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Client Memorandum

BVI and Cayman Islands – Litigation Wrap-Up 2016

The BVI and Cayman Courts are usually the work horses of the Caribbean international financial centres. 2016 proved to be no different. The past 12 months have seen important decisions coming out of both jurisdictions. We highlight some of the key decisions in this article.

British Virgin Islands

Derivative Actions

In the case of Glory Advance International Limited v Merit Fortune Holdings Limited the BVI court had to consider whether to grant leave to Glory Advance to bring a derivative action under section 184C of the BVI Business Companies Act, 2004 ("BC Act") in Hong Kong on behalf of its BVI subsidiary company, Merit Fortune to contest the voluntary appointment of liquidators in Hong Kong to Luck Silver Limited, the wholly owned subsidiary of Merit Fortune. The application was in effect a request for leave to bring a double derivative claim.

Largely relying on technical grounds, the Court refused permission to bring the derivative action. The Court's findings rested principally on its perception that the "expert evidence" adduced by the applicant on Hong Kong law was not impartial, independent, objective and unbiased as the evidence came from onshore Counsel for the applicant. The Court also held that the evidence adduced did not satisfy all of the requirements laid out in the BC Act (such as establishing a real prospect of success or that the proceedings were in the interests of the company). The Court also felt it was inevitable that the BVI parent company and its Hong Kong subsidiary would end up in liquidation due to admissions of deadlock at board and shareholder level, so it was pointless to attempt to unwind the liquidation proceedings in Hong Kong.

Norwich Pharmacal Relief

Whilst other jurisdictions are busy reining in the scope of Norwich Pharmacal relief, the BVI court has broken ranks. The court has held that Norwich Pharmacal relief is available "post-judgment in aid of enforcement of a foreign court's judgment where there is reasonable suspicion for believing that a disclosure defendant is mixed up in the wilful evasion of another's judgment debt" (in this case the disclosure defendant was the registered agent of a BVI company subject to a judgment issued by a foreign court) or "to assist in securing compliance with freezing orders, including such orders made by foreign courts". The Court went on to hold that it was irrelevant to the grant of relief that the BVI company was not set up as a vehicle to help perpetrate wrongdoing but that sometime after its incorporation it was so used. In reaching this conclusion the Court relied on principles applied to claims to pierce the corporate veil.

Forum challenge

The Court of Appeal recently held that in a case concerning allegations of fraudulent misrepresentation, a key factor in determining the most appropriate forum to litigate the claim was where the actions complained of took place. The Court of Appeal held that the Judge at first instance had been wrong to decide that the BVI was the appropriate forum on the basis that the claim concerned shares of a BVI company and documents in the BVI were relied on to have the name of a party allegedly improperly entered on the register of members. The Court of Appeal held that it is the underlying claim that is key to determining forum rather than an ancillary remedy (rectification of the register of members, which is a statutory remedy under BVI law) which may follow if the underlying claim succeeds.

Recovery of Costs

Following a highly criticised Court of Appeal decision on the issue of recoverability of costs incurred by foreign lawyers assisting in BVI court matters, the BVI Court refused to follow the Court of Appeal and held that fees incurred by foreign lawyers are generally recoverable as a disbursement of the BVI legal practitioners and will be assessed in the usual way. However the Court noted that recoverable costs extend only to work undertaken by the foreign law firm by way of assistance to the BVI firm which has ultimate responsibility and supervision of the matter.

Cayman Islands

Right to notice of disclosure of information request made by US Inland Revenue Service

The Cayman Islands have enacted legislation to put into effect treaty obligations to ensure the timely disclosure of information to overseas tax authorities, known as the Tax Information Authority Law (TIAL).

In matter of the United States of America v Verna Cheryl Womack (8 April 2016), the US IRS had obtained and relied on a substantial amount of disclosure of information which it had obtained from service providers in the Cayman Islands under compulsion via the TIAL. The Grand Court considered the question of to what extent a person under investigation or prosecution for tax offences is entitled to notice of attempts to obtain disclosure of their confidential records. In this case much of the disclosure had been given under compulsion by court order, no prior notice of which had been given. Noting that there will always be cases where notice is inappropriate (in particular where by giving notice the investigation risks being compromised) the Court accepted the argument advanced by TTA on Mrs Womack's behalf that the default position is for notice to be given in cases that come before the Court. A person is entitled as of right under Cayman Islands law to a fair hearing and that is likely to be difficult to achieve in conditions of secrecy.

Thompson Resorts v Carl Clappison & Others (CICA 909/2016)

Many successful residential property developments in the Cayman Islands have been built alongside resort hotels and are held through strata title. When an investor purchases a residential unit in the complex the investor agrees to be bound by the by-laws of the strata. A common practice has emerged by which developers grant themselves complete control of the strata through weighted voting rights, much like a manager of a hedge fund will do. In this case the developers, who TTA represented, granted themselves a casting vote on all resolutions, ensuring that they could never be outvoted (the rationale being so the developer could maintain standards and protect the integrity of the development from being hijacked by individual owners). A group of proprietors sought a declaration from the Court that the strata by-laws incorporating the casting vote were unlawful.

At trial the Court found that the by-law was void, making a comparison with public law concepts of reasonableness. The Court of Appeal disagreed, finding that there was no place for public law concepts in private law arrangement between consenting parties. Whilst the weighted voting rights did give the developers complete control over the strata, this was something that was clear from the outset. An investor has a choice whether or not to purchase a unit in a development organised in this manner and must abide by its rules.

Loss of substratum and just and equitable liquidation of a fund

In the case of Xena Investments Limited v Washington Special Opportunity Fund Inc.(1 March 2016),certain investors in a fund, which was in "soft wind down" mode, attempted to have the fund placed into liquidation on the grounds that the fund was no longer viable and there had been a loss in confidence in its management. As to the first ground, the Court held that the mere fact that a fund is in wind down should not of itself and in every case justify a winding up order. A significant factor in this case was that the wind down process had been approved by the company's members through an amendment to its articles of association. As such it could not be argued that the objects of the company could no longer be achieved (in other words, there was no loss of substratum). As to the second ground (loss of confidence in management) the Court was highly critical of the

approach taken by the investor Petitioners listing as many complaints as they could find, after the event, to justify the petition. The Judge, in dismissing the petition, said this amounted to a "substantial regurgitation of stale claims and alleged past ills" and noted that the fund manager's actions were reasonable, commercially defensible and that investors had been made aware of the manager's actions. There will of course still be cases justifying intervention by investors, but care must be taken to identify those cases which are suitable for the draconian remedy of a winding up order.

Normal Service Resumed

The vast majority of business conducted in the Cayman Islands involves residents of other countries. Being able to bring legal proceedings against parties outside the jurisdiction is clearly important. One tool available to claimants of Cayman court proceedings when encountering difficulties serving a defendant is to seek an order for substituted service. Substituted service is available in cases where the defendant is located out of the jurisdiction and the claimant can show that personal service on him is practically impossible.

In the recent case of McKeeva Bush v David Baines et al (11 October 2016) the Grand Court of the Cayman Islands was faced with the unusual situation of a defendant who could not be served personally as he enjoyed diplomatic immunity from service. The case (in which TTA represents the claimant) involved claims by the Former Premier of the Cayman Islands arising out of an alleged conspiracy by the defendants to remove him from political office. One of the defendants, Mr Taylor, had been the Governor of the Cayman Islands at the time of the alleged conspiracy but had left his post to become British Ambassador to Mexico before the proceedings were commenced.

Mr Taylor did not accept service voluntarily. At an ex parte hearing, leave was given to affect substituted service on Mr Taylor as it was legally impossible to serve him personally because of his diplomatic status. Mr Taylor applied to set aside the service, primarily on the grounds that he could and should have been served through diplomatic channels.

The Court found that as serving Ambassador Mr Taylor could not be served personally due to his diplomatic immunity. The Court also noted that service through diplomatic channels had been described in several cases as unreliable or difficult and stressed that under the modern Cayman Islands court rules the Court is obliged to deal with cases in a just, economical and expeditious manner. The Court noted that Mr Taylor had received copies of the claim documents and was accordingly well aware of the allegations against him. His objection to service was technical only and was rejected accordingly.

Conclusion

Speculation is rife that 2017 will see some large insolvency matters in the offshore financial centres (particularly across the Asia/BVI platform) but this sort of speculation has lingered for the past few years without coming to fruition. It is likely that there will continue to be increased activity in shareholder litigation, non-contentious restructurings and take private transactions.

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