

Cayman Court confirms Redemption Creditors' entitlement to Statutory Interest

UPDATE

Update prepared by Peter Hayden (Partner, Cayman Islands)

In a recent decision, the Grand Court of the Cayman Islands determined, for the first time, the question of whether a redeemed but unpaid investor is entitled to receive statutory interest on its debt for the period it remains unpaid.

Section 149 of the Companies Law (the **Law**) provides for interest to be payable on all debts proved in the liquidation. However, an argument was advanced that this did not apply to debts which had been deferred and ranked behind those of ordinary, unsecured creditors. Unsurprisingly, given the clear language of the Law, the Grand Court found that, in solvent liquidations, statutory interest is payable on deferred debts as well as ordinary, unsecured debts.

Peter Hayden, Nicholas Fox, Rocco Cecere and Christopher Levers of Mourant acted for the successful creditors.

Background

This is a further decision in the ongoing representative proceedings between Primeo Fund (in official liquidation) (**Primeo**) and Herald Fund SPC (in official liquidation) (**Herald**).

A number of investors (the **Redemption Creditors**), including Primeo, had submitted redemption requests to Herald for redemption dates on or before 1 December 2008. On 12 December 2008, following the discovery of the Madoff fraud, Herald suspended the calculation of NAV. On 24 December 2008, Herald suspended payment of redemptions. An issue then arose in the Herald liquidation as to whether the Redemption Creditors had creditor claims or whether they were somehow relegated back to shareholder status.

As reported in our briefing dated [6 July 2017](#), the Judicial Committee of the Privy Council, upheld the earlier decisions of both the Grand Court and the Cayman Islands Court of Appeal, and found that the Redemption Creditors ranked as creditors in Herald's liquidation for the unpaid redemption proceeds.

The Privy Council also found that, as a result of the application of section 49(g) of the Law, the creditor claims of the Redemption Creditors were deferred and ranked behind the claims of ordinary, unsecured creditors.

Statutory Interest Issue

Herald sought to challenge the entitlement of the Redemption Creditors to claim statutory interest in the liquidation on their claims for unpaid redemption proceeds on the basis that the Redemption Creditors' debts were not proved for the purposes of section 149 of the Law.

In support of that contention, Herald argued that:

- (i) the statutory "waterfall" approved by the Privy Council in *Pearson v Primeo* provides for the payment of statutory interest before the payment of deferred creditor claims;
- (ii) as the Redemption Creditors' claims were deferred creditor claims, not only were they deferred to the principal claims of Herald's ordinary, unsecured creditors, but also to any and all claims for statutory interest; and
- (iii) the deferred Redemption Creditor claims would therefore not have been "proved" at the point when statutory interest would be paid (which, according to Herald, only occurred once in a liquidation).

In addition, Herald also argued that the proving process contemplated by section 149 of the Law was the formal proof of debt process. As Herald had obtained an order dispensing with the proof of debt process for Primeo and the Redemption Creditors, Herald claimed that those debts had not been proved and therefore did not attract statutory interest.

Primeo, as the representative party for the Redemption Creditors, argued that the Redemption Creditors were creditors whose claims had been proved and paid in the liquidation, and they were therefore entitled to statutory interest pursuant to sections 149(1) and (2) of the Law, which provide for interest to be paid on *any debt proved in the winding up*.

The Court's Decision

The Grand Court held that the Redemption Creditors are *prima facie* entitled to statutory interest. Similar to the position in the United Kingdom, it considered that the statutory interest provisions in the Law were a complete code whose purpose is to compensate creditors who cannot claim interest on a contractual basis for the delay in being paid. It found that, as a matter of policy, there was no good reason for adopting different approaches to deferred creditors and ordinary, unsecured creditors because the prejudice suffered by both classes was *indistinguishable*.

It also found that Herald's reliance upon the statutory "waterfall" was misplaced, agreeing with the dicta of Lord Neuberger in *Re Lehman Brothers International (Europe) (in Administration)* [2017] UKSC 38, that a "waterfall" is a generalised summary of the distribution priorities in an insolvency and *was not intended to be treated as some sort of quasi-statutory statement of immutable legal principle*.

Instead, by reference to the "complete code" set out in the statutory interest provisions, the Grand Court held that, in a solvent liquidation, where there is sufficient surplus for the claims of both ordinary creditors and deferred creditors to be paid in full, including statutory interest, there was no competition between members/former members and ordinary creditors such that section 49(g) did not interfere with a proved creditor's clear entitlement to statutory interest under section 149 of the Law¹.

As Herald was a solvent liquidation, this meant that the Redemption Creditors were eligible for statutory interest if their claims had been proved. In dismissing Herald's argument that the Redemption Creditors' claims had not been proved, the Grand Court found that a fundamental goal of the insolvency code was to reduce the costs of the liquidation process and to maximise returns to stakeholders. The term "proved" must be given a broad, expansive meaning such that a debt will be proved where it has been established through whatever legally recognised process a liquidator deems appropriate.

As Herald had not only obtained an order dispensing with the need for formal proofs, but had also admitted and paid the principal claims of the Redemption Creditors in full, there was no basis for Herald to assert that

¹ Although the issue did not arise in this case because Herald is solvent, the Court noted that, where there is competition between a member/former member and an ordinary creditor, section 49(g) of the Law may operate to reduce or extinguish the interest claims of any redeemed creditors.

those claims had not been proved for the purposes of section 149 of the Law. The Grand Court therefore found that statutory interest is payable to Primeo and the other Redemption Creditors pursuant to section 149 of the Law.

Contacts



Peter Hayden
Partner, Mourant Ozannes
Cayman Islands
+1 345 814 9108
peter.hayden@mourant.com



Nicholas Fox
Partner, Mourant Ozannes
Cayman Islands
+1 345 814 9268
nicholas.fox@mourant.com

This update is only intended to give a summary and general overview of the subject matter. It is not intended to be comprehensive and does not constitute, and should not be taken to be, legal advice. If you would like legal advice or further information on any issue raised by this update, please get in touch with one of your usual contacts. © 2018 MOURANT OZANNES ALL RIGHTS RESERVED

[Document Reference]