IN THE GRAND COURT OF THE CAYMAN ISLANDS

FINANCIAL SERVICES DIVISION

The Honourable Mr. Justice Andrew J. Jones QC
In Open Court, 14th May 2012

Cause FSD No.275 of 2010(AJJ)

BETWEEN:

(1) **IRVING H. PICARD (Trustee for the liquidation of the business of Bernard L. Madoff Investment Securities LLC (in Securities Investor Protection Act liquidation))**

(2) **BERNARD L. MADOFF INVESTMENT SECURITIES LLC (in Securities Investor Protection Act liquidation)**

Plaintiffs

- And -

PRIMEO FUND (In Official Liquidation) **Defendant**

Appearances: Mr. Pushpinder Saini QC instructed by Mr. John Harris of Higgs & Johnson for the Plaintiffs

Mr. Michael Crystal QC instructed by Mr. Peter Hayden and Mr. Nicholas Fox of Mourant for the Defendant

REASONS

1. Primeo Fund ("Primeo") was incorporated in November 1993 as an open ended investment fund. It invested the whole, or practically the whole, of its assets with Bernard L. Madoff Investment Securities LLL ("BLMIS") both directly and, from June 2007 onwards, indirectly through Alpha Prime Equity Hedged Fund ("Alpha") and Herald Segregated One USA Fund ("Herald"). BLMIS is the company through which Mr. Bernard Madoff conducted a fraudulent "ponzi scheme". It is the subject of a liquidation proceeding in New York pursuant to the United States Securities Investor Protection Act. Mr. Irving H. Picard ("the Trustee") is the court appointed trustee of

BLMIS. On 15th July 2009 the Trustee commenced proceedings against Primeo in the United States Bankruptcy Court for the Southern District of New York by which he asserted "claw back" claims pursuant to the Securities Investor Protection Act, the United States Bankruptcy Code and the New York Fraudulent Conveyance Code.[1] Primeo's Official Liquidators decided not to file a motion challenging the jurisdiction of the US court or file an answer or respond in any other way within the period prescribed by the rules, with the result that the Trustee entered a default judgment on 1st September 2009.

2. On 22nd October 2010 the Trustee applied pursuant to section 97(1) of the Companies Law for leave to commence proceedings against Primeo in this jurisdiction.[2] By his originating summons the Trustee sought leave to commence only what is described as a "turnover claim" which is a cause of action arising under US law and vested in the Trustee. However, the scope of the application was enlarged significantly to include causes of action vested in BLMIS and arising under both Cayman Islands law and US law. In the event, Primeo did not oppose this application and the Plaintiffs' writ in this action was issued and served on 9th December 2010. In addition to the "turnover claim", the Plaintiffs' statement of claim asserts constructive trust claims (arising under both Cayman and US law), breach of fiduciary duty claims (arising under US law), preference claims (based upon the application of section 145 of the Companies Law), claims *in personam* for knowing receipt and fraudulent trading claims (based upon the application of section 147 of the Companies Law). At the hearing on 9th December 2010 the Plaintiffs' counsel indicated that he proposed to seek an order for the trial of preliminary issues arising in both the action now commenced against Primeo and in the similar action already commenced against Harley International (Cayman) Limited (In Liquidation) ("Harley")[3]. I directed that this issue be considered at a case management conference to

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[1] Adversary Proceeding No. 08-01789 (BRL) entitled *Irving H. Picard, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC – v- Primeo Fund.*

[2] Cause No. FSD 230 of 2010 entitled *Irving H. Picard as trustee for the liquidation of the business of Bernard L. Madoff Investment Securities LLC (In Securities Investor Protection Act Liquidation) –v- Primeo Fund (in voluntary liquidation).*

[3] *Cause No. FSD 60 of 2010.*

be held on 19th January 2011 which was to be attended by counsel for both Primeo and Harley.

3. In the meantime, on 5th December 2010 the Trustee had filed an amended complaint against Primeo (and some 50 other defendants) in the United States Bankruptcy Court for the Southern District of New York[4] and on 6th January 2011 the original proceeding was dismissed without prejudice. As I understand it, the amended complaint asserts the same causes of action against Primeo as the original one, namely the recovery of allegedly preferential payments and fraudulent transfers made by BLMIS to Primeo, either directly or indirectly through Alpha and Herald. The purpose of discontinuing the original adversary proceeding and commencing a new one was to consolidate the Primeo claim into a larger action.

4. On 19th January 2011 I made an order that the following preliminary issues of law should be determined –

> *(1) Whether, on the assumption that the Plaintiffs have avoidance claims against Primeo under US insolvency law on the basis pleaded in the Plaintiffs' Statement of Claim, the Grand Court is able to apply US insolvency law under section 241 and/or section 242 of the Companies Law (2010 Revision).*
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> *(2) Whether the Grand Court is entitled to apply Section 145 of the Companies Law or equivalent rules as a matter of common law or under Sections 241 or 242 of the Companies Law to avoid the Six Month Payments (as defined in the Statement of Claim) and/or to entitle the Plaintiffs to judgment against Primeo for the Credit Balance (as defined in the Statement of Claim) and/or for any shortfall as if (contrary to the reality) BLMIS had gone into liquidation in the Cayman Islands on 15 December 2008.*

[4] Adversary Proceeding No. 09-1364 (BRL) entitled *Irving H. Picard, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC –v- HSBC Bank Plc et al.*

(3) Whether the Grand Court is entitled to apply section 147 of the Companies Law or equivalent rules as a matter of common law or under sections 241 or 242 of the Companies Law as to require Primeo to make a contribution to the estate of BLMIS.

5. I also directed the determination of further issues concerning insolvency law set-off and analogous substantive law principles. It is important not to lose sight of the fact that the preliminary issues defined in this Order are pure points of Cayman Islands law which will be determined on the basis of counsels' submissions without the need for any affidavit evidence to be filed. The resolution of these issues is important to the outcome of this action, but it is also of some general public importance. A resolution of these preliminary issues (set out above) in favour of Primeo would result in Sections VI, X and XII of the Plaintiffs' statement of claim being struck out as disclosing no reasonable cause of action. Conversely, the resolution of these issues in favour of the Trustee might lead him to the conclusion that it would be unnecessary to pursue the claims pleaded in Sections VII, VIII, IX and XI. It is also relevant that the Order for the determination of preliminary issues was made on the application of the Plaintiffs (as it turned out, with the support of Primeo) after having commenced the new proceeding against Primeo in New York.

6. It was originally intended that the trial of the preliminary issues would take place at a three day hearing commencing on 13th April 2011, failing which I had indicated that, from the Court's point of view, the hearing could take place in May or September of last year. In the event the parties' were unable to agree upon any date which were reasonably convenient for their respective counsel which lead Primeo to issue a summons on 18th August 2011 seeking an order that I fix a hearing date. The date proposed was in February 2012. In the event the hearing was fixed for 10 days commencing on 15th October 2012.

7. My Order of 19th January 2011 included a usual provision that no further steps be taken in the action by either party until further order. However, it was then anticipated that the preliminaries issues would be determined in April with the result that some "further

order" would be made in May or shortly thereafter. When it became clear that there would be a significant delay, Primeo produced a draft of its intended defence and counterclaim and, by a summons issued on 17th August, sought leave to file and serve it. The Plaintiffs opposed this approach on the basis that it would be inconsistent with the concept of ordering the trial of preliminary issues and might result in wasted costs. Primeo's argument was that, in the light of the unexpected delay in fixing a date for the hearing of the preliminary issues, it was no longer appropriate for all other steps in the proceeding to be held up for so long when the determination of the preliminary issues would not necessarily dispose of the totality of the Plaintiffs' claims. I accepted this submission and on 1st September I made an order that the defence and counterclaim (a draft of which had been in the possession of the Trustee for some weeks) could be formally filed and served the following day. The Plaintiffs served a reply and defence to counterclaim on 22nd September 2011.

8. A further case management conference was held on 26th September 2011, the original purpose of which was to fix a date for the hearing of the preliminary issues but its scope was enlarged by the Plaintiffs who made an application for an order that additional issues be added and that expert evidence of US law should be adduced. Since Primeo had been given very little notice of these additional matters, another case management conference was held on 18th November, in advance of which the parties' counsel exchanged lengthy skeleton arguments and filed further affidavit evidence. [5] I ruled that evidence of US law could not be adduced, whilst leaving open the possibility that the parties will make submissions based upon US case law as an aid to the construction of Section 241 of the Companies Law. I also heard a lengthy submission to the effect that Primeo's counterclaim could not succeed because it claims only reflective loss. If this is right, it is said that the counterclaim should be struck out as disclosing no reasonable cause of action, in which case it would be unnecessary to determine the 5th, 6th and 7th issues defined in my Order of 19th January 2011. Having previously decided that the hearing of the preliminary issues would not take place until October 2012, I merely gave liberty to

[5] *The 3rd Affidavit of Richard Fogerty was filed on 11th November 2011 on behalf of Primeo. The 4th Affidavit Gonzallo Zeballos was filed on 25th November 2011 on behalf of the Plaintiffs.*

apply to the Court to determine whether any additional preliminary issue regarding reflective loss should be determined in advance of the October 2012 hearing. No such application has been made.

9. Shortly before this case management conference, on 15th November, the Trustee issued a summons for an order that this action, including the determination of the preliminary issues, be temporarily stayed until further order on case management grounds. This is the summons which I heard and dismissed on 14th May. In support of this summons, the plaintiffs relied upon a written submission delivered on 2nd May and the 5th and 6th Affidavits of Gonzalo Zeballos filed on 9th February and 18th April 2012. It is not in dispute that the Court has an inherent jurisdiction to grant a temporary stay of proceedings on case management grounds which is quite distinct from its jurisdiction to so on *forum non conveniens* or *lis alibi pendens,* although the case law suggests that it is a power which should be exercised only in "rare and compelling circumstances". The Plaintiffs case is put on two grounds.

10. Firstly, it is said that the Cayman action was commenced in October 2010[6] "as a precautionary measure" and "on a protective basis, to cater for the possibility of Primeo failing to submit to the jurisdiction of the U.S. courts". If this was the basis upon which the Trustee sought and obtained leave, it has to be said that he failed to disclose his intention to the Court. His supporting affidavit and counsel's skeleton argument contain no suggestion that the Cayman action should be regarded as some form of protective writ. To the contrary, the Trustee made it clear that he intended to proceed with the Cayman action and that was the basis upon which I made my orders of 8th December 2010 and 19th January 2011. The Trustee now says that Primeo appears to have changed its position in that it has taken steps in the New York action which arguably leads to the conclusion that it has submitted to the jurisdiction of the US courts. This is denied by Primeo and so the Trustee submits that the Cayman action "should be stayed until the position in this regard is clear". Primeo responded to the amended complaint on 16th May

[6] *The originating summons by which the Trustee sought leave to commence this action was issued on 22nd October 2010. Leave was granted on 8th December 2010 and the writ was actually issued the following day.*

2011 by entering into a Stipulation and Consent Order which records its intention to "move to withdraw the reference to the Bankruptcy Court" and the Trustee's agreement to extend time for pleading to the amended complaint until 21 days after its motion has been determined. The meaning and effect of a "motion to withdraw the reference" is explained by Primeo's New York attorney, Mr. Gary Lee of Morrison & Foerster LLC. Put simply, it is a procedural motion by which a proceeding commenced in the Bankruptcy Court is transferred to the District Court. His evidence is very specific that a reference to withdraw the reference does not amount to a submission to the jurisdiction of the New York courts as a matter of New York law and that Primeo's Stipulation and Consent Order expressly reserves Primeo's right to challenge the jurisdiction.[7] Primeo also denies that it has taken any steps which lead to the conclusion, as a matter of Cayman Islands law, that it should be treated as having voluntarily submitted to the jurisdiction such that any judgment of the New York court (whether the Bankruptcy Court or the District Court) is capable of being recognized and/or enforced in the Cayman Islands. Even if it has done so, the evidence is that it will take many years for the Trustee to reach the position of being able to commence an enforcement action in this jurisdiction. The mere fact that the Trustee is arguably in a position in which he may be able to obtain a judgment in a New York court in three or four years' time which is capable of recognition in this jurisdiction is not a compelling reason for staying the Cayman action which has been on foot and actively pursued for the past eighteen months.

11. Secondly, it is said that it would be inappropriate for the same issues to be litigated simultaneously in the two jurisdictions. In principle, this would be a good reason for staying one or other of the proceedings, but it is not in fact something which is happening or is ever likely to happen in this case. It is plainly obvious that the preliminary issues to be determined by this Court in October are matters of Cayman Islands law which will not arise in the New York action. The Trustee's point is that Primeo's defence in the Cayman action pleads the "safe harbour" defence under section 546(e) of the US Bankruptcy Code. In the event that preliminary issues (1) to (3) are decided against Primeo, it will be open to Primeo to rely upon the "safe harbour" defence unless the decision rendered by

[7] *Affidavit of Gary Lee filed on 3rd April 2012, paragraph 16.*

Judge Rakoff in *Picard –v- Katz* on 27th September 2011 is reversed on appeal. The same defence will be available to Primeo (and scores of other defendants) in the New Proceeding if it does indeed change its mind and decide to defend the case on its merits. Whether or not section 546(e) provides a defence to clawback claims made against investors who received payments from BLMIS in circumstances in which the Trustee cannot assert actual fraud against them is an important point of law, the resolution of which will have a significant impact upon the ultimate outcome of the BLMIS liquidation. The idea that this issue will ever be litigated simultaneously before the New York and Cayman courts as between the Trustee and Primeo (or any other investor) is wholly unrealistic. If the Cayman action ever reaches the stage at which Primeo needs to rely upon this defence, there will be no scope for argument about the meaning and effect of section 546(e) of the US Bankruptcy Code. This issue has already been determined against the Trustee at the District Court level and it will be determined at the appellate level in one or other of the cases pending between the Trustee and scores of other investors in the same position as Primeo. The Trustee's counsel made the point that it would be open to the parties in the Cayman action to engage expert witnesses to argue that the decision of the US Court of Appeals is wrong. Whilst he may be technically correct, in reality it is inherently unlikely that I would be persuaded to attach any weight whatsoever to such evidence. The fact that Primeo has pleaded the "safe harbor" defence in the Cayman action and could do so in the New York action (if it decides to defend on the merits) is not a good reason for granting a stay in the circumstances of this case.

12. For these reasons, and for the other reasons expressed by Mr. Crystal in his written submissions, I concluded that application for a stay should be dismissed.

Dated the 6th day of June 2012

The Honourable Mr. Justice Andrew J. Jones QC
JUDGE OF THE GRAND COURT