

**IN THE EASTERN CARIBBEAN SUPREME COURT
IN THE HIGH COURT OF JUSTICE
BRITISH VIRGIN ISLANDS**

CLAIM NO: 0006 OF 2009

BETWEEN:

PROFESSIONAL OFFSHORE OPPORTUNITY FUND LIMITED
Applicant

And

DAIWA SECURITIES TRUST AND BANKING (EUROPE) PLC
AS CUSTODIAN FOR KBCZAF
Respondent

Appearances: Mr Dirk van Heck of Maples and Calder for the Applicant
Mr Richard Evans of Conyers Dill & Pearman for the Respondent

JUDGMENT IN CHAMBERS

[2009: May 26, June 4]

(Application to set aside statutory demand – whether court satisfied as to substantial dispute – effect of decision that court not so satisfied)

[1] Bannister J [ag]: This is an application to set aside a statutory demand dated 23 December 2008. The company on which it was served, Professional Offshore Opportunity Fund Limited, ('the company') was incorporated on 5 August 2005 under the International Business Companies Act 1984, and automatically re-registered under the BVI Companies Act 2004. It carried on business as an open ended investment company. The creditor, Daiwa Securities Trust and Banking (Europe) plc, ('Daiwa') was the holder of 3,895.6634 Class C participating shares in the company as custodian for KBCZAF. I should add that Daiwa obtained its shares in reliance upon a Confidential Private Placement Memorandum ('CPPM') dated December 1, 2005.

- [2] The statutory demand was in the sum of US\$5,782,788, the amount payable by the company to Daiwa pursuant to a redemption request made by Daiwa on 20 June 2008. In brief, the company's answer to the statutory demand is that at a board meeting held on 21 October 2008 a decision was made (I quote from the affidavit of Marc K Swickle ('Mr Swickle') in support of the company's application) at which the decision was taken to suspend the Net Asset Value and suspend payments to redeeming investors. Mr Swickle exhibits what he says is a 'Memorandum' of the same date evidencing the meeting, to which I will return.
- [3] The material parts, for present purposes, of the company's Articles of Association are as follows:

"REDEMPTION OF SHARES

- 25.(a) Subject to the provisions of the Act, the Company may in accordance with these Articles, purchase, redeem or otherwise acquire any of its own shares for a price which shall not exceed the Net Asset Value at the date of such purchase, redemption or acquisition, as determined in accordance with Regulation 28, and either cancel such shares or hold such shares as Treasury Shares. Any shares held as Treasury Shares may be disposed of by the Company on such terms and conditions as the Company by a Resolution of Directors may from time to time determine. Shares may be purchased or otherwise acquired by the Company in exchange for newly issued shares in the Company.
- 26.(a) Subject to the provisions of Regulation 28, a Member may redeem his shares as of each Redemption Day. A Member wishing to exercise his redemption privilege shall deliver to the Company at least sixty (60) days prior to the proposed date of redemption a written redemption request indicating the number of shares to be redeemed. The redemption request must be accompanied by the share certificate or certificates, if any, representing the shares to be redeemed.
- (c) Redemption proceeds will be paid out within thirty (30) days after the relevant Redemption Day.

27. Upon any redemption of a share by a Member, the Member shall cease to have any Member's rights with respect thereto (except the right to receive the net proceeds of the redemption and the right to receive dividends previously declared but not already paid, if any).

DETERMINATION OF NET ASSET VALUE

- 28.(a) The Net Asset Value per share of each class and series of shares shall be calculated and determined by the Company on each Valuation Day by dividing the then net assets of the Company attributable to each class and series by the total number of outstanding shares in each class and series at the Valuation Day.
- (b) The Company may at any time and from time to time suspend the calculation of its Net Asset Value and the purchase and redemption of its shares from the holders thereof for the whole or any part of any period:
- (ii) during the existence of any state of affairs which, in the opinion of the Company, constitutes an emergency as a result of which disposition by the Company of investments owned by it is not reasonable or practicable, or would be seriously prejudicial, to the holders of shares or the Company.

No issue or redemption of shares will take place during any period when the calculation of the Net Asset Value is suspended. Moreover, the Company reserves the right to withhold payment to persons whose shares have been redeemed (or to persons who have served a redemption notice) prior to such suspension until after the suspension is lifted. Such right will be exercised in circumstances where the director of the Company believe that to make such payment during the period of suspension would materially and adversely affect any prejudice the interests of Members who have not redeemed or given notice to redeem. Any such suspension shall be published by the Company in such manner as it may deem appropriate to the persons likely to be affected thereby, and Members requesting the purchase or redemption of their shares by the Company shall be so notified at the time of the request."

- [4] On 18 July 2008 the Fund Administrator acknowledged Daiwa's redemption request, stating that it had been approved for dealing date October 1, 2008.
- [5] On 17 October 2008 the Fund Administrator sent Daiwa confirmed NAV statements showing the calculation giving rise to the figure claimed in the statutory demand.
- [6] On 21 October 2008, according to the evidence of Mr Swickle which I have referred to above, the board met and decided to suspend NAV and suspend redemptions. The Memorandum to which Mr Swickle refers is in the following terms:

"MEMORANDUM

TO: FILE

FROM: GREG GOLDBERG-DIRECTOR
MARC SWICKLE-DIRECTOR

RE: SUSPENSION OF REDEMPTIONS

DATE: OCTOBER 21, 2008

We have taken action today to formally suspend redemptions for Professional Offshore Opportunity Fund, LTD

As the market has continued to weaken PROOF's portfolio companies have begun to suffer on multiple fronts. In addition to the lack of liquidity and depressed stock prices, potential credit issues now are presented to several of our investments as well as subsequent capital rounds having been pulled. In order to preserve our investments it is imperative that we have cash to meet funding requirements of some of our portfolio companies.

In addition, we need cash on hand to deal with new margin requirements at the prime broker level as well as the newly adopted short rules.

Finally, liquidating positions at discounts to our conversion prices while other PIPE managers face similar issue will only result in a significant hit to the NAV that we believe is unwarranted.

David Sims was not present at this meeting. Howard Berger, non-director manager of the fund was present and agreed with our views and determination.

We will instruct Weursch and Gerring to provide us with the documentation necessary to present to the investors informing them of the suspension as well as all communication needed between PROOF and Folio Administrators.

Sgd. Greg Goldberg-Director
Marc Swickle-Director”

The Memorandum appears to bear the signatures of Mr Goldberg and Mr Swickle. It will be noticed that, contrary to what Mr Swickle states in his affidavit, the Memorandum makes no mention of suspension of NAV. When I asked Mr van Heck, who appeared for the company, what was the ‘action taken’ to which the first line of the Memorandum refers, he said that the Memorandum itself was the action referred to. I have to say that I find that a rather forced interpretation.

- [7] On the following day the company circulated all investors in the fund with a document describing itself as a mid month estimate for October. That document, after summarizing the company’s view of the state of the market, included a paragraph in the following terms:

“PROOF and PTF Liquidity Issues

Due to the current economic conditions and credit crisis, we have suffered more than normal redemption requests. Moreover, a great deal of those requests are “tentative” redemptions. While the model remains strong, and in some cases the dislocation in our space has created tremendous opportunities, investors, as stated above, have either had to meet redemptions themselves or simply panicked and redeemed. As such, it is management’s fiduciary obligation to protect the integrity of the fund and the Net Asset Value for all of its investors. To that end Management is considering all options in order to provide the exit terms and conditions for all investors redeeming, and to clearly outline the tremendous opportunity for those remaining and new investors.”

Mr Evans, who appears for Daiwa, says that it is incredible that the company should have written to its investors in this manner only one day after its board had met and suspended, or purported to suspend, redemptions. He relies upon the statement that as at 22 October 2008 the company's management was 'considering all options'. Mr van Heck countered by saying that there is no evidence that the document was not *produced* mid-month. I found that rather a strange submission coming from the only party before the court in a position to provide the evidence that it was. In the absence of such evidence, the Court can only conclude that, if the 22 October 2008 circular is to be believed, the company's position on that date was that no decision had been taken to deal with the difficulties mentioned. That would include any decision to suspend NAV.

- [8] Mr Evans relied strongly upon the absence of any corroboration of this event from Mr Goldberg or from Mr Berger, each of whom is recorded as having attended the meeting. He might have added that nothing seems to have been done with the Memorandum other than to file it. If this meeting really did take place and really did take the decision which Mr Swickle says it took, then one would have expected it to have been passed immediately to the Fund Administrators so that redemptions could be halted forthwith, especially given the urgency which the Memorandum describes. Instead, as will be seen, the redemption process appears to have continued undisturbed until at least 27 October 2009. One has to bear in mind in saying this that no actual cash would have had to have been paid over until 31 October 2009, but it remains astonishing that the Administrators do not appear to have been told of this decision as soon as it was taken.

- [9] On 27 October 2008 the Fund Administrators sent Daiwa an e-mail in the following terms:

“From: “Mashauna Lake-Farrington” mashauna@folioadmin.com
To: info@thomaslimited.com
Date: 10/27/2008 9:37 AM
Subject: Contract Note – September 2008 Redemption

Dear Investor

Attached is the contract note for the recent transaction of Daiwa Securities Trust & Banking (Europe) plc as custodian for KBCZAF regarding Professional Offshore Opportunity Fund Ltd Class C.

Please note that subscription amounts are stated net of initial charges.

Folio Administrators Limited”

The Redemption Confirmation read as follows:

“REDEMPTION CONFIRMATION On Dealing Day October 1, 2008, we confirm we have redeemed the following shares : Description of Shares	
Ordinary Shares of par value USD 0.01 per share	
Class [or Series] of Share	Class C Participating Shares
Number of Shares Redeemed	3,895.6634
Offering Price	1,484.4065
Redemption Amount	USD 5,782,748.10
Dealing Date	October 1, 2008
Reference	32931”

- [10] On 4 December 2008, Attorneys acting for the company wrote to Daiwa's principal (with a copy to the company) explaining that the reason why the Redemption Confirmation had been sent out during a period when redemptions were suspended (and while the company reserved the right, pursuant to Article 28, to withhold payments to persons whose shares had previously been redeemed) was that it had been sent 'inadvertently'. At the hearing, Mr van Heck resiled from this explanation and said that the e-mail of 27 October 2008 attaching the Redemption Confirmation, was deliberately sent, because the redemption had indeed been effected – it was simply that no money would be forthcoming because of the suspension. To describe this change of position as unattractive seems mild. Presumably the company's attorneys had written the letter of 4 December 2008 on instructions and the company had been in possession of a copy of it for getting on for five months, yet Mr Swickle makes no mention of the point in his affidavit in support of the company's application.
- [11] On 31 October 2008 the company became obliged (unless NAV had been validly suspended) to pay out Daiwa's redemption money. The money has never been paid.
- [12] On 4 November 2008 the company sent a circular to all investors. It was headed 'Re: Notification of Temporary Suspension of Investor Redemptions' and signed by Mr Swickle and its first paragraph read as follows:

“Dear Investor:

This letter serves to advise you that as a result of unprecedented adversity in market conditions, the unexpectedly high number and amount of redemption requests, and the need to protect assets for all shareholders of the Professional Offshore Opportunity Fund Limited (the “Fund”), we, as directors of the Fund, have decided to temporarily suspend redemptions of the Fund's shares.”

- [13] Mr Evans, for Daiwa, say that if redemptions had indeed been suspended on 21 October 2008, the fortnight's delay between that being done and investors being notified is extraordinary. He pointed to the final sentence in the section of the CPPM dealing with suspension of redemptions, which reads: 'The Directors will use their best endeavours to notify Fund shareholders of such suspensions and the ending of suspensions'.
- [14] Mr van Heck says that provided that there was a valid suspension, it does not matter whether that took place on 21 October 2008 (as, on his construction, the Memorandum says), provided that it took place before 4 November 2008, when the circular went out. When pressed, however, he accepted, I think, that the only candidate for a decision by the board to suspend in the intervening period is the meeting of 21 October 2008 whose transactions are summarized in the Memorandum.
- [15] Mr van Heck says that provided Article 28(b) was invoked before the company made any actual payment in respect of Daiwa's debt, then despite the fact that Daiwa had completed all the phases of the redemption process and (absent any suspension of NAV) had become entitled to payment on 31 October 2008, it cannot, because of the suspension, claim the money which it is owed as due and payable. If he is right then Daiwa's statutory demand is bad: section 155(2)(a) Insolvency Act 2003.
- [16] Section 157(1) of the Insolvency Act 2003 requires the court to set aside a statutory demand if (inter alia) it is satisfied that there is a substantial dispute as to whether the debt is owing or due. I am not sure what is the distinction drawn in this section between 'owing' and 'due' but it seems most likely that the legislature intended the distinction to be between a debt that was outstanding but not yet payable and one that was both owing and payable. In the present case there is no dispute that the debt is owing (or, as I would prefer to put it, 'due'). The dispute

is as to whether the debt is payable. But provided that the court is satisfied that there is a substantial dispute as to either fact, the demand must be set aside. The wording of Section 157(1) does not require the court to resolve the dispute. It merely requires it to act if “satisfied” that there is a substantial dispute. In my judgment that means that the court must have been left in no doubt that a substantial dispute exists. On the authorities, that also means that the court must be in no doubt that the dispute is one in which the company has an honest belief. Again, the section does not require the court to make a finding of honesty or dishonesty. It requires the court to be satisfied that the company honestly believes in the virtue of its argument. A decision that the court is not satisfied that the dispute is a substantial one in this sense does not of itself involve a finding that the dispute is not substantial or that it is dishonestly maintained on the part of the company. It means no more than that the court has not been convinced as to the substance of it or as to the bona fides with which it is being maintained.

[17] I have to say that I am not satisfied that the dispute in the present case is of a substantial nature and honestly believed in. As I have said, that does not mean that I am making a finding of dishonesty, let alone of forgery or perjury. The company’s dispute may be entirely genuine, for all I know. All I am saying is that I have not been satisfied as to that on the evidence which I have seen, particularly bearing in mind that there has been no evidence put in by the company in response to Daiwa’s evidence in answer. I therefore dismiss this application.

[18] All of this may in any event be academic. It remains the case that Daiwa is and has since 1 October 2008 been an admitted creditor of the company in the sum of upwards of \$5 million. The fact that a company may have a contractual right to suspend payment of its debts does not, in my judgment, make it any less the case (if that be its position) that it is unable to pay them. While I must be careful to avoid the appearance of deciding (and do not decide) on this application issues which would or may arise on an originating application brought by Daiwa for the appointment of a liquidator, it seems to me (without having heard evidence or

argument directed to that issue) that on such an application the company might have considerable difficulty in persuading the court that it was not insolvent within the meaning of section 8(1)(c)(ii) of the Insolvency Act 2003 – statutory demand or no statutory demand.

Edward Bannister
Commercial Court Judge
4 June 2009