate, past members between themselves.

[10] This language makes clear that the sum due to a redeemed (i.e. past) member is to be taken into account for the purposes of the final adjustment[3] of the rights of members and, if appropriate, past members between themselves. In my judgment this means that section 207(3) must be read as covering past members with sums due to them in their character as members. Section 197 clearly envisages such past members as having an interest in the surplus available to members after payment of all admissible liquidation claims.

[11] Mr. Isaacs QC says that this is not so. The adjustment, he submits, is an adjustment between the company and the past member to take account of any sums due *from* the past member to the company which would fall to be set off against an entitlement due from the company to him in his character as a member. The difficulty, it seems to me, with this submission is that that section 197 refers in terms not to an adjustment between past members and the company in question, but to an adjustment of the rights of members and, if appropriate, past members *between themselves*.

[12] If this reasoning is wrong, then I would be prepared to construe the word 'member', where it occurs in section 207(3), as including past members and the sub-section as treating their claims as rights and interests in the surplus - that is to say, in the company, or at any rate in what is left of the company. The alternative is to extinguish their perfectly legitimate claims[4] altogether, which seems to me to be so at odds with the general principles of insolvency law as to compel some alternative conclusion.

[13] While I accept Mr. Isaacs' broad analysis of section 207 as laying down a statutory waterfall of priorities, I therefore reject his ultimate conclusion, that past members

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[3] if any such adjustment is necessary at all: **In re Compania de Electricidad de la Provincia de Buenos Aires Ltd [1980] 1 Ch 146, 173G.** For example, there will be no need for any adjustment if the surplus is sufficient to repay all outstanding subscribed capital as well as any other sums which might be due to members in their character as such

[4] except insofar as they could be used in Mr Isaacs' set off situation

who are owed sums by a company when it goes into liquidation are excluded from all participation in such assets as may be available after satisfaction of the claims of external creditors.

[14] Mr. Phillips QC, for the redeemed members, founds himself first upon certain passages in the lead judgment of the Hon Mde Janice George Creque JA (as she then was) in **Westford Special Situations Fund Ltd v Barfield Nominees Ltd**.[5] First, he points to paragraph [21] of the judgment, in which the learned Justice of Appeal characterized a person with money due to him from the company as a past or present member of it as a creditor of the company but one unable to claim in a liquidation *'in the same way as an ordinary third party creditor.'* He relies, further, on a statement in paragraph [23] where the learned Justice of Appeal said that the effect of section 197, like its counterpart in the UK Insolvency Act 1986,[6] *'was to subordinate the claims of the members (past or present) acting in that character, to the claims of any outside creditor.'* The meaning, says Mr. Phillips QC, is that a past or present member with money owing to him from the company in his character as member may claim in full after the external creditors have been paid and in priority to continuing members without 'members' debts' due to them from the company – in other words, in priority to members who are entitled to a return of their capital and nothing more.

[15] Mr. Philips QC also relies upon a passage from the decision of the Court of Appeal in **Kenneth M Krys and Joanna Lau v Stichting Shell Pensioenfunds**[7], but that does not seem to me to take the matter any further.

[16] Mr. Phillips QC relies upon other materials. He relies upon a dictum of Lindley LJ in **Sibun v Pearce**[8], to the effect that according to the regulations of a particular building society a member who had given notice of withdrawal remained a member until he had been paid out. He could not, said Lindley LJ, come into competition with outside creditors, but was entitled, as against the continuing members, to be paid the amount due to him before they could divide the assets. That case had nothing to do with priorities. It was about whether the required majority had been obtained for the passing of a members' resolution to dissolve the society. Because withdrawing, but as yet unpaid, members had not been brought into the necessary calculations, it was held it had not. The dictum was purely *obiter*. The point had not been raised in argument and was not necessary to the reasoning of Lindley LJ. The citation is of no assistance.

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[5] HCVAP 2010/014 28 March 2011
[6] section 74 (2) (f)
[7] HCVAP 2011/036, 17 September 2012 at paragraph [4]
[8] (1880) 44 Ch D 354, 371

[17] In **Re Te Kumi Land Company Limited**[9] questions arose what priority was conferred upon preference shareholders in a winding up of the company. The ordinary shareholders admitted, in relation to the first of those questions, that according to the terms of the special resolution pursuant to which the preference shares had been issued, the preference shareholders were entitled to be paid all arrears of dividends declared before the commencement of the winding up in priority to the claims of the ordinary shareholders. The question turned on the true construction of the company's constitution and in any case went by concession. The case is of no assistance.

[18] In **Re Maxwell Communications Corporation Plc (No 3)**[10] Vinelott J is reported as summarizing the effect of section 74(2)(f) of the UK Insolvency Act 1986 as being that sums payable to a member are not to be deemed to be a debt due to that member in a case of competition between himself and any other creditor not a member. The case involved the question whether a liability of the company in liquidation which it had been agreed between the company and its counterparty should be subordinated to the claims of other unsecured creditors was to be deferred in its liquidation to its other unsecured liabilities. Counsel for the counterparty submitted, inter alia, that it would be burdensome for the liquidator to have to adjudicate upon contractual (i.e. extra statutory) priorities. In dismissing this rather desperate submission Vinelott J referred to section 74 as illustrating the fact that liquidators were familiar with having to deal with statutory questions of priority and that they should not, therefore, feel any greater difficulty or embarrassment in dealing with a contractual one. The case was not deciding an issue under section 74. It is true that Vinelott J spoke of 'members' debts' as being postponed to the debts of outside creditors, but he did not say that they had priority over the claims of other members to have their capital returned to them. That was not an issue in the case.

[19] **In Re HIH Casualty and General Insurance Ltd** [11] David Richards J had to deal with differences in the statutory priorities under English and, respectively, Australian insolvency law. He pointed out that each system had slightly differing rules upon these matters. In doing so, he said that certain debts may be deferred, giving as his example the fact that a debt due to a person in his capacity as a shareholder of an insolvent company ranks behind those of ordinary creditors under both the English and the Australian systems. Mr. Phillips QC relies upon the expressions 'deferred' and 'ranks behind the general body of unsecured claims' as showing that such debts rank before the claims of shareholders to a

[9] [1944] NZLR 924
[10] [1993] BCC 369, 377
[11] [2005] EWHC 2125 (Ch) at paragraph [36]

return of their capital. In my judgment, they say no such thing. They are entirely neutral on that question.

[20] Mr. Phillips QC referred to academic commentary on the effect of section 74 of the UK Insolvency Act 1986 and, in particular upon the provisions of section 74(2) (f), which is in the following terms:

> 74 (2) (f) a sum due to any member of the company (in his character of a member) by way of dividends, profits or otherwise is not deemed to be a debt of the company, payable to that member in a case of competition between himself and any other creditor not a member of the company, but any such sum may be taken into account for the purpose of the final adjustment of the rights of the contributories among themselves.

[21] Mayson, French and Ryan, in their Company Law[12] state at page 701 that 'members' debts' incurred by a company before liquidation are payable before returns of capital may be made to members. For this proposition they rely upon **Re Consolidated Goldfields of New Zealand**[13], which was not cited to me, and upon **In re Compania de Electricidad de la Provincia de Buenos Aires Ltd**[14] ('**Electricidad**'), which was.

[22] The question for resolution in the **Electricidad** case was whether certain members and past members of the company who were owed dividends or returns of capital declared or agreed before the liquidation remained creditors of the company for the purposes of rule 106 of the then winding up rules so that they were barred by notices served under the rule from participating in subsequent distributions. Slade J, as he then was, held that they were. In the course of doing so he clearly said that while they were unable to rank equally with external creditors, they were entitled to priority over non-members when it came to distribution of the surplus available after the company's liabilities to external creditors had been satisfied.[15] He described this as a *'third, unstated, exception to the general pari passu rule.'*[16]

[23] Mr Phillips QC also relied upon a quotation from McPherson's Law of Company Liquidation[17], in which the author, Professor Keay, observes at paragraph 14.02 that 'members' debts' must be discharged in full before distribution is made to members. He prefaces the remark with the words 'as we have seen', a reference

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[12] 2008/9 Ed
[13] [1953] Ch 689
[14] [1980] Ch 146
[15] 171C-E, 173B-D
[16] 172B-C
[17] 2nd Ed at paragraph 14.02

to earlier passages in his book. Mr Phillips QC did not take me to that material and consequently Mr Isaacs QC had no opportunity to respond to it. I must accordingly treat the observation as unsupported by authority. A reference to a remark at paragraph 13.038 of the same work takes matters no further, since it is common ground that 'members' debts' are deferred to those of outside creditors. The same applies to the cited extract from Loose on Liquidators, 6th Ed.[18]

Discussion

[24] In this jurisdiction it is established that unpaid redeeming members of companies are creditors, but not entitled, in their liquidations, to compete with external creditors. There is no need to resort to foreign authority, judicial or academic, in order to establish that.

[25] I have been referred to no case, here or overseas, where the dispute was between unpaid redeemers (or other persons with 'members' debts') on the one hand and continuing members on the other and which decides that the rights of unpaid redeemers to participate in any surplus remaining after satisfaction of the liabilities owed to external creditors have priority to the entitlement of continuing members to a return of their capital. In paragraph [21] of her judgment in **Westford**, however, Justice of Appeal George-Creque approved the reasoning of leading Counsel for the Appellant who had submitted that one rationale for the enactment of section 197 was to ensure that past members who had not received the totality of their redemption proceeds before commencement of a liquidation did not gain priority over members who had not redeemed in time, thus preventing an unfair and unseemly scramble in the dying days of the company and thus ensuring that members *inter se* are treated *pari passu*. She went on in paragraph [21] of her judgment to describe unpaid or partially paid redeemers as persons with no locus to claim in the liquidation of a company *'other than in the manner permitted by section 197.'*

[26] Since **Westford** was not about priorities between redeemed and continuing members it may be said that these statements are strictly to be treated as *obiter*, but they are clearly part of the reasoning of the Court of Appeal and therefore of very considerable weight. At the very least, they show clearly that when the Court of Appeal spoke of the claims of unpaid redeemers as being subordinated to those of ordinary creditors, it cannot have been deciding that the redeeming members were entitled to priority over the continuing members or that they formed an additional class of their own, midway between external creditors and continuing members.

[18] at paragraph 11.4

[27] In my judgment the fund to which section 197 is directing its attention is the surplus contemplated by section 207(3). Section 197 makes clear that that fund is available to satisfy outstanding claims of members, past and present, in their capacity as such as well as the entitlement of continuing members to a return on their capital. The machinery envisaged by section 197 conspicuously omits any system of priorities and speaks only of an adjustment between members and, where appropriate, past members. In my judgment the term 'adjustment' is apt in the context, because it takes account of the fact that the amount due to continuing members in respect of their capital entitlements may require adjustment to bring into account liabilities to themselves in respect of dividends and other 'members' debts' as well as liabilities to past members. In the absence of any indication in the statute as to how these various entitlements are to be adjusted, equity, in my judgment, requires the application of the *pari passu* principle. In other words, a calculation is to be made of the amounts ('such sum') of the liabilities owed by the company to its past and present members as well as of the entitlement of continuing members to the return of their capital contributions, and the surplus must be returned to them rateably in accordance with that calculation. None of the authorities to which I have been referred requires a different outcome.

[28] There is, in my judgment, neither need nor justification for postulating, as Slade J did in **Electricidad**, a third class of creditor[13] floating uneasily between external creditors and continuing members and unknown to the draftsman of section 207 or to the legislature.

Conclusion

[29] For these reasons I decline to vary my order of 17 May 2012.

Commercial Court Judge
16 November 2012

[13] after (1) preferential claims and (2) all other admitted claims