IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

CAUSE No. FSD 190 OF 2021 (DDJ)

IN THE MATTER OF THE COMPANIES ACT (2023 REVISION)
AND IN THE MATTER OF HQP CORPORATION LIMITED (IN OFFICIAL LIQUIDATION)

Appearances:	Mr Tom Smith KC of Counsel and Ms Shelley White and Mr Will Waldron of Walkers (Cayman) LLP for the Liquidators Mr Robert Levy KC of Counsel and Mr Guy Cowan and Mr Harry Shaw of Campbells LLP for the Petitioners Mr Richard Millett KC of Counsel and Mr Erik Bodden and Dr Alecia Johns of Conyers Dill & Pearman LLP for Access Industries Holdings and AI Autoparts LLC
Before:	The Hon. Justice David Doyle
Heard:	17 and 18 May 2023
Draft Judgment Circulated:	30 June 2023
Judgment delivered:	7 July 2023

HEADNOTE

Directions to liquidators in respect of whether shareholders may in principle assert claims against the Company for damages for misrepresentation in relation to their subscription for shares in the Company and how such claims rank in the liquidation of the Company; House of Lords decision in Houldsworth abandoned by Parliament not followed; the effect of English precedent in Cayman Islands law; circumstances in which a Cayman court may decline to follow English precedent

INDEX

JUDGMENT

Introduction

1. Martin Trott and Christopher Smith of R & H Restructuring (Cayman) Ltd, the joint official liquidators of HQP Corporation Limited (in official liquidation) (the "Company"), (the "Liquidators") by way of a Summons dated 11 November 2022 (the "Application") seek directions from the Court on 3 issues:

   (1) the treatment of share redemption requests made pursuant to the Company's articles and in particular, whether putatively redeeming Preferred Shareholders remain members or become creditors in respect of their unpaid redemption proceeds ("Issue 1");

   (2) whether the Preferred Shareholders may in principle assert claims against the Company for damages for misrepresentation in relation to their subscription for shares in the Company ("Issue 2"); and

   (3) to the extent misrepresentation claims are available to the Preferred Shareholders, how such claims rank in the liquidation of the Company ("Issue 3").

Thanks

2. The Court was greatly assisted by the parties and their legal representatives and I place on record my thanks, in order of appearance, to Tom Smith KC for the Liquidators, Robert Levy KC for DCM Ventures China Fund (DCM VIII), L.P., DCM VIII, L.P, DCM Affiliates Fund VIII, L.P., and Jencap Helmet (the "Petitioners") and Richard Millett KC for Access Industries Holdings ("Access") and AI Autoparts LLC ("AI") and the respective legal teams. It was a real pleasure and privilege to be subjected to their considerable written and oral advocacy skills. I should also thank them for the good, helpful and constructive spirit within which the hearing was conducted. All 3 leaders are a great credit to the legal profession and a fine example to all attorneys of how to assist the court as responsible officers of the court.

Issue 1 – do the putatively redeeming Preferred Shareholders remain members or become creditors in respect of their unpaid redemption proceeds?

3. In respect of Issue 1, I am content to provide a direction that the Liquidators may proceed with the conduct of the liquidation on the basis that the Preferred Shareholders (as such term is defined in the third affidavit of Christopher Smith sworn in support of the Application (the "Preferred Shareholders")) who submitted redemption requests between 17 February 2021 and 2 July 2021 remain unredeemed shareholders of the Company in respect of the relevant instrument which was the subject of the redemption request.

4. Ultimately the direction in respect of Issue 1 was agreed between the parties but counsel recognised the Court nevertheless needed to be satisfied that it was a proper direction to make. I am so satisfied on the particular facts, on the proper construction of the Articles, in this case. Mr Millett puts the position with admirable clarity and conciseness in his skeleton argument dated 9 May 2023. On the proper construction of the Company's Articles (in particular Schedule A thereto) this is not a case (such as *Culross Global SPC v Strategic Turnaround Master Partnership Ltd* 2010 (2) CILR 364 or *Re Herald Fund SPC* 2016 (2) CILR 330 (CICA); 2017 (2) CILR 75 (PC)) where it was possible under the Articles for a redeemer to be fully redeemed (and so cease to be a member) yet remain unpaid and become a creditor for the redemption price. On the contrary, until payment of the redemption price, the redeeming shareholder remains a member: redemption only occurs upon payment by the Company. As Lord Mance, delivering the judgment of the Board in *Herald* pointed out at paragraph [15], the moment when redemption occurs, and when the prior shareholding interest is extinguished or acquired is a moment which can be defined and shaped by the articles.

Issue 2 – may the Preferred Shareholders in principle assert claims against the Company for damages for misrepresentation in relation to their subscription for shares in the Company?

5. Issue 2 was hotly contested and raised the fundamental issue as to the impact of authorities from other jurisdictions especially England and Wales on the law of the Cayman Islands.

Stare decisis*, *ratio decidendi* and *obiter dicta

6. Before turning to the impact of English precedent on the law of the Cayman Islands we should briefly consider the position of *stare decisis*, *ratio decidendi* and *obiter dicta* which are important subjects in common law jurisdictions.

7. Going back to basics it must be remembered that it is only the *ratio decidendi* of an authority that is strictly binding in the relevant jurisdiction, but well-reasoned high level *obiter dicta* may be persuasive. A.T.H. Smith in *Glanville Williams: Learning the Law* (Fifteenth Edition) in respect of the position under English law stated at page 95:

> "English courts are obliged to follow previous decisions of English courts within more or less well-developed limits. This is called the doctrine of precedent [or *stare decisis;* let decided things stand]. The part of a case that is said to possess authority is the *ratio decidendi*, that is to say, the rule of law upon which the decision is founded."

8. At pages 105-106 the following is added:

> "In contrast with the *ratio decidendi* is the *obiter dictum*. The latter is a mere saying "by the way", a chance remark, which is not binding upon future courts, though it may be respected according to the reputation of the judge, the eminence of the court, and the circumstances in which it came to be pronounced … The reason for not regarding an *obiter dictum* as binding is that it was probably made without a full consideration of the cases on the point, and that, if very broad in its terms, it was probably made without a full consideration of all the consequences that may follow from it; alternatively the judge may not have expressed a concluded opinion."

9. Garner in *The Law of Judicial Precedent* (Thomson Reuters 2016) ("Garner") deals with the distinction between *ratio decidendi* and *obiter dicta* at page 44:

"The *Holding* [ratio decidendi] of an appellant court constitutes the precedent, as a point necessarily decided. *Dicta* do not: they are merely remarks made in the course of a decision but not essential to the reasoning behind that decision".

10. Sir Christopher Clarke, the President of the Court of Appeal of Bermuda in *The Corporation of Hamilton v The Attorney General* [2022] CA (Bda) Civ 6, stated:

> "90. It is sometimes suggested (and was suggested by Mr Myers) that the question whether a decision on an issue forms part of the *ratio* depends on whether the decision was necessary in order to produce the result which the Court reached. In my judgment this is too simplistic a view."

And added:

> "91. In order to decide what was the *ratio* of any decision it is necessary, in my view, to examine the route which the Court took in order to see whether the point in issue was an essential part of the Court's reasoning."

11. Neil Duxbury in *The Nature and Authority of Precedent* (Cambridge University Press 2008) ("Duxbury") at pages 12-13 states:

> "… precedents set by courts do not merely claim the attention of, but actually *bind*, other courts. This is the doctrine of *stare decisis* – i.e., earlier judicial decisions must be followed when the same points arise again in litigation."

12. Duxbury at pages 113 – 116 deals with the topic of "Distinguishing" and the following are extracts from his treatment of the subject:

> "'Distinguishing' is what judges do when they make a distinction between one case and another … we distinguish within as well as between cases. Distinguishing within a case is primarily a matter of differentiating the *ratio decidendi* from *obiter dicta* – separating the facts which are materially relevant from those which are irrelevant to a decision.

> Distinguishing between cases is first and foremost a matter of demonstrating factual differences between the earlier and the instant case – of showing that the *ratio* of a precedent does not satisfactorily apply to the case at hand [page 113] …
>
> Most courts will distinguish cases fairly routinely and without controversy … courts are not only drawing a distinction but also arguing that the distinction is material, that it provides a justification for not following the precedent. Not just any old difference provides such a justification: the distinction must be such that it provides a sufficiently convincing reason for declining to follow a previous decision … The judge who tries to distinguish cases on the basis of materially irrelevant facts is likely to be easily found out. Lawyers and other judges who have reason to scrutinize his effort will probably have no trouble showing it to be the initiative of someone who is careless or dishonest, and so his reputation might be damaged and his decision appealed. That judges have the power to distinguish does not mean they can flout precedent whenever it suits them …" [page 114]

13. Cross and Harris in *Precedent in English Law* (Fourth Edition, Clarendon Press, Oxford 1991) ("Cross and Harris") at page 3 state:

> "It is a basic principle of the administration of justice that like cases should be decided alike."

14. Garner refers to the nature and authority of judicial precedents at page 21 with the following introductory words:

> "1. Treating Like Cases Alike
>
> Like cases should be decided alike. Following established precedents helps keep the law settled, furthers the rule of law, and promotes both consistency and predictability."

15. The legal system of the Cayman Islands is a common law system based on case-law. Cross and Harris at pages 3-4 state:

> "In a system based on case-law, a judge in a subsequent case *must* have regard to those matters; they are not, as in some other legal systems, merely material which he *may* take into consideration in coming to his decision."

16. Elizabeth W. Davies' *The Legal System of the Cayman Islands* (Law Reports International, Oxford 1989), in a section dealing with "Judicial Precedent" starting at page 188 (not 138 as specified in the Index), states:

> "It has been observed that the development of the Cayman Islands legal system is, in many respects, similar to that of the English legal system. One area in which similarity is present is the importance of the doctrine of judicial precedent. This doctrine applies equally to law in these Islands (albeit in a form modified to suit the courts in this jurisdiction) as it does to law in England."

17. At page 193 the author states:

> "Difficulties do arise, however, when major reform takes place in England but is not taken up in the Islands."

18. Lord Neuberger and Lord Reed in *International Energy Group Ltd v Zurich Insurance plc* [2016] AC 509, in the complex field of mesothelioma claims, stated:

> "209 In conclusion, it seems to us that it is at least worth considering what lessons can be learnt from the history summarised in this judgment and more fully treated by Lord Mance and Lord Sumption JJSC. There is often much to be said for the courts developing the common law to achieve what appears to be a just result in a particular type of case, even though it involves departing from established common law principles. Indeed, it can be said with force that that precisely reflects the genius of the common law, namely its ability to develop and adapt with the benefit of experience. However, in some types of case, it is better for the courts to accept that common law principle precludes a fair result, and to say so, on the basis that it is then up to Parliament (often with the assistance of the Law Commission) to sort the law out. In particular, the courts need to recognise that, unlike

Parliament, they cannot legislate in the public interest for special cases, and they risk sowing confusion in the common law if they attempt to do so.

210 When the issue is potentially wide ranging with significant and unforeseeable (especially known unknown) implications, judges may be well advised to conclude that the legislature should be better able than the courts to deal with the matter in a comprehensive and coherent way. It can fairly be said that the problem for the courts in taking such a course is that the judges cannot be sure whether Parliament will act to remedy what the courts may regard as an injustice. The answer to that may be for the courts to make it clear that they are giving Parliament the opportunity to legislate, and, if it does not do so, the courts may then reconsider their reluctance to develop the common law. For the courts to develop the law on a case-by-case basis, pragmatically but without any clear basis in principle, as each decision leads to a new set of problems requiring resolution at the highest level, as has happened in relation to mesothelioma claims, is not satisfactory either in terms of legal certainty or in terms of public time and money."

19. Lord Mance at paragraph 27 stated "The United Kingdom Parliament's reaction was its right, but does not alter the common law position apart from statute, or have any necessary effect in jurisdictions where the common law position has not been statutorily modified."

20. In *Willers v Joyce* [2018] AC 843 Lord Neuberger stated at paragraph 12 that "the JCPC should regard itself as bound by any decision of the House of Lords or the Supreme Court – at least when applying the law of England and Wales. That last qualification is important: in some JCPC jurisdictions, the applicable common law is that of England and Wales, whereas in other JCPC jurisdictions, the common law is local common law, which will often be, but is by no means always necessarily, identical to that of England and Wales."

21. In *Broad Idea International Ltd v Convoy Collateral Ltd* [2021] UKPC 24 Lord Leggatt (with whom Lord Briggs, Lord Sales and Lord Hamblen agreed) at paragraph 67 stated:

"The common law does not operate on the principle of third time lucky. On the contrary, at its core is the doctrine of stare decisis, meaning "stand by what has been decided". That

doctrine remains as essential as ever to securing stability, consistency and predictability in the common law. The Board has never acted on a strict rule that it is bound by its own previous decisions, nor those of the House of Lords or Supreme Court; but the Board will not depart from a previous decision of its own or of the House of Lords or Supreme Court without compelling reason to do so: see Lord Mance and J Turner, *Privy Council Practice* (2017), paras 5.07 – 5.21 and the cases there cited."

22. There is no doubt that English law and procedure has had and continues to have an important influence on the law and procedure of the Cayman Islands. See, for prime examples, section 11 (1) (like jurisdiction of His Majesty's High Court) and section 18 (jurisdiction to be exercised in accordance with the Rules but English practice to apply where no other provision made so far as "local circumstances permit" and any directions of the court) of the Grand Court Act (as revised). This is also illustrated by reference to Order 1, rule 5 (2) of the Grand Court Rules ("GCR") which provides that the Supreme Court Practice 1999 of England and Wales may be relied upon where appropriate as an aid to the interpretation and application of the GCR. In *Maples FS Limited v B&B Protector Services Limited and others* (Unreported, FSD 213 of 2021 (DDJ),14 July 2022) I stated:

> "25. … I think it sensible and appropriate also to have regard to subsequent editions of the English White Book and the developing case law in Cayman and other sophisticated common law jurisdictions throughout the world including England and Wales."

23. Where the English and Cayman statutory provisions or procedural rules are the same or substantially similar, of course, it makes sense to have regard to the English case law on the relevant statutory provision or procedural rule and to treat it, depending on the circumstances of the case, as a useful precedent.

English precedent in Cayman Islands law

24. Very little local precedent dealing with English precedent in Cayman Islands law was brought to my attention despite the importance of this subject to Issue 2. I gently touched upon the impact of

English precedent in Cayman Islands law, without receiving the benefit of argument from counsel, in *Arnage v Walkers* (Unreported, FSD 105 of 2014 (DDJ), 5 May 2021) at paragraphs 49 – 52:

> "49. It is important however to emphasise that English authorities are, of course, not binding in courts in the Cayman Islands but depending on the context and the issue under consideration English authorities, especially at appellate level, may be persuasive and in some cases highly persuasive. In considering the impact of English authorities regard must always be had to local circumstances.
>
> 50. In respect of the weight to be attached to judgments of the English Court of Appeal, Zacca P in *Miller v R* 1998 CILR 161 at 164 sets out the position of the Court of Appeal of the Cayman Islands as follows, albeit in the context of a criminal appeal:
>
> > "A decision of the English Court of Appeal, while not formally binding upon this court automatically, is necessarily one of great persuasive authority, specifically where it is unanimous and is directed towards a doctrine of the common law."
>
> 51. Sanderson J in *National Trust for Cayman Islands v Planning Appeals Tribunal* 2002 CILR 59 at 66 para 19 referred to *Miller* stating that in such appeal, the Court of Appeal acknowledged that "unanimous decisions of the English Court of Appeal are strong persuasive authority locally but not binding authority." Sanderson J referred to *de Lasala v de Lasala* [1980] A.C. 546 an authority in the Judicial Committee of the Privy Council in an appeal from Hong Kong adding, "the Privy Council stated that on questions of common law, a decision of the House of Lords was of very great persuasive authority locally because of the common membership of those courts. However, it stated that this principle does not apply where circumstances locally make it inappropriate to develop a field of common law in a manner similar to England."

52. The Privy Council also referred to *de Lasala* in *Frankland v R* 1987-89 MLR 65 at 80 where Lord Ackner, delivering the judgment of the Board, stated:

> "Decisions of the English courts, particularly decisions of the House of Lords and the Court of Appeal in England, are not binding on Manx courts, but they are of high persuasive authority… Such decisions should generally be followed unless either there is some provision to the contrary, or, exceptionally, there is some (sic) good reason for not following the particular English decision. The persuasive effect of a judgment of the House of Lords, which has largely the same composition of the Judicial Committee of the Privy Council, the final Court of Appeal from a Manx court, is bound to be very high."

25. Paragraph 52 contains a typographical error. Before the words "good reason" the words "some local condition which would give" should be inserted.

26. I also brought to counsel's attention the Cayman Islands Court of Appeal judgment in *Schramm v Financial Secretary, Registrar of Companies* 2004-05 CILR 104. In that case the Court of Appeal was invited by counsel for the appellant to disapprove of the decisions of the English Court of Appeal in the cases of *In re Pinto Silver Mining Co.* (1878) 8 Ch D 273 and *In re London & Caledonian Marine Ins. Co.* (1879) 11 Ch. D 140. Collett JA declined to accept such invitation stating at paragraph 9 of the judgment delivered on 5 August 2004:

> "Quite apart from the respect which this court pays to the decisions of established courts of similar jurisdiction in the Commonwealth, it was pointed out to us that the decisions in question were subsequently approved by the House of Lords in *Russian & English Bank v Baring Brothers & Co Ltd* [[1936] A.C. 405]. It is rarely, if ever, that a court at this level fails to follow a line of authority so established. We are not prepared to do so in this case since there is no compelling reasons for us to do so." (My underlining.)

27. Without throwing the last sentence out of all reasonable proportion and attaching too much weight to it, it does appear implicit in that sentence that the Cayman Islands Court of Appeal would decline to follow a decision of the House of Lords (now the Supreme Court of the United Kingdom) if there was a "compelling reason" for them to do so.

28. Part of the headnote to the report of the judgment of the Cayman Islands Court of Appeal (Robinson, P., Kerr and Carberry, JJA) in *Smith v Commissioner of Police* 1980 – 83 CILR 126 reads as follows:

> "(5) In reaching this conclusion, the court was entitled to disregard a previous decision of the Judicial Committee of the Privy Council which had held that a licence was merely a privilege which could be revoked without observing the rules of natural justice and that certiorari did not lie against a licensing authority in such circumstances. Although in subsequent cases this decision had been heavily criticised – its effect had been limited to its special facts and it was no longer considered to be good law – the court was not entitled to depart from it for these reasons alone, since it was bound to follow every part of the *ratio decidendi* of a decision of the Judicial Committee. There were, however, other decisions of the Judicial Committee in which the *rationes decidendi* conflicted with that in the earlier case without actually overruling it. In these circumstances the court was entitled to choose to follow whichever decision it found the more convincing – and it could therefore choose not to follow the earlier decision (page 169, line 41 – page 170, line 18; page 177, lines 18-39; page 178, lines 15-30)."

29. In *Smith* the Cayman Islands Court of Appeal considered authorities from England, Ceylon, Australia, Canada and New Zealand and at page 178 preferred to follow an Australian High Court authority (*Banks v Transport Regulation Bd (Victoria)* (1968) 119 CLR) rather than the Privy Council case of *Nakkuda Ali v Jayarantne* [1951] AC 66. Carberry JA delivering the judgment of the court prayed in aid the following comments of Lord Diplock in *Baker v R* [1975] AC 744 at 788:

> "Strictly speaking the per incuriam rule as such, while it justifies a court which is bound by precedent in refusing to follow one of its own previous decisions (*Young v. Bristol Aeroplane Co. Ltd.* [1944] K.B. 718), does not apply to decisions of courts of appellate jurisdiction superior to that of the court in which the rule is sought to be invoked: *Broome v. Cassell & Co. Ltd* [1972] A.C. 1027. To permit this use of the per incuriam rule would open the door to disregard of precedent by the court of inferior jurisdiction by the simple device of holding that decisions of superior courts with which it disagreed must have been given per incuriam."

30. In *Omni Securities Limited v Deloitte and Touche* 2000 CILR 102, Collett JA at page 111 (with whom Zacca P and Georges JA concurred), stated:

> "The concept of a "shadow director" is a creature of UK statute which appears to have first seen the light of day in 1917. There has been no authority cited to us which so much as hints at its existence in the common law of England before that date. That same concept is conspicuously absent from the Cayman statutes, and since English common law was received into these Islands not later than 1865, there can be no room to discover its existence in Cayman law at all. There is, of course, no Cayman common law as distinct from the common law of England received into the dependency when these Islands were deemed first settled. The suggestion to the contrary made in the plaintiff's skeleton argument is thus untenable."

31. The Court of Appeal of Jamaica (Duffus Ag P, Lewis JA and Moody Ag JA) in *Levy v Administrator of the Cayman Islands* 1952-79 CILR 42 on 23 April 1963 dealt with arguments as to the introduction of the common law of England into the Cayman Islands by the original settlers. Duffus Ag P, at page 46 stated:

> "I am satisfied that the Cayman Islands must be regarded as settled territory, and that the persons who settled in the Cayman Islands must be deemed to have taken with them to the

> Cayman Islands the common law of England when they first settled here in the early 17th Century …"

Levy was applied by Chief Justice Summerfield in *Eden v R* 1952-79 CILR 406 who at page 414 stated, "[t]hat is the position today [29 October 1979] subject to any statute."

32. The helpful subject matter index of the Cayman Islands Law Reports 1952-2000 contains 4 pages of cases under the heading – "Jurisprudence – Reception of English Law", mainly in respect of practice and procedure. See for example *Re Inco Bank & Trust Corp* 1994 – 95 CILR 99 (Smellie J as he then was) in respect of the status of the English winding up rules in the Cayman Islands.

33. More recently, Kawaley J in *Arcelormittal North American Holdings LLC v Essar Global Fund Limited* (Unreported, FSD 2 of 2019, 16 November 2021) at paragraph 43, in the context of the *Norwich Pharmacal* jurisdiction, stated:

> "The English High Court's inherent jurisdiction and current practice is available to fill any gaps in the local statutes and rules. The converse also applies. English practice must be read subject to relevant local statutes and rules."

34. Kawaley J in *Dell v Smickle* (Unreported, Probate and Administration, 129 of 2019, 5 October 2021) at paragraph 9, in the context of the granting of letters of administration, stated:

> "Care must obviously be taken when applying English statutory provisions as a gap-filling measure, in the probate context, to ensure that one does not subvert the primacy of the Succession Act and Cayman Islands law. In *Uzzell*, section 42 was applied to incorporate not a minor and context-laden provision of English; rather a broad jurisdictional provision was applied, consistent with the notion that this Court's general jurisdiction corresponds to that of the English High Court by virtue of section 11 of the Grand Court Law."

At paragraph 19 Kawaley J referred to section 42 of the Succession Act which "provides that where any matter is not provided for, English law and practice shall "*so far as local circumstances permit*" apply."

35. In *Perry v Lopag* (Unreported, CICA 16 of 2020 (Formerly FSD 205 of 2017 (NSJ)), 11 November 2021 and with errata 19 November 2021) Sir Jack Beatson JA (with whom President Sir John Goldring and Sir Richard Field JA agreed) at paragraph 77 stated:

> "A question of foreign law is treated as a question of fact to be proved in English law and in Cayman law by the evidence of suitably qualified experts in the relevant foreign law. It is common ground that in the absence of any Cayman authority on the approach to an appeal against a finding as to foreign law by the trial judge this court should adopt the approach in the English authorities."

36. Lord Lloyd-Jones in *Ramoon v Governor of the Cayman Islands* [2023] UKPC 9 at paragraph 51 stated:

> "… The decision of the Supreme Court in *Al Rawi* is, of course, not binding on the Judicial Committee of the Privy Council sitting on appeal from the Court of Appeal of the Cayman Islands. Nevertheless, *Al Rawi* possesses the authority of a decision of the Supreme Court comprising eight justices. (Lord Rodger of Earlsferry who had sat on the hearing of the appeal died before judgment was given.) Moreover, the Board finds the reasoning of Lord Dyson compelling. In the Board's view, it is simply not open to it to invent a CMP [closed material procedure] for the Cayman Islands under the guise of the development of the common law. This would be considerably more than an incremental development. It would be a major change involving an inroad into fundamental common law rights. Such a step should be taken, if at all, by the legislature which is better placed than is the judiciary to assess the policy considerations relating to the necessity for such a procedure and the practicalities of its operation. It would also be open to the legislature to define with

precision the scope of the exception and to make detailed procedural rules to regulate the procedure." (My underlining.)

37. Because of the lack of detailed jurisprudence in the Cayman Islands in respect of the position of English precedent in Cayman it may be helpful to look at other relatively compact common law jurisdictions to see how they treat English precedent.

38. Before I undertake that exercise I record that I take account of the wise words of Assistant Justice Kawaley sitting as a judge in Bermuda in his 471 page judgment in *Wong v Grand View Private Trust Company Limited and others* [2022] SC (Bda) Com (22 June 2022). In that case Assistant Justice Kawaley was considering the reception of English law which at paragraph 867 he said occurred in two principal ways "at common law or by statute". At paragraph 904 Assistant Justice Kawaley stated:

> "Reception is ultimately a jurisdiction-specific process so authorities from other jurisdictions are only really helpful to the extent that they elucidate the general judicial approach to the question."

English precedent in the Isle of Man

39. In *Frankland v R* 1978-80 MLR 275 the Appeal Division of the Isle of Man High Court (Glidewell JA and Brown, Acting JA) referred to *de Lasala* and at page 291 stated:

> "…The correct principle in our view is that decisions of English courts, particularly the House of Lords and the Court of Appeal are persuasive in the Manx courts but not binding. They should, however, generally be followed unless either there is something to the contrary in a Manx statute or there is some clear decision of a Manx court to the contrary, or exceptionally, there is some local condition which would give good reason for not following the particular English decision. When one comes to consider the persuasive effect of English decisions, the persuasive effect of a judgment of the House of Lords which

has, of course, largely the same composition of the Judicial Committee of the Privy Council which is a Manx court – the highest court of this Island – is obviously very considerable."

40. Glidewell JA delivering the judgment of the court at page 292 stated that Privy Council decisions from the Isle of Man are binding on Manx courts. Referring to *de Lasala,* he stated:

> "I said a moment ago that that decision itself was binding on us, strictly that is not correct, because that is an appeal from Hong Kong and not from the Isle of Man. It could only be when it was an appeal from the Isle of Man that it strictly could be binding upon us, but it is clearly of even more persuasive authority since it is the Judicial Committee of the Privy Council than is a decision of the House of Lords."

41. The Privy Council (1987-89 MLR 65 at page 80) stated that Glidewell JA had correctly pointed out the position in respect of decisions of the English courts in the Manx courts and at pages 81 and 82 added:

> "Glidewell, J.A. correctly took the view that there was nothing in local conditions, much less in local statutes, that should lead the court to the view that the objective test as laid down in *D.P.P. v. Smith* was not the common law of England and therefore the law of the Isle of Man until Tynwald enacted the contrary in 1983. In reaching this conclusion, he expressed his awareness of the criticisms, particularly by academic writers, of *D.P.P. v. Smith*. It does not appear, however, that the learned Judge of Appeal's attention was drawn to Lord Diplock's clear view expressed in *Hyam v. D.P.P.* (4) that the decision was erroneous and how that error came to be made, following in this regard the observations of Byrne, J. when giving the judgment of the Court of Criminal Appeal in *D.P.P. v. Smith*, which their lordships have quoted. Moreover, Glidewell, J.A. did not have the benefit of the very recent observations made by Lord Bridge in his speech in *R. v. Moloney* (7) which their lordships have set out above, and those of Lord Scarman in his speech in *R. v. Hancock* (6) also quoted.

> Their lordships, having had the benefit of extended argument, and particularly in the light of the recent cases, have concluded that the decision in *D.P.P. v. Smith*, insofar as it laid down an objective test of the intent in the crime of murder, did not accurately represent the English common law. It therefore follows that the trial judges in both trials were in error in directing the jury that they were entitled to ascertain the intent of the accused by reference to an objective test."

42. In effect the Privy Council was saying that there was nothing in local statutes, local conditions or academic criticism that would have justified the Manx court in not following the objective test in *DPP v Smith*. However, noting that senior English judges (Lords Diplock, Bridge and Scarman) had commented adversely on *DPP v Smith,* the Privy Council in effect held that the decision in *DPP v Smith,* insofar as it laid down an objective test of intent in the crime of murder, did not accurately represent the English common law.

43. The Appeal Division of the Isle of Man (Deemster Luft and Hytner JA) in *Pate v R* 1981 – 84 MLR 130 dealt with the issue of provocation in Manx law. In England, Parliament had intervened by way of the Homicide Act 1957 but Tynwald, the Manx Parliament, had not followed suit. The success of the appellant's submissions depended "in part upon the view this court takes of the extent to which English authorities decided after 1957 … apply in the Isle of Man, and in part on the view we take of the true application of the authorities prior to that date … Unless there are strong reasons for not doing so, this court will follow decisions of the House of Lords and the English Court of Appeal. One strong reason for not following decisions of those courts would be different local conditions in the Isle of Man."

44. Judge of Appeal Hytner (who served the Isle of Man in that capacity for some 17 years) referred to the House of Lords' decision in *Bedder v DPP* [1954] 1 WLR 1119 describing it as "much criticised" and declined to follow it. Reference was made to the words of Lord Simon in *R v Camplin* [1978] 2 ALL ER 168 at 179 that "some of its implications constitute affronts to common sense and justice." Hytner JA at page 139 of *Pate* stated:

> "Where a decision of the House of Lords or the English Court of Appeal can be said to affront common sense and any sense of justice that, in our view, constitutes a sufficient special circumstance to warrant this court refusing to follow it." (My underlining.)

45. In respect of the Manx test laid down by the Privy Council in *Frankland*, I should for the sake of completeness refer to a couple of subsequent Manx judgments. The Appeal Division of the Isle of Man (Deemster Kerruish and Tattersall JA) in *Dominator Limited v Gilberson SL* 2009 MLR 161 referred to what they described as dicta in the *Frankland* case in respect of following English decisions and stated:

> "92. For the purposes of this appeal it is unnecessary for this court to express any view as to whether or not such dicta have the same force today as they had over 20 years ago. However, even without the benefit of full argument on such issue, we are bound to express some doubt whether they do so in the context of a jurisdiction which is becoming increasingly independent of English statutes and procedure and is frequently choosing to be informed by or to adopt the common law and practices found in jurisdictions other than England.
>
> 93. Similarly it may be that this court's decision in *In the matter of the Petition of Cussons* [2001-03] MLR 539, at 548, where this court stated:
>
> > 'The correct approach seems to us to be to establish the English precedent … and to follow that precedent unless there is any jurisdiction to depart from it in line with *Frankland v R.*'
>
> will need at some stage to be reconsidered."

46. The Appeal Division (Deemster Doyle, Tattersall JA and Deemster Corlett) in *R v Hamblett* 2013 MLR 385 in a judgment delivered on 12 September 2013 referred to *Dominator* at paragraph 39 and at paragraph 40 added:

> "In the past this court has frequently emphasised that local conditions may justify a different approach to that adopted in England and Wales … Moreover in *Invercargill City Council v Hamlin* [1996], ALL ER 756, [1996] AC 624 the Privy Council expressly held that the New Zealand Court of Appeal was entitled to develop the common law of New Zealand in areas of the common law which were developing and not settled." (My underlining.)

47. It may also be of interest to note that Judge of Appeal Hytner sitting in the Appeal Division of the Isle of Man in *Barr and Anglo International Holdings Limited* 1990-92 MLR 398 at 409, in the context of contempt of court, stated:

> "Since this court is not in any event bound by decisions of the English courts, it should not be assumed that we would follow dicta abandoned by Parliament." (My underlining.)

48. At page 410 the appeal judge, having reviewed some of the relevant authorities, added:

> "We are, therefore, satisfied that such part of the English common law as has been preserved by Parliament represents the Manx common law."

49. In *Bitel v Kyrgyz Mobil* (unreported judgment of the High Court of the Isle of Man delivered on 30 November 2007) in my capacity as a Deemster at first instance I stated:

> "535. Judge of Appeal Hytner in *Barr and Anglo International Holdings Limited* 1990-92 MLR 398 at page 409 stated:
>
> > "Since this court is not in any way bound by decisions of the English courts it should not be assumed that we would follow dicta abandoned by Parliament."
>
> 536. In *City and International Securities Limited* 2001-03 MLR 239 Deemster Cain had little difficulty in not following the majority judgments in *Home Office v Harman* [1983]

A.C. 280 (House of Lords) which had been challenged before the European Commission of Human Rights.

537. In *Aguilar v Anglican Windows (IOM) Limited* 1987-89 MLR 317 at 325 an advocate endeavoured to persuade Deemster Corrin not to follow the Privy Council decision in *Selvanayagam v University of West Indies* on the grounds that it had been the subject of criticism and that their Lordships had confused remoteness and mitigation. Deemster Corrin at page 325 stated that the decision "is, nevertheless, a decision of the Privy Council and, if not actually binding, is very persuasive authority in this court, and I propose to follow it."

538. Deemster Corrin in *Cusack, Cotter v Scroop Limited* (judgment 16th January 1997) stated at page 9:

> "The Isle of Man is an active member of the Commonwealth and whilst historically it has tended to follow English law I feel quite free to look for guidance to other Commonwealth countries as there is no binding or persuasive authority to the contrary in England."

539. The High Court of Australia in *Cook v Cook* (1986) 162 CLR 376 at 390 stated:

> "... the history of the country and of the common law makes it inevitable and desirable that the courts of this country will continue to obtain assistance and guidance from the learning and reasoning of United Kingdom courts just as Australian courts benefit from the learning and reasoning of other great common law courts."

540. Thanks in the main to Deemster William Cain and to Dr Alan Milner of Law Reports International the Island has had an excellent system of local law reporting for some many years now. Increasingly it is to our own local judgments that we are turning in dealing with the legal issues of the day.

> 541. In addition to applying our own local precedents Manx courts will also continue to benefit from the learning and reasoning of judgments of the English courts and "other great common law courts" including the High Court of Australia."

50. Deemster Cain in *Re City and International Securities Limited* 2001-03 MLR 239 declined to follow the majority judgments of the House of Lords in *Home Office v Harman* [1983] AC 280 (as challenged before the European Commission on Human Rights and amicably settled with procedural rules in England being subsequently changed) and considered the proper course for the Manx courts was to follow the minority judgments, stating at paragraph 15:

> "Decisions of the House of Lords are not binding on this court, although they will generally be followed … I consider that this is one of those exceptional cases where this court should not follow a decision of the House of Lords. I therefore hold that it is not a contempt of court to publish documents which have been read aloud in open court."

51. Following Deemster Cain's lead I decided in *Barclays Private Clients International Limited* 2016 MLR Note 13 (judgment dated 17 August 2016) at paragraph 34 of the judgment not to follow the majority speeches in the House of Lords in the English case of *Nokes v Doncaster Amalgamated Collieries Ltd* [1940] AC 101 which concerned employment contracts in a bygone age, preferring to follow the powerful dissenting judgment of Lord Romer. I also noted at paragraph 36 the changed regulatory environment and that the effect of *Nokes* in English law had been overturned by subsequent legislation in the United Kingdom.

52. Certainty is also important. At page 40 of Ramsey B Moore's *Isle of Man and International Law* (1926) the learned Attorney refers to the words of Deemster Callow in 1911 in the case of *Goldsmith* that not to follow the English rule laid down in *Fletcher v Ashburner* and adopt a more equitable practice would "involve endless confusion, and would be to the prejudice of the Manx courts and legal profession. No one would know where they stood" and adds:

> "English decisions have always been accepted in the Isle of Man in the absence of local laws to the contrary, to the great advantage and uniformity of legal practice. But the Manx courts have never felt themselves bound to slavishly adhere to these principles".

53. Deemster Corlett in *Kaupthing Singer & Friedlander (Isle of Man) Limited (in liquidation)* 2017 MLR 151 in a judgment delivered on 16 June 2017 stated at paragraph 56:

> "In summary I do not consider it appropriate to follow the English line of authority, particularly bearing in mind that the decisions arrived at appear to have been substantially dictated by a legislative history which the Isle of Man does not share. None of those authorities is in any event binding upon me. I am therefore free to choose a path which best reflects my view of the fairness (or relative unfairness) of the situation and which best promotes the policy set out by Tynwald in the law of insolvency in respect of which I am unable to see why there should be any discernible difference in result as between individual bankruptcy and corporate insolvency."

English precedent in Jersey

54. I turn now to an important judgment of the Court of Appeal of Jersey (James McNeill KC, Sir William Bailhache and Jeremy Storey KC) in *Energy Investments Global Limited v Albion Energy Limited* [2020] JCA 258. Bailhache JA, giving the judgment of the Court, stated:

> "36. The Respondent relies on the dictum of Lord Guest in Carl Zeiss Stiftung v Rayner and Keeler Limited (No 2) [1967] 1 AC 853 HL, where at p938 paragraphs A-C, he said:-
>
> > "In the case of [an English judgment] the cause of action is merged with the judgment… Not so in the case of foreign judgments… The plaintiff, therefore, has the option either of suing on the judgment or on the original cause of action. The doctrine of non-merger… is still, as I understand it, good law."
>
> 37. Advocate Hoy submitted that this was the English rule until the 1982 Act [Civil Jurisdiction and Judgments Act]. A statute which did not apply here would not change the position and thus it followed that if we were to apply the English common law doctrine of merger in the island, we should apply the whole of it. In

effect, what the Respondent is inviting us to do is to declare the law of Jersey, in this respect so far in a state of uncertainty because there is no previous authority on the point, to be the same as the common law of England before 1982 in circumstances where, by statute that year, Parliament has decreed that the English common law be abrogated. In our judgment this would be both inappropriate and unnecessary. It is not the position that English common law provides any form of binding precedent in Jersey. Different expressions have been used in the courts from time to time to describe the nature of the doctrine of precedent in Jersey, but one thing which is certain is that nowhere in modern practice is there to be found any statement that decisions of the English courts are binding in the island. It is accordingly not the case that the court is obliged to apply the English common law rule. Nor, obviously, it is the case that the courts of this island are required to apply an Act of Parliament which changed the position in England but which does not apply to us here. Neither the English common law nor the inapplicable statute have any binding force in this jurisdiction. They are not of themselves precedents which we are required to follow.

38. The consequence is that we need to examine this issue, not from the perspective of English decisions of previous centuries nor from the perspective of what Parliament has ordained for England and Wales, but instead from the perspective of what is right as a matter of principle. In that limited context, we can have regard to the fact that Parliament has abrogated the common law rule, although for the reason given that is not conclusive." (My underlining.)

55. Sir Michael Birt, sitting as a Commissioner in Jersey in *The Attorney General v K* [2016] JRC 158, in the context of sentencing guidelines in criminal cases, at paragraph 67 stated:

"67. We would add that even if, contrary to our view, Da Graca is to be treated as a guideline case, it would, in our respectful view, be open to the Superior Number to suggest new guidelines if satisfied that there had been a compelling change of circumstance. In State of Qatar v Al Thani [1999] JLR 118 at 126, the Court considered the doctrine of precedent in this jurisdiction and held that the doctrine

of stare decisis as expounded by the English courts was not part of the law of Jersey. However, it went on to say:-

> "A hierarchical structure of courts requires that deference be accorded by lower courts to higher courts. Even in France judges of lower courts will in practice follow the decision of higher courts in most cases. This court is generally bound by the decisions of the Court of Appeal and of course, as it always has been, by the decisions of the Judicial Committee of the Privy Council sitting on appeal from the courts of this jurisdiction. We qualify the proposition only because, in our judgment, it is open to the Royal Court, as it would be to a Scottish court, to decline to follow a decision which has been invalidated by subsequent legislation or some such compelling change of circumstance."" (My underlining.)

English precedent in Guernsey

56. Let us now take a trip across the water to Guernsey. In *Morton v Paint* (1996) 21 GLJ 61 (judgment of the Guernsey Court of Appeal 9 February 1996) Blom-Cooper J at page 40 stated:

> "Accordingly, Guernsey law, in adopting the English law rules in the field of tortious liability, could properly conform to what the UK Parliament had decreed was the "eminently sensible" rule. To bring the law of Guernsey into line with the statutory rule in England, and not to allow a parting of the ways for the two jurisdictions, does not have to await enactment of a similar law by the states of Guernsey. It can be done judicially. The argument, ably advanced by Mr Wessels for the respondent, would mean the ossifying of the very organism of the common law – namely, its constant adaptability to changing social conditions. It cannot be right that the law of negligence should remain stunted in its growth so long as the state of Guernsey fails to legislate.
>
> As Lord Scarman observed in Gillick v. West Norfolk and Wisbech Area Health Authority [1986] AC 112 at p.183D:

"It is, of course, a judicial commonplace to proclaim the adaptability and flexibility of the judge-made common law. But this is more frequently proclaimed than acted on. The mark of the great judge from Coke through Mansfield to our day has been the capacity and the will to search out principle, to discard the detail appropriate (perhaps) to earlier times and to apply principle in such a way as to satisfy the needs of his own time. If judge-made law is to survive as a living and relevant body of law, we must make the effort, however inadequately, to follow the lead of the great masters of the judicial art.""

57. Southwell J on pages 59 – 60 stated:

"(5) It would not be appropriate to leave Guernsey law in the state reached by English law nearly 40 years ago, which was justly criticised as something of a blot on English jurisprudence and requiring urgent reform. For the Guernsey Courts to cling to obsolete English common law cases which ceased to be authoritative in England and Wales 39 years ago would not be in the interests of those who live in Guernsey or their visitors. It would be the more inappropriate because, as Mr Wessels accepted, it would involve clinging to such out of date cases concerning liability to lawful visitors, while adopting the more recent developments in Herrington concerning liability to trespassers, which in turn had to be superseded by statute in England and Wales because of their uncertainty.

In my judgment the weight of the argument lies on the side of development of Guernsey law by the courts, taking the principles evolved in Donoghue and Zaluzna as the basis of this development.

Accordingly, in my judgment the appeal should be allowed, and the duty of care owed by Mr Paint to Mrs Morton should be declared to be a duty to have done what a reasonable man would have done in the circumstances by way of response to the risk, in so far as foreseeable, in accordance with the Donoghue v Stevenson principles of the law of negligence." (My underlining, save for the underlined case law references.)

58. A youthful Sumption J agreed with both judgments.

59. Lord Hope in *Simon v Helmot* [2012] UKPC 5 at paragraph 6 referred to *Morton v Paint* and stated:

> "The English common law has persuasive force in Guernsey in areas not governed by Guernsey statutes or Guernsey customary law, in much the same way as it has in Scotland …"

Adding at paragraph 7:

> "This is not to say that the solutions that have been adopted in English law will be applied in Guernsey without an inquiry as to whether the underlying conditions in the respective jurisdictions are truly comparable …" (My underlining.)

60. Lord Clarke (giving the judgment of the Board) in *Spread Trustee Company Limited v Sarah Anne Hutcheson & others* [2011] UKPC 13 reassuringly showed that the Judicial Committee of the Privy Council is conscious of local sensitivities in the Crown Dependencies. At paragraph 40 he stated:

> "The Board entirely accepts that Guernsey looks to other jurisdictions for assistance in developing particular areas of the law … Guernsey law must in the end be interpreted in the light of its own terminology, context and history …"

61. I am conscious also of Lord Neuberger's comment at paragraph 13 of *Willers v Joyce* [2016] UKSC 44:

> "…the common law can develop in different ways in different jurisdictions (although it is highly desirable that all common law judges generally try and march together) …"

English precedent in Bermuda

62. In *Re First Virginia Reinsurance Ltd* [2003] Bda LR 47 Kawaley J (as he then was) sitting in Bermuda declined to follow an aspect of a first instance English authority *Re Emmadart Ltd* [1979] 1 ALL ER 599 which had been repealed by statute and not followed by a line of Australian cases. In that case, counsel submitted that *Re Emmadart Ltd* should not be followed in Bermuda for two

broad reasons. Firstly, the decision was so unsatisfactory that it had been repealed by statute; section 124(1) of the Insolvency Act 1986 (UK) expressly empowered by the directors to petition for a company's winding up. Secondly, because Australian case law had "superior reasoning which was to be preferred." Kawaley J, for the detailed and cogent reasons specified in his judgment, felt that the case against applying the *Emmadart* analysis to the case of an insolvent company was a compelling one and the reasoning in that case was "fundamentally flawed".

English precedent in Hong Kong

63. Let us now fly off to Hong Kong, another jurisdiction with which the Cayman Islands have very strong connections. Harris J, one of the leading commercial judges in Hong Kong and internationally well respected, in *Re CEFC Shanghai International Group Ltd* [2020] 1 HKLRD 676 distinguished the House of Lords decision in *Galbraith v Grimshaw* [1910] AC 508 and declined to follow it. Harris J at paragraph 19 was of the opinion that the analysis of the House of Lords in the early 20th century was "inconsistent with contemporary cross-border insolvency law and its reasoning is inapplicable to modern common law cross-border insolvency assistance". (My underlining.)

64. Harris J at paragraph 20 noted that *Galbraith v Grimshaw* had been subject to much academic criticism acknowledged by Their Lordships in *Al Sabah v Grupo Torras SA* [2005] UKPC 1; [2005] AC 333 as having "some force".

65. Harris J at paragraph 21 stated that the reasoning in *Galbraith v Grimshaw* "was in fact narrow" and concerned the rules of relation-back and a Scottish trustee and added:

> "At the time *Galbraith v Grimshaw* was determined cross-border insolvency assistance as we now understand it had not evolved."

66. Before the Hong Kong Court of Final Appeal was established the Privy Council dealt with an appeal from the Court of Appeal of Hong Kong in *Tai Hing Cotton Mill Ltd v Liu Chong Hing Bank Ltd* [1986] 1 AC 80. Lord Scarman, in the language of the 1980s, delivered Their Lordships' judgment and at page 108 stated:

> "It was suggested, though only faintly, that even if English courts are bound to follow the decision in *Macmillan's* case the Judicial Committee is not so constrained. This is a misapprehension. Once it is accepted, as in this case it is, that the applicable law is English, their Lordships of the Judicial Committee will follow a House of Lords' decision which covers the point in issue. The Judicial Committee is not the final judicial authority for the determination of English law. That is the responsibility of the House of Lords in its judicial capacity. Though the Judicial Committee enjoys a greater freedom from the binding effect of precedent than does the House of Lords, it is in no position on a question of English law to invoke the *Practice Statement (Judicial Precedent)* [1966] 1 W.L.R. 1234 of July 1966 pursuant to which the House has assumed the power to depart in certain circumstances from a previous decision of the House. And their Lordships note, in passing, the Statement's warning against the danger of disturbing retrospectively the basis on which contracts have been entered into. It is, of course, open to the Judicial Committee to depart from a House of Lords' decision in a case where, by reason of custom, statute, or for other reasons peculiar to the jurisdiction where the matter in dispute arose, the Judicial Committee is required to determine whether English law should or should not apply. Only if it be decided or accepted (as in this case) that English law is the law to be applied will the Judicial Committee consider itself bound to follow a House of Lords' decision. An illustration of the principle in operation is afforded by the recent New Zealand appeal *Hart v. O'Connor* [1985] A.C. 1000, in which the Board reversed a very learned judgment of the New Zealand Court of Appeal as to the contractual capacity of a mentally disabled person, holding that because English law applied, the duty of the New Zealand Court of Appeal was not to depart from what the Board was satisfied was the settled principle of that law." (My underlining.)

67. Lord Scarman's comments must now be read in light of *Attorney General for Hong Kong v Reid* and *Willers v Joyce*.

68. Johannes M. M. Chan in *Paths of Justice* (Hong Kong University Press 2018) at page 6:

> "We followed English law in many areas, sometimes too slavishly, without consideration of local circumstances. There are also many areas of local significance that have not been researched at all."

English precedent in New Zealand

69. We now travel to a well-known JCPC decision on an appeal from the Court of Appeal of New Zealand, namely *Attorney General for Hong Kong v Reid* [1994] 1 AC 324, to consider the historical position of English precedent in New Zealand. Lord Templeman at pages 338-339:

> "The New Zealand Court of Appeal in the present case declined to enter into the merits of *Lister & Co. v. Stubbs*, 45 CH.D. 1, founding itself on a passage in the judgment of this Board delivered by Lord Scarman in *Tai Hing Cotton Mill Ltd. v. Liu Chong Hing Bank Ltd.* [1986] A.C. 80, 108, where his Lordship said the duty of the New Zealand Court of Appeal was not to depart from a settled principle of English law. While their Lordships regard the application of stare decisis in the New Zealand Court of Appeal as a matter for that court, they desire to make the following remarks, in case Lord Scarman's comments in *Tai Hing Cotton Mill Ltd. v. Liu Chong Hing Bank Ltd.* have in any way been misunderstood.
>
> In the present case the Court of Appeal did not say and could not have meant that it was bound by a decision of the English Court of Appeal, since for many years the New Zealand courts have not regarded themselves as bound by decisions of the House of Lords, although of course continuing to pay great respect to them. The reasoning of the Court of Appeal, as their Lordships understand it, was rather that in the absence of differentiating local circumstances the court should follow a decision representing contemporary English law, leaving its correctness for consideration by this Board. Without in any way criticising that approach in the circumstances of this case, where the decision in question was of such long standing, their Lordships wish to add that nevertheless the New Zealand Court of Appeal must be free to review an English Court of Appeal authority on its merits and to depart from it if the authority is considered to be wrong. *Hart v. O'Connor* [1985] A.C. 1000 to which Lord Scarman referred in the passage mentioned by the Court of Appeal concerned

the very different situation of the Court of Appeal wishing to apply English law but, in the judgments of this Board, misapprehending the state of the contemporary law. In any case where the New Zealand Court of Appeal has to decide whether to follow an English authority, its own views on the issue, untrammelled by authority, will always be of great assistance to the Board." (My underlining.)

Summary of the position of precedent in Cayman Islands law

70. Pulling all these loose threads together I think the basic tapestry which appears before me reveals the following:

(1) the *ratio* of a judgment of the Judicial Committee of the Privy Council on an appeal from the Cayman Islands is binding on all judges of the Cayman Islands (*de Lasala* and *Frankland*);

(2) English decisions, even of the House of Lords and now the Supreme Court, are not binding on any judges in the Cayman Islands but they may be persuasive and in some cases highly persuasive (*Frankland; Ramoon*; *Energy Investments*);

(3) a judge in the Cayman Islands may decline to follow a decision of an English court even at appellate level if:

(a) there is some provision to the contrary in a statute of the Cayman Islands (*Frankland*; *Simon v Helmot*);

(b) there is some clear decision of a court of the Cayman Islands to the contrary (*Frankland*);

(c) there is, exceptionally, some local condition which would give good reason not to follow it (*Frankland*);

(d) there has been some compelling change of circumstance since the delivery of the English decision (*The Attorney General v K*);

(e) there is some "compelling reason" not to follow it (*Schramm*) such as the reasoning being "fundamentally flawed" (*Re First Virginia Reinsurance*);

(f) if the English decision has been abandoned or invalidated by the UK Parliament or not followed in other great common law courts such as the High Court of Australia (*Anglo v Barr; The Attorney General v K; State of Qatar v Al Thani*; *Morton v Paint*; *Barclays*);

(g) where English procedural rules have been implemented to remove the effect of the English decision (*Re City and International Securities*);

(h) where the common law was developing and is not settled (*Invercargill*);

(i) where the English decision has been "much criticised" and can be said to "affront common sense and any sense of justice" (*Pate*);

(j) where it is undesirable to "cling to obsolete English common law cases which have ceased to be authoritative in England and Wales" (*Morton v Paint*);

(k) where the underlying conditions in the respective jurisdictions are not truly comparable (*Simon v Hulmot*);

(l) where it is inconsistent with contemporary law and its reasoning is inapplicable to the modern common law (*Re CEFC*; *Barclays*);

(m) where by reason of custom, statute or for some other reasons peculiar to Cayman the English decision should be departed from (*Tai Hing Cotton Mill*); and

(n) if the English decision is obviously wrong or otherwise not persuasive (*AG v Reid*).

71. In the vast majority of cases the Cayman Islands courts will continue to follow English decisions where appropriate. At the risk of stating the obvious the above categories are simply categories (based on previous case law) of where a Cayman judge may be justified in not following an English decision. This does not turn the doctrine of precedent on its head. Cayman Islands courts at first

instance will still, of course, be bound by the ratios of the Cayman Islands Court of Appeal and the Judicial Committee of the Privy Council on appeals from the Cayman Islands. Moreover, Cayman Islands judges at first instance would normally also follow the judgments of other judges at first instance unless satisfied that such judgments were wrong (see for example Cresswell J in *Alibaba.com* 2012 (1) CILR 272, Kawaley J in *Simamba v HSA* 2019 (2) CILR 213 and Parker J in *Padma Fund* (Unreported, FSD 201 of 2021 (RPJ), 8 October 2021)).

72. I appreciate that category (n) creates a risk of perhaps causing some confusion and uncertainty but I do not see why Cayman judges should be required to follow English decisions that are obviously wrong or otherwise not persuasive. Does the importance of certainty really require us to do that? I do not think so. We are a separate jurisdiction with our own common law. If the local judges overstep the mark in developing local common law in the best interests of the Cayman Islands the Cayman Parliament can intervene and legislate.

73. I accept that the reality will be in the vast majority of cases the Cayman Islands courts will follow English common law precedent but in some exceptional cases, especially where such precedent has been abandoned by the UK Parliament, it may decide to follow precedent from other leading common law courts such as the High Court of Australia. As we develop and mature as an independent jurisdiction we should have the confidence to break the umbilical cord from the English common law and develop our own common law to suit the best interests of the Cayman Islands. More and more we will be turning to local precedent.

74. In the present case, I ask myself should this Court reasonably be expected to follow a House of Lords decision from 1880 which has been much criticised, abandoned by the UK Parliament and not followed by the High Court of Australia or by the Supreme Court of Bermuda at first instance? It is to that question which we must now turn.

Houldsworth v City of Glasgow Bank

75. Much has been written and said about *Houldsworth v City of Glasgow Bank* 1880 5 App Cas. 317 (H.L.(Sc.)).

76. Mr Millett says it is part of Cayman Islands common law and I should follow it. Mr Levy says it is distinguishable from the facts of the instant case (and should be distinguished) or should not be followed or form any part of Cayman Islands law. Mr Levy says that the decision in *Houldsworth* cannot sensibly be sustained in view of developments in company law since 1880, and the very different context in which it was decided. Mr Smith, although adopting a neutral stance on behalf of the Liquidators, provided opinions to the Liquidators stating that it would likely not be followed in the Cayman Islands. In his undated skeleton argument (provided for the hearing in May 2023) Mr Smith gently submitted that in the absence of any specific Cayman authority on the point, for their part the Liquidators would tend to approach the matter on the basis that the answer to Issue 2 is supplied by the decision of the High Court of Australia in *Sons of Gwalia Ltd v Margaretic* [2007] HCA 1; [2007] 3 LRC 462 (*"Sons of Gwalia"*), being the most recent and leading Commonwealth authority on the point and which deals with all the earlier cases.

77. *Houldsworth* is a difficult case and of its time. It is necessary to determine what *Houldsworth* decided. I shall analyse the judgments to see if I can ascertain a *ratio*. I will also consider subsequent textbook and judicial commentaries upon it to see if they can shed any further light on this case.

78. The House of Lords in *Houldsworth* was dealing with a Scottish appeal. The author of the headnote appears to have concluded that the case was authority for the principle that a person induced by the fraud of the agents of a joint stock company to become "a partner in that company can bring no action for damages against the company whilst he remains in it: his *only* remedy is *restitutio in integrum*, and rescission of the contract; and if that becomes impossible – by the winding-up of the company or by any other means – his action for damages is irrelevant and cannot be maintained."

79. The bank was described in the headnote as "a co-partnership registered under the Companies Act 1862". It was an "unlimited company" and had "by virtue of its articles of co-partnership power to deal in its own shares." Mr Houldsworth was "registered as a partner" and after the bank went into liquidation he raised an action "upon the ground of fraudulent misrepresentations made by the directors and other bank officials to him." It was held that rescission was impossible as decided by

Oakes v Turquand and *Tennett v City of Glasgow Bank*. Mr Herschell QC appeared for Mr Houldsworth.

80. Earl Cairns LC at page 323 stated:

> "The *Winding-up Act* has no provision for the payment of claims against the company except the claims of creditors. Creditors are supposed to be paid *pari passu*, and there is no provision after they are paid for opening up fresh claims by a contributory against the company."

81. Earl Cairns at page 323 set out a question which he ultimately answered in the negative:

> "Can a man, induced by the fraudulent misrepresentations of agents of a company to take shares in the company, after he discovers the fraud, elect to retain the shares, and to sue the company for damages?"

82. Earl Cairns at pages 323 – 324 directed his mind to "the case of shares or stock in a partnership or company". Earl Cairns refers to a buyer agreeing to enter into a partnership "taking his share of past liabilities, and his chance of future profits or losses. He has not bought any chattel or piece of property for himself; he has merged himself into a society, to the property of which he has agreed to contribute, and the property of which, including his own contributions, he has agreed shall be used and applied in a particular and no other way."

83. Earl Cairns at page 325 referred to the "contract which the new partner has entered". The Lord Chancellor assumed he was entitled to rescind his contract, leave the company and recover any money he has paid or any damages he has sustained "but he prefers to remain at the company and to affirm his contract." He then brings an action against the company and if he succeeds money will be paid out of the assets and contributions of the company:

> "The result is, he is making a claim which is inconsistent with the contract into which he has entered, and by which he wishes to abide; in other words, he is in substance, if not in form, taking the course which is described as approbating and reprobating, a course which is not allowed either in Scotch or English law."

84. I pause to state four obvious facts. First, a share is a "piece of property". By section 33 (1)(a) of Companies Act it is stated to be personal estate. Second, a shareholder in a limited company has not "merged himself in a society" (see *Salomon v Salomon* [1897] AC 22). Third, a shareholder in a limited company is not required to contribute an amount exceeding the amount, if any, unpaid on the shares (section 49(d) of the Companies Act). In our case all the shares have already been fully paid. Fourth, Earl Cairns was dealing with what he described as "a partnership contract".

85. Lord Selbourne at page 330 felt that "for rescission the Appellant is confessedly too late."

86. Lord Hatherley at page 331 felt that "if there cannot be a *restituto in integrum*, the contract cannot be rescinded."

87. Lord Blackburn at page 335 did not even think it necessary to hear from counsel for the Respondent. The three silks lined up by the bank (no doubt at great expense), Mr Kay QC, Mr Benjamin QC, Mr Davey QC and the junior Mr Balfour all remained silent in the knowledge of a victory in the bag. At page 337 Lord Blackburn described the contract with a joint stock company to take share as "a very peculiar one". Lord Blackburn felt that whether the court was dealing with a deed of co-partnership as a bank, or a joint stock company "the contract equally is in substance an agreement with the company to become a partner in the company on the terms that the partner shall, in common with all his co-partners for the time being, contribute to make good all liabilities of the co-partnership as if this incoming partner had been a member of the partnership from the beginning." A corporate lawyer in 2023 may have real difficulty relating that description from 1880 to an investor in a limited company whose shares were fully paid.

Textbook commentary on Houldsworth

88. I set out below the way in which *Houldsworth* was dealt with by the textbook writers in the late 1800s, early 1900s and in 1957. I am most grateful to counsel for their assistance in this respect and the individuals who had the pleasure of diving deeply into the dusty shelves of the magnificent libraries in the Inns of Court in London.

89. Bris S *The Law of Corporations and Companies: A Treatise on the Doctrine of Ultra Vires* (3rd Ed. 1893) at page 433 referred at footnote 8 to *Houldsworth* as authority for the proposition that after

a winding up order a shareholder cannot bring "an action for damages against the corporation – as against the latter his right of every description in respect of the alleged fraud are gone."

90. Buckley on *The Law and Practice under the Companies Acts* (5th Ed. 1887) at page 97 put forward *Houldsworth* to support the following statement:

> "The remedy of a shareholder who has been induced to take his shares by fraud is rescission and *restitutio in integrum*. He cannot retain the shares and have damages for the fraud in the same way as if it had been a purchase of goods, he could retain the goods and have damages. He cannot remain a member of the corporation and have damages against the corporation of which he himself is a member."

91. In the 12th edition published in 1949 reference to *Re Addlestone Linoleum Company* [1887] 37 Ch D 191 ("*Addlestone")* was added at footnote (b) on page 263 and at pages 281 to 281 the following statement appeared:

> "If the company has gone into liquidation, and rescission has become impossible he [the shareholder] can have no remedy against the company at all. His action for damages is as irrelevant against the company in liquidation as it would be against the going company."

92. Chadwyck Healey and others in *A Treatise on the Law and Practice relating to Joint Stock Companies* (3rd edition 1894) cite *Houldsworth* on page 605 to support the statement:

> "After the [winding-up] order, he can no longer sue the company for the misrepresentation by which he was induced to take the shares."

93. Hamilton in *A Manual of Company Law* (2nd edition 1901) at pages 154-155 uses *Houldsworth* to support the statement that a person who was induced to subscribe by misrepresentation will lose his right to rescission by the commencement of the winding-up of the company and will also be debarred from obtaining damages.

94. Kerr in *A Treatise on the Law of Fraud and Mistake* (3rd Edition 1902) at page 86 uses *Houldsworth* to support the statement that a person who has been induced to purchase shares by the fraud of the

directors cannot maintain an action against the company if he retains his shares or if rescission is impossible by reason of the winding up of the company but he may sue the directors personally.

95. Walker B Lindley (the son of Lord Lindley) in *A Treatise on the Law of Companies as considered as a branch of the law of partnership* (6th Edition 1902) at page 94 in a publication of its time and heavily influenced by the law of partnership cites *Houldsworth* for the statement that:

> "It is however settled that a shareholder who has been induced by fraud to take shares in a company cannot maintain an action (or its equivalent, viz., a claim) for damages against the company when it is being wound up. This doctrine is based upon the winding-up provisions of the Companies Act 1862, and upon the rights of creditors under winding-up proceedings, and has no application to actions against individual directors or other persons."

96. Palmer's *Company Law* (1898) refers to *Houldsworth* at pages 47, 48 and 235 but not for any propositions relevant to the issue presently before the Court. Perhaps, in his mind at least, it was not authority for the general proposition other authors were using it for.

97. Rawlins and Macnaghten in *Law and Practice in Relation to Companies* (1901) at page 332 cite *Houldsworth* to support the general statement that:

> "When winding up has commenced, not only is the shareholder debarred from repudiating his shares, although he may have been induced to accept them by fraud of the company and its officers, but he cannot sue the company or its liquidator."

98. Smith in *A Summary of the Law of Companies* (9th Edition 1907) at page 38 cites *Houldsworth* to support the statement:

> "If a person induced to take shares in a company by misrepresentation cannot get rescission of his contract he is without any remedy against the company."

99. Let us now fast forward some 50 years to 1957 and Gower in *Principles of Modern Company Law* (2nd Edition 1957) at pages 295-196 (footnotes omitted) states:

> "In fact, however, it seems clear that the company is not liable in damages when shares have been purchased in such circumstances. This is because of the anomalous rule, laid down by the House of Lords in *Houldsworth v. City of Glasgow Bank*, to the effect that damages cannot be recovered from the company unless the allotment of shares is also rescinded. In laying down this rule the House do not seem to have recognised fully the separation between the corporate entity and the member, but the decision can be explained on two grounds. The first is that to recover damages would be inconsistent with the terms of the implied contract between all the shareholders. The second justification depends on the recognition of share capital as a guarantee fund for creditors. As we shall see, this conception is at the basis of the rule that a shareholder who wishes to rescind must do so promptly, since the existence of his shares may have led others to extend credit to the company. But if a shareholder were permitted to recover damages notwithstanding that he had lost the right to rescind, the consequences to third parties would be just as detrimental, since the assets of the company would be equally depleted. Hence the rule that he must act promptly, and unless he does so and rescinds the allotment (thus ceasing to be a shareholder) he will lose all remedies against the company." (My underlining.)

Houldsworth in context

100. Mr Millett says that I must consider *Houldsworth* in its proper context including *Oakes v Turquand* [1867], *Tennett v The City of Glasgow Bank* [1879] and *Hull and County Bank* [1888].

101. *Oakes v Turquand* [1867] LR 2 HL 325 concerned a limited company. The first paragraph of the headnote states:

> "Where a person has been, by the fraudulent misrepresentations of directors, or by their fraudulent concealment of facts, drawn into a contract to purchase shares in a company, the directors cannot enforce the contract against him, but he may rescind it. But he must do so within a reasonable time."

102. After judgment was delivered Mr Swanston, junior counsel for the unsuccessful appellants (his leader Mr Giffard QC was wise enough to stay silent off his feet), boldly rose to his feet and had

the temerity to ask a question to avoid "some misunderstanding of your judgment" and he was promptly put firmly back in his place with the following judicial rebuke delivered by the Lord Chancellor at page 379 of the report:

> "I really do not think these points ought to be allowed to be raised at this stage. It is becoming very much the fashion to bring up points after the original hearing. I do not think that that is right, or that it is a practice we ought to encourage."

103. Attorneys in 2023 would do well to reflect upon those words uttered in 1867.

104. In *Tennant v City of Glasgow Bank* [1879] 4 App Case 615 HL (Sc.) Earl Cairns LC at 621 stated that in *Oakes v Turquand*:

> "This House has established that it is too late, after winding-up has commenced, to rescind a contract for shares on the ground of fraud."

105. *Re Hull and County Bank* [1880] 15 Ch D 507 concerned a limited company. Jessell MR at page 511 referred to the position where an applicant has been induced to become a shareholder by fraudulent misrepresentation: "Can he after winding up be relieved? I think he cannot …"

106. *Addlestone* also concerned a limited company. Kay J at pages 198-199 stated that in *Houldsworth*:

> "it was held that fraudulent misrepresentations of a director inducing the plaintiff to take shares might give him a right to rescind the contract, but gave him no right whatever to hold the shares and prove for damages against the company."

107. Lindley LJ at pages 205-206 stated:

> "The principle on which the House of Lords decided [*Houldsworth*] was that a shareholder contracts to contribute a certain amount to be applied in payment of the debts and liabilities of the company, and that it is inconsistent with his position as a shareholder, while he remains such, to claim back any of that money – he must not directly or indirectly receive back any part of it, and this appears to me to govern the present case."

Soden

108. The headnote to the report of judgments of the House of Lords in *Soden v British & Commonwealth Holdings Plc* [1998] A.C. 298 reads as follows:

> "*Held*, dismissing the appeal, that the rationale of section 74(2)(f) of the Insolvency Act 1986 was to ensure that the rights of members as such did not compete with the rights of the general body of creditors; that a sum was due to a member "in his character of a member" within section 74(2)(f) if the right to receive it was based on a cause of action founded on the statutory contract between the members and the company and members *inter se* imposed by section 14(1) of the Companies Act 1985 and such other provisions of the Act as conferred rights or imposed liabilities on members, but that where membership, though an essential qualification for acquiring the claim, was not the foundation of the cause of action, it fell outside section 74(2)(f); that an action founded on a misrepresentation by a company on the purchase of existing shares from third parties was not based on the statutory contract; and that, accordingly, any damages recovered by the first defendant would not be subordinated to the claims of other creditors (post, pp. 323C-G, 324A-C, 327A-F).
>
> *In re Addlestone Linoleum Co.* (1887) 37 Ch.D. 191, Kay J. and C.A., and *Webb Distributors (Aust.) Pty. Ltd. v. State of Victoria* (1993) 11 A.C.S.R. 731 distinguished."

109. The judges in that case had the benefit of submissions from company law heavy weights in Erskine Chambers including Robin Potts KC with Dan Prentice for the plaintiffs and William Stubbs KC and Catherine Roberts. Peter Gibson LJ in the Court of Appeal dealt with section 74(2)(f) of the UK Insolvency Act 1986. Section 74, so far as material, was in the following form:

> "(1) When a company is wound up, every present and past member is liable to contribute to its assets to any amount sufficient for payment of its debts and liabilities, and the expenses of the winding up, and for the adjustment of the rights of the contributories among themselves. (2) This is subject as follows … (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."

110. Peter Gibson LJ at page 310 referred to the reliance placed on *Houldsworth* by Mr Potts and said:

> "It was held that it was not possible for a member to claim damages against the company while remaining a member, and as the company had gone into liquidation, it was too late to rescind the contract. Mr Potts acknowledged that this decision lacks the clarity and sophistication of later judgments, but he rightly submitted that the ratio of the case and the policy underlying the ratio were relatively clear, viz. a member is precluded from bringing an action for damages for deceit arising out of a contract for the subscription for shares without first rescinding his contract of membership. It was in substance a case of approbating and reprobating, which, Earl Cairns L.C., said was not permitted."

111. Peter Gibson LJ referred to *Addlestone*, *Ooregum Gold Mining Co. of India v Roper* [1892] AC125 and *Webb*.

112. Lord Browne-Wilkinson in the House of Lords in *Soden* at page 323 onwards referred to the submission of Mr Potts that a sum due to a person in his character as a member of a company where it is due to him under the bundle of rights which constitute his shares in the company or by reason of a warranty or misrepresentation on the part of the company going to the characteristics or value of the shares which induces him to acquire those shares and dealt with such submissions as follows:

> "I cannot accept these submissions. Section 74(2)(f) requires a distinction to be drawn between, on the one hand, sums due to a member in his character of a member by way of dividends, profits or otherwise and, on the other hand, sums due to a member otherwise than in his character as a member. In the absence of any other indications to the contrary, sums due in the character of a member must be sums falling due under and by virtue of the statutory contract between the members and the company and the members inter se constituted by section 14(1) of the Companies Act 1985:

> "Subject to the provisions of this Act, the memorandum and articles, when registered, bind the company and its members to the same extent as if they respectively had been signed and sealed by each member, and contained covenants on the part of each member to observe all the provisions of the memorandum and of the articles."

A contract to similar effect was prescribed by section 16 of the Act of 1862 and all Acts since then. To the bundle of rights and liabilities created by the memorandum and articles of the company must be added those rights and obligations of members conferred and imposed on members by the Companies Act. For ease of reference, I will refer to the combined effect of section 14 and the other rights and liabilities of members imposed by the Companies Acts as "the statutory contract." In my judgment, in the absence of any contrary indication sums due to a member "in his character of a member" are only those sums the right to which is based by way of cause of action on the statutory contract.

That is the correct interpretation is supported by the words in section 74(2)(f) "by way of dividends, profits or otherwise." There was some discussion in the judgment of the Court of Appeal whether these words disclose a genus requiring a sum "otherwise" due to be given a narrow construction under the ejusdem generis rule and as to what, if any, genus was disclosed by the words "by way of dividends, profits." In my view that is not the right approach to the section. The words "by way of dividends, profits or otherwise" are illustrations of what constitute sums due to a member in his character as such. They neither widen nor restrict the meaning of that phrase. But the reference to dividends and profits as examples of sums due in the character of a member entirely accords with the view I have reached as to the meaning of the section since they indicate rights founded on the statutory contract and not otherwise.

Moreover, the construction of the section which I favour accords with principle. The principle is not "members come last:" a member having a cause of action independent of the statutory contract is in no worse a position than any other creditor. The relevant principle is that the rights of members *as members* come last, i.e. rights founded on the statutory contract are, as the price of limited liability, subordinated to the rights of creditors

based on other legal causes of action. The rationale of the section is to ensure that the rights of members as such do not compete with the rights of the general body of creditors.

If this is the correct dividing line between sums due in the character of a member and those not so due, there is no room for including in the former class cases where membership, though an essential qualification for acquiring the claim, is not the foundation of the cause of action. This is illustrated by the decisions on directors' remuneration. After an early aberration (*In re Leicester Club and County Racecourse Co.; Ex parte Cannon* (1885) 30 Ch.D. 629) it is now clearly established that directors' fees are not due to a director "in his character of a member" even where the articles of the company require a director to hold a share qualification and provide for the remuneration of the directors: *In re Dale and Plant Ltd.* (1889) 43 Ch.D. 255; *In re New British Iron Co.; Ex parte Beckwith* [1898] 1 Ch. 324; *In re W.H. Eutrope & Sons Pty. Ltd.* [1932] V.L.R. 453. Although membership is a necessary qualification for appointment as a director, the cause of action to recover the remuneration is not based on the rights of a member but on a separate contract to pay remuneration.

Mr Potts placed great reliance on the decisions in the *Addlestone* and *Webb* cases, in both of which it was held that a sum due in respect of damages payable for breach of contract or misrepresentation made by the company on the occasion of the *issue* (as opposed to the purchase) of its shares were held to be excluded by the section. Before considering these cases, there are two background points to be made. First, there was a principle established in *Houldsworth v. City of Glasgow Bank* (1880) 5 App.Cas. 317 that a shareholder could not sue for damages for misrepresentation inducing his subscription for shares unless he first rescinded the contract and that once the company had gone into liquidation such rescission was impossible. This principle has now been modified by section 111A of the Companies Act 1985, as inserted by section 131(1) of the Companies Act 1989. Second, it was not until the decision of this House in *Ooregum Gold Mining Co. of India Ltd. v. Roper; Wallroth v. Roper* [1892] A.C. 125 that it was established that a company had no power to issue shares at a discount."

113. Lord Browne-Wilkinson continued at pages 325-327 as follows:

"If there had been a cause of action in the *Addlestone* case, it must, as it seems to me, have been based upon the statutory contract between the member and the company. "Dividends" and "profits" represent what might be called positive claims of membership; the fruits which have accrued to be called positive claims of membership. But the principle must apply equally to negative claims; claims based upon having paid money to the company under the statutory contract which the member says that he is entitled to have refunded by way of compensation for misrepresentation or breach of contract. These, too, are claims necessarily made in his character as a member. But, in any event, the reasons given by Kay J. for treating the case as falling within section 38(7) are directed exclusively to matters relevant to a claim involving the issues of shares by the company but irrelevant to a claim relating to the purchase of fully paid shares from a third party. Under the statutory contract (including the obligation in the winding up to pay all sums not previously paid on the shares) the claimants were bound to pay the unpaid £2 10s. in respect of each share. If such a payment were not made the capital of the company would not be maintained and the general body of creditors would be thereby prejudiced. If, in such a case, the member could recovery by way of damages for breach of the contract to issue the shares at a discount the same amount as he was bound to contribute on the winding up that would indirectly produce an unauthorised reduction in the capital of the company. Such a failure to maintain the capital of the company would be in conflict with what Lord Macnaghten (in the *Ooregum* case [1892] A.C. 125, 145) said was the dominant and cardinal principle of the Companies Acts, i.e. "that the investor shall purchase immunity from liability beyond a certain limit, on the terms that there shall be and remain a liability up to that limit."

There is nothing in the *Addlestone* case to justify the application of that decision to cases where the claim against the company is founded on a misrepresentation made by the company on the purchase of existing shares from a third party. To allow proof for such a claim in competition with the general body of creditors does not either directly or indirectly produce a reduction of capital. The general body of creditors are in exactly the same position as they would have been in had the claim been wholly unrelated to shares in the company.

The decision of the High Court of Australia in the *Webb* case, 11 A.C.S.R. 731 stands on exactly the same footing. Section 360(1)(k) of the Companies Code of Victoria was in substantially the same terms as section 38(7) of the English Act of 1862 and section 74(2)(f) of the Act of 1986. The court held that section 361 was applicable to building societies as well as to the limited companies. Three societies had issued non-withdrawable shares. The claimants were claiming to prove for damages in the winding up of the building societies such damages being based on misrepresentations made by the societies on the issue of such shares to the effect that the shares were redeemable "like a deposit." The High Court held that the claim was excluded by the *Houldsworth* principle and held that the proposition deducible from that case was that a shareholder may not directly or indirectly receive back any part of his or her contribution to the capital save with the approval of the court. The High Court further relied on the *Addlestone* decision and section 360(1) but carefully delimited its application to cases of contracts to subscribe for shares. They held, 11 A.C.S.R. 731, 741 that the claim in that case "falls within the area which section 360(1)(k) seeks to regulate: the protection of creditors by maintaining the capital of the company." It is therefore quite clear that both the decision and the reasoning of the High Court were dependent upon the same factors as those in the *Addlestone* case, i.e. the protection of creditors from indirect reductions of capital. Those are factors relevant to cases of subscription for shares issued by the company but wholly irrelevant to purchases from third parties of already issued shares.

I express no view as to the present law of the United Kingdom where the sum due is in respect of a misrepresentation or breach of contract relating to the issue of Shares. Section 111A of the Act of 1985 provides:

> "A person is not debarred from obtaining damages or other compensation from a company by reason only of his holding or having held shares in the company or any right to apply or subscribe for shares or to be included in the company's register in respect of shares."

It is plain that this section operates so as, at least in part, to override the *Houldsworth* principle. But to what extent and with what consequential results is not yet clear. All that

is necessary for the decision of the present case is to demonstrate, as I have sought to do, that the decisions in *Addlestone*, 37 Ch.D. 191 and *Webb*, 11 A.C.S.R. 731 do not apply to claims other than those relating to the issue of shares by the company.

For these reasons, which are substantially the same as those given by the trial judge and the Court of Appeal in their admirable judgments, I am clearly of the opinion that the sum if any due to B. & C. is not due to it in its "character of a member" of Atlantic within section 74(2)(f). The claim stands on exactly the same footing as any other claim by B. & C. against Atlantic which is wholly unrelated to the shares in Atlantic. In the circumstances, it is unnecessary to deal with the further point relied upon by B. & C. (but rejected by the Court of Appeal) that B. & C.'s claim being unliquidated is not "a sum due" within the meaning of the section.

I would dismiss the appeal."

114. Lords Lloyd, Steyn, Hoffmann and Hope agreed with Lord Brown-Wilkinson.

SPhinX

115. *Houldsworth* was very gently touched upon by Smellie CJ, as he then was, in *SPhinX Group of Companies* 2010 (2) CILR 1. In that case, the issue was whether the court should make a representation order in an application by liquidators for directions as to the proper administration of the liquidation estate in respect of 23 distinct issues or questions. Smellie CJ held that the Grand Court had inherent jurisdiction which was recognised by section 18(2) of the Grand Court Act. Question 20 raised an issue in respect of potential investor misrepresentation claims. Such issue was not before the court for determination but Smellie CJ, strictly *obiter* by way of introductory comments to the main representation order issue before the court and it would appear without the benefit of full argument on the misrepresentation point and with no reference to subsequent statutory developments following *Houldsworth* nor to *Sons of Gwalia* stated:

"21. On the long-standing authority of the House of Lords' decision in *Houldsworth v City of Glasgow Bank* (11), the SPhinX companies having been placed into liquidation, an

investor seeking rescission of his share purchase contract and *restitutio in integrum* on the grounds of misrepresentation may well no longer have available to him such remedies …"

Direct Lending

116. *Houldsworth* was also mentioned by Segal J in *Re Direct Lending Feeder Fund Ltd* (Unreported, FSD 108 of 2019, 10 November 2022). At paragraph 24 Segal J in a sentence prior to his mention of *Houldsworth* stated:

> "… the JOLs said that they had been advised that there was an open question under Cayman Islands law as to whether a shareholder who had been induced by a misrepresentation to subscribe for shares can claim damages against a company in liquidation …"

117. At paragraph 94 Segal J refers to *SPhinX* and at paragraph 95 to Smellie CJ's judgment and his brief mention of *Houldsworth*.

The treatment of *Houldsworth* in two other jurisdictions

118. I now turn to the treatment of *Houldsworth* in two other jurisdictions.

***Televest* in Bermuda**

119. Ground J (as he then was) in 1995 had to consider the application of *Houldsworth* as a matter of the law of Bermuda. In his Reasons for Order in *Televest Ltd* (12 July 1995) at page 3 the judge referred to the preferred shareholders seeking to maintain a claim based upon material misrepresentations made in the prospectuses for the issue of their shares. Ground J stated:

> "…. The problem they face with this approach is that the common law of England was that a shareholder could not pursue an action for damages for deceit against a company in respect of the contract by which he obtained his shares, unless he was entitled to rescind the contract of allotment: Houldsworth -v- City of Glasgow Bank (1880) 5 App. Cas. 317. This rule, which was subsequently extended to actions for breach of the contract of allotment, precluded an action for damages where rescission had become impossible, for

example because a winding-up order had been made. The rule was subsequently much criticised and has since been abrogated in England by section 111A of the Companies Act 1985, (inserted by the Companies Act 1989) which provides:

> "A person is not debarred from obtaining damages or other compensation from a company by reason only of his holding or having held shares in the company …"

However, that provision has not yet been followed by the Legislature in Bermuda.

Various arguments have been advanced to me to show that the subsequent history of statutory intervention to create rights in respect of non-fraudulent misrepresentations has overridden the rule in Houldsworth -v- City of Glasgow Bank (*supra*), but each of those arguments is itself fraught with difficulty and uncertainty. It was also suggested to me that being a decision of the House of Lords, and not of the Privy Council, I was not obliged to follow that decision – a submission which in strict law is correct, but which in due deference I find hard to apply. I prefer another approach.

The speeches of their Lordships in *Houldsworth's* case make it plain that they are concerned with the case of the shareholder who is in real sense a member of the company, and can participate in its decisions. It is also plain that they were applying an earlier decision on facts which were materially similar, Addie -v- the Western Bank, LR 1 HL.Sc. 145, and which they considered was indistinguishable. On that aspect Lord Blackburn had this to say:

> "But one very important question was raised by the judgments in the Court of Session, and argued by the counsel at your Lordships' Bar, which, if ever it becomes necessary to decide it, may require much consideration. The contract with a joint stock company to take shares in that company is a very peculiar one. Whether the company be, as the Western Bank was, a banking co-partnership in Scotland … having such a deed of co-partnership as that bank had, or a joint stock

> company registered under the Companies Act 1862, the contract equally is in substance an agreement with the company to become a partner in the company on the terms that the partner shall, in common with all his co-partners for the time being, contribute to make good all liabilities of the co-partnership as if this incoming partner had been a member of the partnership from the beginning. Further, he consents that any of his co-partners may, by procuring a person to take his shares, get rid (at least *inter socios*) of his liability, substituting that of the incoming shareholder. I know of no other contract which in these respects resembles this contract.
>
> It was with this peculiar kind of contract that the House of Lords had to deal in Addie -v- The Western Bank, and it is with this peculiar kind of contract that your Lordships have now to deal. I do not think the House is called on now to decide whether a difference in the kind of contract induced by the fraud would make a sufficient distinction in law to prevent the decision in *Addie's Case* from governing such a case as that."

In the instant case there is no real partnership: the Articles of the company are already in evidence (although not agreed for the purposes of this hearing), and from them it is apparent that the redeemable preference shares carried neither voting rights nor the right to participate in the appointment of directors. To that extent the preferred shareholders were entirely in the hands of the holders of the common shares, who constituted the real partnership that controlled the company. Nor did the preferred shareholders contract *inter se* to contribute to the liabilities of the company in the way envisaged by Lord Blackburn: no call could be made upon them, as the shares were in their nature fully paid up, and while it is true that the extent of the investment was hostage to the fortunes of the company, a shareholder could terminate that liability at any time when the company was solvent by giving notice to redeem. In those circumstances, I do not see why any principle should debar them from seeking a remedy in damages, be it for fraud, breach of contract, negligence or misrepresentation, against the company. It is not as if they have in any

meaningful sense become a part of the Company, and are thus essentially suing themselves. If further demonstration were needed, the example given by the Lord Chancellor, Earl Cairns, at p.325 of the decision in *Houldsworth's case*, illustrates just how removed the circumstances he was considering are from those of this case.

In my view, therefore, the shares were essentially an investment vehicle and not in any real sense to be compared with the type of shareholding envisaged by their Lordships in *Houldsworth's case*. In that case the House of Lords expressly envisaged their decision being distinguished in different circumstances, and I find that the circumstances before me are different and distinguishable, and that therefore that decision and any supposed rule established by it is no bar to these preferred shareholders pursuing claims against the Company.

In view of this decision I have not gone on to consider the application of section 31 of the Companies Act 1981, preferring not to do so in the somewhat artificial circumstances of this application, if it could be avoided.

SUMMARY

For the reasons given above I distinguish this case from Houldsworth -v- City of Glasgow Bank (1880) 5 App. Cas. 317, and hold that the preferred shareholders are not debarred by reason of that case from making a claim for damages in the liquidation based upon alleged misrepresentations made to them, however such a claim is framed.

At this stage I do not think that it is for me to decide whether the preferred shareholders are in fact creditors by reason of any particular misrepresentation, and so rather than give a direction in the form sought, I propose simply to direct that proofs of debt filed by the preferred shareholders should not be disallowed on the grounds of the rule in *Houldsworth's case*, but should be considered on their merits. I should, however, be happy

to hear counsel further on the appropriate direction in view of my reasons, and I therefore give a liberty to apply in this regard.

However, that may not necessarily dispose of the substance of the application before me, because in considering the claims of the preferred shareholders the Liquidators will still be bound by section 158(g) of the Companies Act 1981. That subsection provides that:

> "(g) A sum due to any member of a company, in his character as member, by way of dividends, profits or otherwise shall not be 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 purposes of the final adjustment of the rights of the contributories among themselves." (My emphasis.)

No argument has been addressed to me on the application of this subsection, and at this stage I simply observe that in *In re Addlestone Linoleum Company* (1887) 37 Ch D 191 CA (a case which counsel very properly put before me to illustrate the extension of the rule in *Houldsworth's case* to claims in contract), both the first instance judge and two members of the Court of Appeal considered that a claim for damages for breach of the allotment contract fell within the English precursor of this subsection. In view of that, I invite counsel to consider this point and address me further upon it if they wish, and I give a liberty to apply to do so."

***Sons of Gwalia* in Australia**

120. I now turn to *Sons of Gwalia,* an appeal dealt with by the High Court of Australia, that country's well-respected final court of appeal. I note all the points raised by Mr Millett in respect of *Sons of Gwalia* but I nevertheless find it of great persuasive weight in respect of Issue 2 and Issue 3.

121. In *Sons of Gwalia* the respondent bought shares in the appellant gold-mining company on the Australian Stock Exchange and 11 days later the company collapsed and went into administration.

Having made a claim for damages or compensation (under various Australian statutes) and the tort of deceit the respondent notified the administrators that he intended to submit his claim for proof as a creditor. The administrators applied to the Federal Court of Australia for a declaration that his claim was not provable or alternatively a declaration in terms of section 563A of the Corporations Act 2001 that payment of that claim was "to be postponed until all debts owed to, or claims made by, persons or otherwise than in their capacity as members of the company [had] been satisfied." At first instance the judge made declarations in favour of the respondent that he was a creditor of the company and his claim was not postponed until debts owed to, or claims made by, persons other than the respondent or others in his position had been satisfied. On appeal his decision was upheld by the Full Court. The administrators and a creditor which was not a shareholder, representing the body of general creditors appealed to the High Court. The non-shareholder contended that there was a common law principle derived from House of Lords authority (*Houldsworth*) that a shareholder was not entitled, directly or indirectly, to receive back any part of his contribution to the capital of the company, which precluded the respondent from suing for damages for misrepresentation inducing his acquisition of his shares or proving such a claim as a debt in a winding up unless he first rescinded the "membership contract" which he was unable to do once the company went into liquidation.

122. The headline states that it was held (Callinan J dissenting) that assuming the respondent had a valid claim against the company, that claim was not founded on any obligations owed by or to him as a member of the company, because on the true construction of section 563A of the 2001 Act a "person's capacity as a member of the company" defined and confined the particular kinds of obligations that were to be postponed until all other debts owed by the company were paid and in doing so the phrase identified the particular kinds of 'debt owed by a company' to which particular consequences, namely postponement of payment, were attached. An obligation did not fall within section 563A unless there was a connection between the obligation and membership of the company and the obligation which the respondent sought to enforce against the company was not founded on any rights he obtained or any obligations he incurred which the 2001 Act created in favour of a company's members. He was not seeking to recover any paid-up capital, or to avoid any liability to make a contribution to the company's capital and his claim would have been no different if he had ceased to be a member at the time it was made, or if his name had never been entered on the

register of members. Instead, insofar as it was based on the statutory causes of action his claim arose out of the company's contravention of the investor and consumer protection provisions and the consequent liability for damages or other relief if sued by any person who suffered or was likely to suffer loss and damage as a result of such contravention, and insofar as his claim was based on the tort of deceit, it was a claim that stood altogether apart from any obligation created by the 2001 Act and owed by the company to its members. The respondent's claims were therefore not claims for money "owed by a company to a person in the person's capacity as a member of the company".

123. It followed that shareholders' claims to recover losses caused by a company's wrongdoing ranked equally with the claims of other unsecured creditors in the distribution of the assets of the company, and were not postponed until all debts owed to general creditors had been satisfied – *Soden* followed, *Houldsworth* explained, *Webb* doubted.

124. Per Gleeson CJ – a distinction was to be drawn between a shareholder claiming in the capacity of a member and a shareholder claiming otherwise than in the capacity of a member, and to make that distinction it was necessary to analyse the nature of a claim rather than merely describe its effect on other creditors. Per Gleeson CJ, Gummow, Kirby, Hayne, Heydon and Crennan JJ – there was no general policy in the 2001 Act that 'members came last' and there was no common law 'principle' of company law derived from *Houldsworth* applicable in Australia, since neither *Webb* nor *Houldsworth* itself established any common law 'principle' that a shareholder, no matter how his shares were acquired, could not sue a company to recover losses caused by the company's misrepresentation inducing his acquisition of his shares if the company went into liquidation.

125. Per Callinan J (dissenting) – having regard to the scope and objects of the 2001 Act, the language used in section 567A itself, the context and the history and the relevant case law and the desirability of maintaining coherence and fairness in the law, section 563A was to be construed as meaning that a shareholder did not have equal rights with ordinary creditors in a winding up in respect of a claim concerning the value of shares on which his membership of the company was based.

126. Gleeson CJ at paragraph [3] referred to the long history of section 563A "that goes back before the decision in *Salomon v Salomon & Co Ltd* [1897] AC 22 to a time when the separateness of a

corporation from its members had not been fully recognised, and when the difference between corporations and partnerships was not as distinct as it later became."

127. Gleeson CJ at paragraph [14]:

> "The principle in *Houldsworth* is famously elusive."

128. At paragraph [13] Gleeson CJ stated:

> "According to the second appellant's argument, there is a principle of common law, emerging from *Houldsworth*, which precludes a shareholder from proving in a winding up (or indeed a deed of company arrangement) for damages for misrepresentation inducing any acquisition of shares unless the shareholder has first rescinded 'the membership contract.' Once the company has become insolvent and has gone into liquidation or voluntary administration, rescission is not available."

129. Gleeson CJ at paragraph [16]:

> "*Houldsworth* was never authority for a principle as wide as that asserted by the second appellant."

130. Gleeson CJ at paragraph [20] referred to *Houldsworth* and "two possible sources of influence" that "might have been at work in *Houldsworth*", "one relating to partnership law, the other relating to the raising and maintenance of share capital". Gleeson CJ referred to the fact that *Houldsworth* was dealing with an unlimited company and on liquidation "the investor became liable to pay calls as a contributory, and the liability was unlimited" and "what the investor was attempting to do was, in effect, to obtain from the company reimbursement in respect of his liability to pay calls in the winding up of the company, in circumstances where he could no longer obtain rescission of the contract of allotment pursuant to which he acquired the shares which exposed him to the liability to pay calls."

131. Gleeson CJ referred to *Addlestone* and set out the following words of Lindley LJ in that 1887 case:

> "The principle on which the House of Lords decided *Houldsworth v City of Glasgow Bank* was that a shareholder contracts to contribute a certain amount to be applied in payment of the debts and liabilities of the company, and that it is inconsistent with his position as a shareholder, while he remains such, to claim back any of that money – he must not directly or indirectly receive back any part of it."

132. Gummow J at paragraph [49] stated:

> "… in Australia the existence of any such common law 'principle' of company law based upon *Houldsworth* should be rejected. Further, *Houldsworth* did not supply the support relied upon for the reasoning in *Webb*."

133. Gummow J at paragraph [65]:

> "… *Houldsworth* was decided at a time when the 1862 UK Act was relatively new and when other areas of law applicable to the relations between members, directors and the company were in a state of fluidity."

134. Gummow J at paragraph 69 referred to the reasoning in *Houldsworth* and its reliance on analogies with the principles of partnership law and approbating and reprobating and alternative remedies. Gummow J respectfully commented at paragraph [70] stating:

> "That reasoning bears the marks of its time."

135. Gummow J at paragraph [78]:

> "It is not easy to discern why an action for damages was inconsistent with the features of the contract whereby shares were taken up. Nor is it clear why this inconsistency should have prevented the shareholder from claiming that the fraud of the directors was imputable to the company."

136. Gummow J at paragraph [79]:

> "Accordingly, *Houldsworth* should not be regarded in Australia as establishing any principle based upon the above reasoning; nor does it establish any exception respecting the responsibility of a principal for the frauds of an agent, stated by *Ashburner* in the passage referred to above."

137. Gummow J at paragraph [80] referred to *Salomon v A Salomon & Co Ltd* [1897] AC 22 and at paragraph [83] referred to Professor Gower in 1954 describing the 'anomalous rule' in *Houldsworth* and attempting to rationalise it on the notion that share capital is a 'guarantee fund' for creditors. Professor Gower's attempts plainly did not impress Gummow J and nor do they impress me. Gummow J at paragraph [85], with considerable persuasive force, stated:

> "… there is much to be said for the view that a company satisfying its liability in tort to a member should not be characterised as attempting an unauthorised reduction of capital. The award of damages is not charged upon any fund representing capital. Large awards may adversely affect the market value of shares in the company, but they do not require any return on capital."

138. Gummow J at paragraph [89] made reference to *Houldsworth* and *Addlestone* and stated:

> "References to partnership indicate an incomplete understanding of the separate nature of the personality of the corporate entity from those of the corporators. At the time *Addlestone* was decided, partnership law and company law were not distinctly regarded."

139. In 1878 it was established English law that a partner "shall not prove in competition with the creditors of the firm, who are in fact his own creditors" (*Lindley* 4th edn. 1878 pp 1187ff).

140. Kirby J with characteristic openness and pragmatism, fully conscious of the different roles of the judiciary and legislature at paragraph [133] stated:

> "If Parliament concludes that the interpretation adopted by the Federal Court in these appeals, now confirmed by this court, strikes the wrong balance between the rights of general creditors and the claims of disaffected shareholders, it can easily repair the defect by amending s563A of the 20021 Act … It should not therefore be assumed that the

inclusion of shareholder claims, such as those of the respondent, with the debts of general creditors is contrary to the will of Parliament or the result of a slip or oversight requiring a measure of judicial inventiveness and surgery."

141. Hayne J felt that the answers to the questions that arose in the appeal were to be answered by reference to the relevant statutory provisions in particular section 563A and section 553 of the 2001 Act. I set out section 553(1) of the Australian 2001 Act as follows:

> "Subject to this Division, in every winding up, all debts payable by, and all claims against, the company (present or future, certain or contingent, ascertaining or sounding only in damages), being debts of claims the circumstances giving rise to which occurred before the relevant date, are admissible to proof against the company."

142. Section 563A of the Australian 2001 Act is as follows:

> "Payment of a debt owed by a company to a person in the person's capacity as a member of the company, whether by way of dividends, profits or otherwise, is to be postponed until all debts owed to, or claims made by, persons otherwise than as members of the company have been satisfied."

143. At paragraph [137] Hayne J set out the complicated questions for the court's determination with simplicity, clarity and conciseness:

> "What is meant by s563A by 'a debt owed by a company to a person *in the person's capacity as a member of the company*"? Is a claim by a shareholder for damages assessed as the loss sustained as a result of the shareholder's acquisition of the shares, when the shares were less valuable than was represented, or would have been revealed to be the case had proper disclosure been made, a claim in the capacity of shareholder? Does the answer to that question differ according to whether the shareholder acquired the shares by subscription and allotment by the company, or acquired them by transfer from an existing shareholder?"

144. Hayne J at paragraph [183] recorded that the decision in *Houldsworth* concerned an unlimited company and was decided before *Salomon v Salomon & Co* which "revealed what is now accepted to be one of the axiomatic consequences of incorporation – the separate legal personalities of the corporation and its consequences." Hayne J also records that *Houldsworth* has been said "to be a decision that is anomalous because it shows confusion between the corporation and its members." Hayne J continued:

> "It has been described as being 'of legendary impenetrability' (see *Soden v British & Commonwealth Holdings plc* [1995] 1 BCLC 686 at 695). It is as Tadgell J said in *State of Victoria v Hodgson* [1992] 2 VR 613 to 625, a decision that 'no doubt bears the stamp of its era'. All this notwithstanding, the parties in *Webb Distributors* placed *Houldsworth*, not the applicable statutory provisions, at the forefront of their arguments."

145. Hayne J at paragraph [190] states:

> "Neither *Webb Distributors* nor *Houldsworth* established any common law 'principle' that no shareholder, no matter how the shares were acquired, can have a claim of the kind now in issue against a company whose assets were to be administered as on a liquidation."

146. Hayne J at paragraph [206] stated that the obligation which Mr Margaretic sought to enforce was not an obligation which the 2001 Act creates in favour of a company's members and concluded that the claim in the tort of deceit is not a claim "owed by a company to a person in the person's capacity as a member of the company."

147. I should record that I did not find Callinan J's sole dissent as persuasive.

148. Heydon J agreed with Hayne J at paragraph [262] and also concluded that Mr Margaretic's claim is not a claim for payment of 'a debt owed by a company to a person in [his] capacity as a member of the company'.

149. Heydon J at paragraph [263] had nothing to say about *Webb* and *Houldsworth* in addition to Hayne J's explanation as to why "they are not determinative."

150. Crennan J at paragraph [265] agreed with Gleeson CJ and Hayne J and "generally" agreed with Gummow J and his analysis "of what was referred to in argument as a 'principle' said to be derived from [*Houldsworth*]."

151. Crennan J at paragraph [273] stated:

> "Any obligation on the company to pay compensation to Mr Margaretic for fraudulent misrepresentation inducing him to become a member and occasioning him loss does not answer the description of being owed to Mr Margaretic 'in [his] capacity as a member of the company'."

152. To complete the Australian picture I should refer to a release dated 26 November 2010 from David Bradbury MP in Australia, Parliamentary Secretary to the Treasurer where the following is stated:

> "Sons of Gwalia Bill passes Federal Parliament
>
> A Bill that reverses the Sons of Gwalia High Court decision and restores certainty to shareholders and creditors was passed by the Federal Parliament this week, said Parliamentary Secretary to the Treasurer, David Bradbury.
>
> The *Corporations Amendment (Sons of Gwalia) Bill 2020* reverses the High Court's decision in the *Sons of Gwalia v Margaretic* case, in which it was found that section 563A of the Corporations Act did not subordinate certain compensation claims by shareholders below the claims of other creditors.
>
> The decision not only challenged the common understanding of the ranking of claims but it created uncertainty for unsecured lenders and restricted the availability of credit for businesses.
>
> "These amendments give effect to the Gillard Government's decision to restore the common understanding of the subordination of claims prior to the Sons of Gwalia High Court decision," said Mr Bradbury.

> "The High Court decision would have allowed certain shareholders to have their claims for damages against an insolvent company ranked alongside unsecured creditors.
>
> "When someone makes a decision to invest in a company, they do so in the hope of sharing in the company's profits.
>
> "Creditors, on the other hand, are simply owed money for services or work they have provided, or for a return of the credit that has been extended.
>
> "The effect of the High Court decision meant that unsecured creditors were less willing to lend money, reducing the availability of credit and increasing the cost of borrowing for business.
>
> "The amendments also streamline the treatment of shareholder claimants in an external administration and eliminate common law restrictions on the capacity of a shareholder to recover damages against a company.
>
> "This is an important amendment to our Corporations Act that will restore certainty for shareholders and creditors and I welcome its passage through the Parliament.""

153. It is important to note that the legislative intervention was in respect of the ranking of compensation claims rather than their existence.

Further criticism of *Houldsworth*

154. The dissatisfaction with *Houldsworth* has not been limited to statements by leading Australian judges. It has also attracted criticism from the Company Law Committee of the English Law Society and Bar Council, and has been abandoned by the UK Parliament.

155. In September 1988, the Company Law Committee of the Law Society of England and Wales produced a memorandum on *Houldsworth*. The memorandum had the approval of the Law Reform Committee of the General Council of the Bar. In the introduction it was recommended that doubts about the rule in *Houldsworth* be removed by amending legislation. It was noted that "For many years the rule, a mere footnote in most textbooks, was largely ignored by practitioners", adding that

"The practical effects are potentially serious for investors." In April 1985 it had been recommended that the rule should be abolished. The memorandum refers in detail to "What the case decided". It reviewed the subsequent decisions including *Addlestone*. Under section 8 it is stated:

> "We understand that the Department of Trade and Industry is concerned that the abolition of the "rule" might lead to abuse. We do not think that concern is justified."

156. Under section 9 Conclusions the following is stated:

> "We consider that it [the 'rule' in *Houldsworth*] cannot be justified in the interests of investor protection and it fails to produce the benefits which are sometimes claimed for it. We therefore strongly recommend that the law be changed to make it clear that no person should be precluded from making any claim in contract, tort or otherwise by reason of his being a subscriber or shareholder in the company. If thought fit the rule could continue to apply on an insolvent liquidation, in the case of an unlimited company or to the extent of calls on partly paid shares. But we believe that it should be given a prompt burial as regards other situations. A short clause could achieve the desired effect and we suggest that the next Companies Bill would be an appropriate vehicle."

157. The impact of *Houldsworth* has been abandoned by the UK Parliament by way of section 131 of the Companies Act 1989 which was inserted into section 111A of the Companies Act 1985 which has been retained as section 655 of the Companies Act 2006.

158. In Technical Series Issue No 28 INSOL International *Update on Shareholder and Equity – Related Claims in Insolvency Proceedings* October 2013 at page 3 stated:

> "The English common law had previously acknowledged a rule, established in *Houldsworth v. City of Glasgow Bank* (1880) 5 App. Cas. 317, that a shareholder was prohibited from claiming damages from a company for misrepresentation inducing his subscription for shares unless he had first rescinded the subscription contract, and that once a company had entered liquidation such recission was impossible. This was largely nullified by section 111A of the Company Act 1985 (as inserted by section 131(1) of the Company Act 1989) but the rule was central to early judicial treatment of shareholder

claims and operated to negate any detailed consideration of the issue of subordination prior to the amendment of the 1985 Act."

159. Scott Wotherspoon in *Property by any other name: the trouble with shareholder claims in Australia* (2007) 81 ALJ 75 refers to *Oakes*, *Tennent* and *Houldsworth* and "attacks the basal legitimacy of those cases and describe[s] the consequences that their overruling will have on Australian company law". At page 88 it is stated:

"Once it is accepted:

(1) that a member is separate from the company itself;

(2) that a member can be creditor of the same company;

(3) the perceived inability to rescind the subscription contract after the commencement of the winding up has no bearing on a shareholder's entitlements in deceit;

(4) a desire to protect creditors by preventing an *indirect* return of capital cannot preclude a shareholder maintaining a claim to rescind and so likewise should not preclude the maintenance of a shareholder's claim for damages; and

(5) that a claim in deceit is functionally distinct from a claim for rescission and, as will be seen in Part IV, neither claims arise under the statutory contract,

then the justification for the continuation of the rule in *Houldsworth's case* in Australia falls."

160. On page 89 reference is made to the importance of certainty in the law:

> "But a rule that is considered by many to be incoherent or inequitable may nonetheless be a just rule. A rule that is predictable and operates with certainty has the attraction of having normative force. Once appraised of the rule, people can order their affairs to accommodate the rule or simply choose not to participate in the market in which the rule applies."

161. The author, however, concludes on page 92 as follows:

> "The arguments advanced in this article have attempted to demonstrate that judicial intervention in this area is warranted, indeed essential. The reasoning in the 19th century trio is consistent with fundamental principles of private law and property law. This inconsistency is the main reason for their erratic application. In the current state of the authorities, the certainty demanded of the rule of law is undermined to the point that it discredits the Australian legal system.
>
> The fact that the United Kingdom Parliament has sought to abolish the rule in *Houldsworth's case* might do no more than suggest that the High Court should leave any change to Parliament. It is submitted that this would be an inappropriate judicial response to the problem. As Australia's ultimate court of appeal, the High Court is uniquely placed to expose the errors inherent in the cases that have been subject to attack in this article …"

162. Marina Nehme and Margaret Hyland in *Houldsworth: An obsolete piece in the legislative puzzle* 12 UWSLR 124 briefly and critically examine the reasoning behind the *Houldsworth* 'rule':

> "An argument will be developed that this 19th century case is antiquated and serves only to complicate and confuse the application of the statutory regime. Accordingly, the principle in the case should be abolished by legislative intervention. It is only through parliamentary action that the real or illusory application of the *Houldsworth* rule can be erased once and for all from the corporate landscape."

163. The authors refer to the Australian case law including *Sons of Gwalia* adding at pages 150-151 that:

> It is important to acknowledge that even though *Houldsworth* was not applied in [*Sons of Gwalia*], the High Court did not abolish the *Houldsworth* rule. This leaves us today in an unenviable situation because there is confusion as to when the *Houldsworth* rule will apply … Due to the confusion, the legislator needs to intervene and abolish *Houldsworth*. The case is a relic of the past; a past that is based on a very different legal and economic foundation."

164. Di Lernia: *Should the rule in Houldsworth Case be abrogated by statute?* (2009, Masters Thesis, University of New South Wales) submitted that the Australian High Court "was justified in

choosing not to apply the rule in *Houldsworth's Case* and thus allowing shareholders to claim as unsecured creditors" but noted that "the rule may still prove good law in certain cases". The author seeks to demonstrate that "the decision in *Houldsworth* and subsequent interpretation and application of the "rule" therein suffer from deep flaws, and have been productive of relative injustice. It is argued that it is necessary to put the current uncertainty surrounding the applicability of *Houldsworth* in Australia beyond doubt through legislative abrogation of the rule in *Houldsworth's Case*." The author, in an Australian context, seeks to argue that "a policy of shareholder parity with unsecured creditors best meets the goals of insolvency and securities law regimes while contributing to the sustainability of a fair and efficient market, and investor participation in it."

Decision not to follow *Houldsworth* and reasons for such decision

165. Attempts may be made to distinguish *Houldsworth* from the facts of the present case before the Court. In *Houldsworth* the relevant entity was an unlimited co-partnership. In the present case, the Company is a limited liability company and the shares are fully paid up. The present case does not involve investors seeking to claim back money which they have contracted to contribute to pay the debts and liabilities of the Company. To that extent, it can easily be distinguished on the facts. However, the *ratio* of *Houldsworth* appears to have been interpreted subsequently as applying to limited companies. I have set out the headnote and some of the textbook commentary earlier in this judgment. I have also set out the comments of Lindley LJ in *Addlestone* at pages 205-206 and the comments of Peter Gibson LJ and Lord Browne-Wilkinson in *Soden* in respect of the *ratio* of *Houldsworth*. If *Houldsworth* were good English and Cayman Islands law, I do not think I could legitimately distinguish it.

166. Having had the benefit of detailed submissions on the issue I have however concluded that *Houldsworth* can no longer be regarded as good English law (indeed it has been abandoned by the UK Parliament). It is not a part of Cayman Islands common law. In my judgment, this is one of those rare cases where this court is justified, indeed obliged, to decline to follow an English decision.

167. Mr Millett, with hints against inappropriate "judicial activism", submitted that it would be "positively dangerous for the court to play lawmaker", and stressed the importance of certainty to investors who choose Cayman. He respectfully suggested that if the Grand Court refuses to follow *Houldsworth* there would be significant risks of "serious adverse unintended consequences", including "a serious impact on the willingness of lenders to lend". His warnings advanced to an assertion that if the Grand Court refused to follow *Houldsworth* it would "open floodgates to investor claims" and would turn the decision of the Cayman Islands Court of Appeal and the Privy Council in *Herald Fund SPC (in official liquidation)* [2016] 2 CILR 330 on their heads and would mean that investors would be far readier to redeem to exit their investment, for fear of being subordinated to investors who stayed in and then decided to file a misrepresentation claim. I also note the comments of Lord Collins in *Singularis Holdings Limited v PricewaterhouseCoopers* [2014] UKPC 36 in respect of judicial law-making and the respective roles of the judiciary and the legislature.

168. I do not, for one moment, accept the charge that in not following *Houldsworth* I would be playing lawmaker or becoming an inappropriate judicial activist. If there has been any judicial over-reach in this area of law it has arguably been committed by the House of Lords who in their judicial capacity in *Houldsworth* in effect amended or restricted section 158 of the English Company Act 1862 (not referred to in the judgments) to exclude claims by those who invested into an unlimited banking company with articles of partnership on the basis of fraudulent misrepresentation made by the directors and other bank officials. All I am doing is applying section 139(1) of the Companies Act (2023 Revision) of the Parliament of the Cayman Islands and declining to follow a judgment from a foreign jurisdiction which has been abandoned by its own Parliament and not followed in other jurisdictions including Australia and Bermuda. I am simply applying a local statutory provision untainted by a foreign judgment abandoned by its own Parliament. That is far from acting as a lawmaker or an inappropriate judicial activist.

169. Section 139 provides as follows:

> "Provable debts

> 139. (1) All debts payable on a contingency and all claims against the company whether present or future, certain or contingent, ascertained or sounding only in damages, shall be admissible to proof against the company and the official liquidator shall make a just estimate so far as is possible of the value of all such debts or claims as may be subject to any contingency or sound only in damages or which for some other reason do not bear a certain value.
>
> (2) Foreign taxes, fines and penalties shall be admissible to proof against the company only if and to the extent that a judgment in respect of the same would be enforceable against the company pursuant to the *Foreign Judgments Reciprocal Enforcement Act (1996 Revision)* or any laws permitting the enforcement of foreign taxes, fines and penalties."

170. Debts arising from claims for damages for misrepresentation fall within the wide wording of section 139(1) of the Companies Act (2023 Revision). By Cayman Islands statute these claims are admissible to proof against the Company. In arriving at that conclusion I am not injecting any uncertainty into this area of law. I am simply applying a local statutory provision untainted by *Houldsworth,* an authority arising in a foreign jurisdiction and not binding on this court and subsequently abandoned by its own Parliament. If the Parliament of the Cayman Islands wishes to legislate to amend section 139(1) or in respect of any "severe adverse unintended consequences" of this judgment, to use the cautionary words of Mr Millett, then that is a matter for Parliament.

171. If policy considerations are relevant one factor to consider would be investor protection in a country whose vibrant economy is in large part based on the attraction of outside investors using Cayman corporate vehicles. If those investments are based on fraudulent misrepresentations it would be unfortunate, to put it mildly, if such defrauded investor did not have a remedy against the relevant Cayman company. A remedy against a director may be insufficient. I was not addressed on any persuasive policy reasons as to why an investor in such circumstances should not in its capacity as a creditor have a claim against the Cayman company.

172. I have decided that I should not follow *Houldsworth* for a number of reasons:

(1) it is arguably contrary to or adds an unjustifiable judicial restriction to the plain wording of a local statute (section 139 of the Companies Act);

(2) it has been abandoned by the UK Parliament, and has been heavily and persuasively criticised by others and not followed in the High Court of Australia and the Supreme Court in Bermuda at first instance;

(3) its reasoning is inconsistent with contemporary company law;

(4) it is an obsolete English common law decision which has ceased to be authoritative in England; and

(5) it is simply not persuasive in the present context.

173. I have therefore concluded that the proper direction that I should give the Liquidators on Issue 2 is that they may proceed with the conduct of the liquidation on the basis that any Preferred Shareholder shall be permitted to submit a proof of debt asserting a claim for damages for misrepresentation against the Company, and any such proof of debt shall be adjudicated (and/or otherwise treated procedurally by the Liquidators) in accordance with Order 16 of the Companies Winding Up Rules (2023 Consolidation) (proof of debts in official liquidation).

Issue 3 – how do the misrepresentation claims rank in the liquidation?

174. I have considered the respective positions and arguments of the parties in respect of ranking. The Liquidators refer to the initial opinion of Mr Smith which contended that the misrepresentation claims would not be caught by section 2 or 5(c) of Schedule A to the Articles and would therefore rank *pari passu* with the redemption claims but ahead of the claims of the unredeemed Preferred Shareholders. This contention was repeated in a supplemental opinion of Mr Smith.

175. The Liquidators consider that section 37(7)(a) of the Companies Act would not apply as the redemption closing was scheduled to take place after the commencement of the Company's liquidation (and did not take place). The redemption payments would therefore fall outside the scope of section 37(7) by virtue of section 37(7)(a)(i).

176. The Liquidators also refer to the effect of the Articles in particular Article 102 and section 2(a) of Schedule A to the Articles. The question is whether section 2(a) is sufficiently broad to cover potential damages claims, including claims for fraudulent misrepresentation in connection with the subscription for the shares and therefore whether the entitlement of the Series D Shareholders fall to be paid in priority to claims for damages for misrepresentation of other Preferred Shareholders, in accordance with the waterfall set out in section 2(a). Section 2 provides that the entitlements of the Series D Shareholders are to be paid "[b]efore any distribution or payment shall be made to the holders" of the other series of shares. The Liquidators say that the critical question is whether this operates so as to subordinate claims for damages for misrepresentation by such shareholders. The Liquidators recognise that there are arguments both ways.

177. The Liquidators refer to the argument that the commercial purpose of section 2(a) is to entrench the priority of the Series D Shareholders, and the other series of Shareholders, relative to each other and this should, as a result, extend to all types of claim which in any way relate to the shares. Furthermore, any damages award for misrepresentation can be said to be literally a "distribution or payment". On the other hand, it can be said that it makes no sense to regard section 2(a) as extending to claims for damages for misrepresentation where it is said that the effect of the misrepresentation was to cause the shareholder wrongly to agree to the effect of the contractual waterfall under the Articles. Otherwise, there is circularity. The Liquidators add that the allegations made in the case presently before the Court include contentions that, not only did the fraudulent conduct induce them into subscribing for shares, but that it also persuaded them to accede to the creation of new shares and the admissions of new classes of investors whose rights under the amended Articles had priority.

178. In his Initial Opinion dated 13 April 2022, Mr Smith at paragraph 68 refers to arguments either way on Issue 3. One argument refers to the commercial purpose of section 5(c) to entrench the priority of the Series D shareholders and the other series of shareholders. At paragraph 69, Mr Smith says:

> "169. On the other hand, the language of section 5(c) does not clearly extend to such other claims. Moreover, it can be said that it makes no sense to regard section 5(c)

as extending to claims for damages for misrepresentation where it is said that the effect of the misrepresentation was to cause the shareholder wrongly to agree to the effect of the contractual waterfall. As noted above, the allegations made in the present case include contentions that, not only did the fraudulent conduct induce them into subscribing for shares, but that it also persuaded them to accede to the creation of new shares and the admission of new classes of investors whose rights under the amended Articles had priority."

179. At paragraph 70, Mr Smith comes off the fence and says:

"Overall, I think that a court would be likely to regard this latter argument as decisive."

180. In his Supplemental Opinion dated 2 November 2022, Mr Smith at paragraph 33 refers to "arguments both ways on this" and again mentions the "commercial purpose" argument. At paragraph 34, Mr Smith refers to paragraph 69 of his Initial Opinion and the "no sense" argument:

"34. On the other hand, as pointed out in the Initial Opinion at [69], it can be said that it makes no sense to regard section 2(a) as extending to claims for damages for misrepresentation where it is said that the effect of the misrepresentation was to cause the shareholder wrongly to agree to the effect of the contractual waterfall under the Articles. As we understand it, the allegations made in the present case include contentions that, not only did the fraudulent conduct induce them into subscribing for shares, but that it also persuaded them to accede to the creation of new shares and the admission of new classes of investors whose rights under the amended Articles had priority."

181. At paragraph 35, Mr Smith comes off the fence and concludes:

35. In these circumstances, we think that the Court would be more likely to take the view that section 2(a) is concerned with the return of capital to investors and not with damages claims made by such investors."

182. The Petitioners' position is that the misrepresentation claims do not fall within section 49(g) of the Companies Act and would rank as ordinary unsecured claims in the liquidation. They should therefore be provable in competition with the ordinary trade creditors of the Company and be paid *pari passu* on that basis.

183. The Petitioners refer to section 49(g) of the Companies Act and similar provisions in English and Australian legislation.

184. The Petitioners say that to determine the priority of the misrepresentation claims it must be considered whether the sums which would be due to the Preferred Shareholders are due to them "in their capacity as a member" of the Company "by way of dividends, profits or otherwise" and thus whether they fall within section 49(g) of the Companies Act. The position of the Petitioners is that the misrepresentation claims do not fall within such words, properly construed.

185. The Petitioners refer to *Re Addlestone*, *Soden* and *Sons of Gwalia* and submit that the answer to this issue should be that tortious claims for damages for misrepresentation made by a member against the Company of the type identified in the case presently before me do not fall within section 49(g). The Petitioners again with considerable persuasive force say that such claims are, properly analysed, not brought by a member in their character as a member, and they are not claims which have as their foundation rights or obligations arising under the statutory contract. To the contrary the claims are for damages arising by reason of a tort practised on the member by the Company, before the member became a member.

186. The Petitioners submit that Lord Browne-Wilkinson's comment in *Soden* in respect of negative claims (at page 325G) is not only *obiter* but, respectfully, it is also incorrect. This is because, like Earl Cairns in *Houldsworth*, it falls into the trap of conflating a subscription contract with the statutory contract composed of the articles and the relevant statutory obligations.

187. The Petitioners add that even if the claims could be said to arise out of the share purchase agreements, they are agreements which are separate to the statutory contract. In fact, the claims do not arise out of those agreements, properly analysed. The foundation of the misrepresentation claim is a (pre-contractual) tort. It is not the agreement itself (which is the product of the inducement), and the claim does not arise from some obligation owed by the Company to the member pursuant to their statutory relationship. I find these submissions compelling.

188. The Petitioners state that there is no principled basis for suggesting a member who suffers financial damages by reason of such conduct cannot prove in the Company's liquidation in parity with its ordinary creditors. Thus, the statutory construction suggested accords with common sense and inherent justice.

189. The Petitioners invite the Court to conclude that the damages claims which might be available to Preferred Shareholders do not fall within section 49(g) of the Companies Act and the claims of such members would rank as ordinary creditor claims to be paid *pari passu* with such claims.

190. In a section in their skeleton argument dated 10 May 2023 entitled "Subsequent Priority of Claims if Subordinated to Ordinary Claims", the Petitioners say that properly construed Article 102 and section 2(a) of Schedule A to the Articles are not concerned with payments made to members in respect of damages claims which all or some of those members may have. They are concerned with distributions (of dividends due or of the Company's capital) to members upon a liquidation of the Company. The Petitioners add that it is inherently unlikely that the members intended that section 2(a) of Schedule A to the Articles should extend to claims for damages for misrepresentation at all, but particularly where the effect of the misrepresentation was to cause the shareholders to agree to put those provisions into place.

191. Access and AI submit that if the Court is not with them on their primary contention and declines to follow *Houldsworth* then nonetheless their claims rank for proof in priority to the claims of the misrepresentation claimants, and neither *pari passu* with or subordinate to them. They add that come what may the misrepresentation claims should certainly not rank above the liquidation preference waterfall contained in section 2 of the Schedule to the Articles. They say that the Liquidators are non-committal on this issue (Initial Opinion of Mr Smith dated 13 April 2022 at

[68] and [69] and the Supplemental Opinion at [33] and [34]). I do not regard paragraph [70] of Mr Smith's Initial Opinion (quoted above) as "non-committal." Again I do not regard paragraph [35] of Mr Smith's Supplemental Opinion (quoted above) as "non-committal".

192. Access and AI submit that if the misrepresentation claims are admitted to proof in the liquidation they should rank neither ahead nor behind the relevant Preferred Shareholder's claim for the respective liquidation amounts. They say that there is no principled basis on which to accord them such priority or subordination. Their argument continues that since they remain members and their claims are in the character of a member, they must remain bound by section 2 and the upshot is that their damages claim will rank in accordance with the relevant position in the waterfall that the Preferred Shares the subject matter of their claims hold, and *pari passu* with other shareholder claimants for the relevant series liquidation amount.

193. Access and AI refer to *Addlestone*, *Webb Distributors*, *Soden* and *Sons of Gwalia*. They refer in particular to the comments of Lord Browne-Wilkinson in *Soden*, at page 323, that "sums due in the character of a member must be sums falling due under and by virtue of the statutory contract between the members and the company" and at page 325 "… the principle must apply equally to negative claims; claims based upon having paid money to the company under the statutory contract which the member says he is entitled to have refunded by way of contract." They seek to distinguish *Sons of Gwalia* and submit that there are other reasons for this Court not to follow it because (1) it created uncertainty for unsecured lenders and its effect was reversed in the Corporations Amendment (Sons of Gwalia) Act 2010; and (2) it is contrary to *Addlestone* and *Soden* which although not formally binding on this Court are nonetheless part of the common law of Cayman except to the extent that they are either inconsistent with Cayman Islands legislation or the Grand Court has developed the principle in a different way, neither of which they say is the case.

194. Standing back from the cases they refer to two underlying points:

(1) a claim for damages for misrepresentation which induced a contract of subscription for shares is, in economic terms, a claim for restitutionary damages in the amount of the contributed capital, just as it would be if the claim were for restitution based on, say,

mistake. The fact that the cause of action is a common law claim for damages based on a tort is not relevant: the practical outcome from both the shareholder's and the company's point of view is a return of capital. That is not so with an open market purchase since the loss claimed is not measured by reference to the subscription price but to the trade price at which the shareholder bought the shares from the seller, which may bear little relationship to the value of the capital originally subscribed for; and

(2) a claim for damages for misrepresentation inducing a subscription agreement is founded on the statutory contract because it is via the subscription agreement that the statutory contract comes into being and the member's obligation to contribute capital and other liabilities arise. It is artificial and over-narrow to limit "sums due to a member in his character as a member" to those contractually due to and from the company under the articles, as opposed to the subscription agreement and the articles taken together as a transaction. After all, a subscription agreement is simply an agreement to buy the contract of membership comprised in the articles, and with it the order of priority on a winding up. It would be absurd to make the application of section 49(g) depend on the cause of action, or the manner in which the claim is pleaded, or the measure in which the claim is pleaded, or the measure of the loss claimed.

195. Access and AI say that the next question is how, within section 49 (g), any admitted misrepresentation claims should rank in relation to other shareholders who are owed series liquidation amounts under section 2. They say there are three possibilities. Either (1) misrepresentation claimants rank ahead of all other Preferred Shareholders; or (2) they rank behind all other Preferred Shareholders, or (3) they rank *pari passu* with each series holders in their respective claims for the relevant liquidation amount. They, somewhat unconvincingly, say that the misrepresentation claimants cannot be accorded either priority to all other shareholders or subordinated to all other shareholders and that therefore leaves a *pari passu* approach on a series by series basis. I am unpersuaded by their submissions that the misrepresentation claims should map the position in the waterfall which the relevant series of shares in which they were induced to invest holds and that this would be a simple and principled result which would be consistent with

the contractual arrangements with the other shareholders and with the statutory scheme under section 49(g).

196. They make the generalised and somewhat vague submission that it would be unprincipled and unjust to afford misrepresentation claimants priority over all other shareholders and such would set section 2(a) at naught.

197. In conclusion on this issue Access and AI say that the claims for damages for misrepresentation are claims due to members in their character as members for the purposes of section 49(g) of the Companies Act. They add that as such they rank behind unsecured creditors but *pari passu* on a per series basis with the relevant series shareholders for their respective liquidation amounts pursuant to section 2(a) of Schedule A of the Company's Articles.

198. I have to say that on this issue I found Mr Levy's submissions and *Sons of Gwalia* far more persuasive than Mr Millett's submissions and Lord Browne-Wilkinson's *obiter* comment in *Soden*.

199. Section 49(g) of the Companies Act (2023 Revision) does not apply to misrepresentation claims. These debts are not debts due to Preferred Shareholders in their capacity as members and any sums due to those successfully advancing misrepresentation claims would not be due to them under the statutory contract between members and the company and the members *inter se* constituted by the relevant statutory provision. I do not find Lord Browne-Wilkinson's *obiter* comment in *Soden* on "negative claims" relied upon by Mr Millett persuasive. I agree with Mr Levy that a subscription contract is necessarily anterior to and separate from the statutory contract. A claim for misrepresentation as envisaged in the case presently before me arises from a tort independent to the statutory contract. The cause of action is not founded on the rights arising by virtue of and derived from the statutory contract. There is considerable force in Mr Levy's submission that on Lord Browne-Wilkinson's own analysis, a claim for damages for misrepresentation in the sense relevant to the case presently before me is not a claim brought "in the character of a member". This position is also strongly and persuasively supported by *Sons of Gwalia* (see in particular Gummow J at [52], [87]-[93]; Hayne J at [205] and [206]). I appreciate that on this ranking point *Sons of Gwalia* has in effect been abandoned by the Australian Parliament apparently following

representations by the lending industry. I nevertheless still find the judicial reasoning on this ranking point highly persuasive.

200. Furthermore, the contractual waterfall set out in the Articles is not applicable. Article 102 of the Articles provides that if the Company shall be wound up, the assets available for distribution amongst the members shall be distributed in accordance with section 2 of Schedule A. I agree with Mr Levy that Article 102 applies to the members in their capacity as members and the debts arising from misrepresentation claims are not debts arising in their capacity as members. The cause of action in tort is not based on the statutory contract. The debts are not member debts, they are creditor debts of those who are determined to have valid claims based on misrepresentations prior to becoming members. I do not agree that section 2(c) of Schedule A is wide enough to cover debts arising from damages claims for misrepresentation.

201. In respect of Issue 3 I have decided that I should direct that the Liquidators may proceed with the conduct of the liquidation on the basis that the claims of any admitted proofs of debt submitted by Preferred Shareholders in respect of damages for misrepresentation against the Company shall rank as unsecured debts of the Company.

Costs

202. There was also an ancillary issue in respect of costs which I can deal with fairly briefly as it was in effect agreed between the parties and what was suggested by way of costs orders was proper. In my judgment, the costs of the Liquidators of and incidental to the Application should be paid out of the assets of the Company as an expense of the liquidation. The costs of and incidental to the Application of the other parties appearing before the Court should also be paid out of the assets of the Company as an expense of the liquidation such costs to be taxed on the indemnity basis if not agreed by the Liquidators.

Apologies for length of judgment

203. I am conscious that this judgment is far too long and I apologise for that. By way of tentative explanation I offer the following:

(1) Firstly, with my present judicial commitments (including preparing for and presiding over hearings and delivering judgments thereafter) I simply could not in June and July find the time to further edit the judgment to reduce its length. As Winston Churchill and many others have been reported to have said in the past: If I had more time available my speech/contribution would have been much shorter.

(2) Secondly, on Issue 2 as I decided not to follow the House of Lords in *Houldsworth* I felt the need to explain myself in detail. I was provided with no detailed local Cayman guidance at appellate level or at first instance level as to the position of English precedent in Cayman Islands law and therefore spent many pages of this judgment reviewing relevant authorities from other jurisdictions and attempting a summary of the position under the laws of the Cayman Islands. I then had to deal with *Houldsworth*, *Soden* and *Sons of Gwalia* at some length.

(3) Thirdly, I also felt the need to explain in detail my decision not to follow the *obiter* comment of Lord Browne-Wilkinson in *Soden* on negative claims in respect of Issue 3.

Order

204. Counsel should forward a draft order reflecting the determinations contained in this judgment within 5 days from the delivery of this judgment.

David Doyle

THE HON. JUSTICE DAVID DOYLE
JUDGE OF THE GRAND COURT