IN THE GRAND COURT OF THE CAYMAN ISLANDS

5-03-12

FINANCIAL SERVICES DIVISION

The Hon Mr. Justice Andrew J. Jones QC
In Chambers, 28th February 2012 and
in Open Court, 5th March 2012

Cause No. FSD 60 of 2010 (AJJ)

IN THE MATTER OF THE COMPANIES LAW (2010 REVISION)

AND IN THE MATTER OF HARLEY INTERNATIONAL (CAYMAN) LIMITED (In Official Liquidation)

Appearances: Alexia Adda of Higgs & Johnson on behalf of Irving H. Picard in his capacity as Trustee for the liquidation of the business of Bernard L. Madoff Investment Securities LLC ("the Trustee" and "BLMIS")

Simon Dickson of Mourant Ozannes on behalf of the Joint Official Liquidators of Harley International (Cayman) Limited ("the Official Liquidators" and "Harley")

RULING

Introduction

1. This is an application by Mr. Irving H. Picard in his capacity as trustee for the liquidation of Bernard L. Madoff Investment Securities LLC which is in liquidation pursuant to the United States Securities Investor Protection Act 1970. I shall refer to them as "the Trustee" and "BLMIS". The Trustee was appointed trustee for the purposes of the liquidation by order of the United States Bankruptcy Court for the Southern District of New York made on 15th December 2008. I subsequently made a declaration pursuant to Section 241(1) of the Companies Law that the Trustee be recognized as the sole person having the right to act on behalf of BLMIS in this jurisdiction.[1] He subsequently commenced proceedings in this Court against Harley

[1] *Re Bernard L. Madoff Investment Securities LLC* [2010] (1) CILR 231.

International (Cayman) Limited ("Harley") as a result of which I have treated BLMIS as a claimant having a right to make and/or be heard upon applications made in the Harley liquidation. The Trustee now applies, pursuant to Order 24, rule 6 of the Companies Winding Up Rules, for an order that a report dated 13th January 2012 and prepared and filed by Harley's Official Liquidators ("the Report") be sealed. The Trustee's application is supported by the Official Liquidators.

2. CWR O.24, r.6 confers a limited power upon the Court to order that any document required to be put on the Court file in a liquidation proceeding shall be sealed and kept confidential for a specific period or until the happening of a specified event. There is jurisdiction to make such an order only if the Court is satisfied that (a) the information contained in the Report is of a confidential nature and will not come into the public domain unless and until it is filed in Court and (b) the publication or immediate publication of the information contained in the Report will harm the economic interests of the company's stakeholders. If the Court is satisfied in respect of both limbs of this test, the judge then has power to make an order that the Report be sealed for a limited time. This discretionary power has to be exercised for the purpose of protecting the economic interests of the general body of creditors (if the company is insolvent) or shareholders (if it is solvent). The Court's power cannot be exercised for the benefit of third parties.

Factual Background and Procedural History

3. Harley was incorporated on 1st September 1992 and carried on business as a collective investment company. In April 1996 it established a managed account with BLMIS through which it invested almost all of its assets. As at 30th November 2008 Harley's reported (unaudited) net asset value was approximately US$2.6 billion, practically all of which was represented by cash and securities apparently held in custody on its behalf by BLMIS. The Trustee characterizes Harley as a "feeder fund" which collected money from investors around the world and transferred it to BLMIS to be invested on its behalf. In fact, BLMIS was a huge "Ponzi scheme" operated by Mr Bernard Madoff who subsequently pleaded guilty to multiple counts of fraud and is now serving a sentence of imprisonment. Over the lifetime of its relationship with BLMIS, Harley had invested a total of about US$2.35 billion and withdrew about US$1.07 billion. Therefore, on a strict "cash-in/cash out" basis (disregarding reported profits which were fictitious), Harley claims to be a net loser as a result of the Madoff fraud, having a claim against BLMIS for about US$1.28 billion. As a

result of these events Harley was put into voluntary liquidation on the resolution of its sole voting shareholder on 31st March 2009 and the liquidation was brought under the supervision of the Court by an order made on 6th May 2009.

4. On 12th May 2009 the Trustee commenced an adversary proceeding against Harley in the United States Bankruptcy Court in which it is alleged that Harley knew or should have known that the account statements issued by BLMIS did not reflect legitimate trading activity and that Mr. Madoff was engaged in fraud.[2] For present purposes it is not necessary to describe the causes of action pleaded in this complaint save to say that it includes a claim to avoid the repayment of sums totalling US$425 million which were repaid by BLMIS during the 90 days immediately preceding the commencement of its liquidation on the basis that these payments constitute a preference under the Bankruptcy Code and/ the Securities Investor Protection Act. Harley's Official Liquidators did not serve any defence or otherwise respond to this action with the result that a default judgment was entered against Harley on 8th July 2009. By an order made on 21st January 2010 I gave the Trustee leave to commence proceedings in this jurisdiction, by which he asserts causes of action similar to those asserted in the US proceeding. On 19th January 2011 I directed that certain matters arising in this proceeding be determined as preliminary issues. Subject to the outcome of the Trustee's pending application for a stay of the proceedings, the trial of the preliminary issues is listed to commence on 15th October 2012. This proceeding raises difficult and complex issues upon which I do not need to make any comment for the purposes of ruling upon this application. Suffice it to say that, so long as the Trustee's claims have not been dismissed, he is being treated as a claimant or contingent creditor who has an interest in the Harley liquidation, such that he is entitled to make and/or be heard on applications in the liquidation proceeding.

5. On 12th October 2010 the Trustee issued a summons pursuant to Section 114 of the Companies Law seeking disclosure of information and documents held by the Official Liquidators which are relevant to potential causes of action which Harley may have against any Fortis entity, in particular its former administrator which was Fortis Prime Fund Solutions (IOM) Limited ("Fortis IOM").[3]

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[2] *Re Bernard L. Madoff Investment Securities LLC, Irvin H. Picard as Trustee –v- Harley International (Cayman) Limited,* No.08-01789 (BRL) pending in the United States Bankruptcy Court for the Southern District of New York.

[3] The Fortis Bank (Nederland) NV, of which Fortis IOM was a subsidiary, merged with ABN AMRO Bank NV with effect from 1st July 2010, as a result of which Fortis IOM changed its named to ABN AMRO Fund Services (IOM)

By an order made on 8th December 2010, I dismissed this application because it is the function of Harley's Official Liquidators, not the Trustee, to investigate whether or not Harley has any cause of action against its former professional service providers. I therefore directed the Official Liquidators to investigate and report upon the causes of action which may exist against Harley's former administrator and/or custodian. I directed the Official Liquidators to file a report within three months and serve a copy of it on the Trustee. This direction has an important consequence upon the present application. In the event, the Official Liquidators served a draft report upon the Trustee within the three month period stipulated in my order, but they did not complete it until 12th January 2012. A copy of the final Report was sent to the Trustee on the following day.

6. On 6th December 2011 the Official Liquidators issued a summons seeking the Court's approval of their remuneration for the period from 30th September 2010 to 31st October 2011. Such applications are normally dealt with as discreet matters on a regular six monthly timetable, but on this occasion the Official Liquidators included in their summons an application for "directions generally" in respect of the Report. This summons was served on the Trustee. It came on for hearing on 20th January 2012 when the Trustee was not represented, apparently as a result of an oversight. Having read the Report, I directed that it be filed.[4] The Trustee now seeks an order pursuant to CWR O.24, r.6 that the Report be sealed. As I understand it, this application is motivated by the fact that the Trustee disagrees with the conclusion expressed in the Report that proceedings should not be commenced against Fortis IOM. The Trustee says that he is in possession of new evidence which might lead to a different conclusion and that the disclosure of the Report to Fortis IOM might be prejudicial to any action which may in fact be commenced. This new evidence has not been disclosed to the Official Liquidators or to the Court. Whether or not there is any good reason for directing that this Report should not be disclosed to Fortis IOM at the present time, the Trustee's argument overlooks the fact that the effect of an order that it be sealed is that it cannot be disclosed to *anyone,* including Harley's stakeholders.

Limited. However, the Official Liquidators have continued to refer to the company by its former name in their Report and, for the sake of consistency, I shall do likewise.

[4] In fact, the original order made on 8th December 2010 required that the Report be filed. In effect, my order of 20th January 2012 merely confirmed and re-stated my previous order.

Court Files Relating to Liquidation Proceedings

7. Court files relating to liquidation proceedings are not open to inspection by the general public, a fact often overlooked by those more familiar with conducting bankruptcy proceedings in the United States. CWR O.26, rule 4(1) defines who may inspect these files as follows –

> "The following persons shall have the right to inspect the Court file in respect of a liquidation proceeding and take copies of filed documents –
>
> (a) the liquidator;
> (b) any former liquidator or controller of the company;
> (c) any person who was a director or professional service provider of the company immediately before the commencement of the liquidation;
> (d) the [Monetary] Authority, in the case of a company which carried on a regulated business; and
> (e) any person stating himself in writing to be a creditor or contributory of the company."

8. The content of a Court file relating to a liquidation proceeding will contain the following categories of documentation. First, it will contain the petition by which the proceeding is commenced, together with the supporting/opposing affidavits, any interlocutory summonses and orders, and the Court's ruling and winding up order.[5] Second, it will contain various certificates and notices reflecting key decisions made by the official liquidator, such as his determination of the company's financial status (as solvent, insolvent or of doubtful solvency), the currency of the liquidation and the composition of the liquidation committee. Third, the official liquidator's reports to creditors/shareholders (but not reports to the liquidation committee) are required to be filed. Fourth, documents relating to appeals against the rejection of proofs of debt and applications to expunge admitted proofs are put on the Court file. Similarly, in connection with solvent liquidations in which the register of shareholders is rectified, notice of rectification is filed but the underlying documentation will only be filed if there is an appeal

[5] The petition and the winding up order became a matter of public record (which can be inspected and copied by any member of the general public) as a result of being placed on the *Register of Writs and Other Originating Process* and the *Register of Judgments* respectively. Because winding up orders and supervision orders affect a company's status and are binding upon the whole world, they are also required to be registered with the Registrar of Companies and thereby become a matter of public record by a second route.

against the official liquidator's decision. Finally, the Court file will contain summonses, affidavits and orders relating to all the sanction applications made throughout the life of the liquidation proceeding, including the applications for approval of the official liquidator's remuneration. It follows that Court files often contain a very large number of reports and affidavits (sworn by or on behalf of official liquidators, creditors, shareholders and others) but it is relevant to note that the exhibits to these affidavits are not retained on the Court file.

9. The right to inspect and copy the contents of a Court file under O.26, rule 4(1) is not absolute. It is exercised by submitting a written request to the Registrar of the Financial Services Division who must satisfy himself about the "propriety" of the application which means that the Registrar must be satisfied that the applicant is a person falling within one or more of the categories specified in the Rule and that the application is made for a proper purpose. In deciding whether or not to allow inspection, the Registrar may consult with the official liquidator or the judge to whom the matter is assigned, but he is not bound to do so especially when the application is made on behalf of a creditor or contributory of the company. In the event that the Registrar refuses to allow inspection, the applicant may apply to the assigned judge who may allow inspection, either unconditionally or on such terms as he thinks fit. For example, it would be open to me to allow Fortis IOM, which clearly falls within Rule 4(1)(c), to inspect all the contents of Harley's Court file except for the Report or any other materials relating to the Official Liquidators' decision whether or not to commence proceedings against it.[6] Clearly, when an official liquidator decides (or is directed) not to commence proceedings against a former service provider, it should be informed of the decision. Conversely, when proceedings are threatened or commenced by an official liquidator, the defendant is entitled to know whether the proceedings have been sanctioned by the Court, but it will be inappropriate for the defendant to have copies of any reports, affidavits or written submissions which discuss the merits of the cause of action.

10. However, the effect of the Trustee's application to seal the Report would go beyond denying Fortis IOM the right to inspect and take a copy of it. The effect of an order under CWR O.24, rule 6(1) is that *no one* may inspect the document(s) in question. In particular, it would prevent all the investors (whether they are actual shareholders or unpaid redeemed shareholders) from inspecting the Report, notwithstanding that it was prepared for the purpose of informing them about the

[6] An order to this effect was made in *Re ICP Strategic Credit Income Master Fund Ltd (In Liquidation),* unreported 1st September 2011.

Official Liquidators' decision. This result is justifiable only if the Court is satisfied that disclosure (or immediate disclosure) to Harley's stakeholders will harm their own economic interests. Having exercised its right to inspect and take a copy of a document on the Court file, a creditor/shareholder may do what he pleases with his copy and may pass it on to others if he wishes to do so. Those who exercise their rights under CWR O.26, rule 4(1) are not subject to any express or implied duty of confidentiality. For this reason the Court assumes that disclosure pursuant to this rule will result in documents being put into the public domain. However, the threshold issue arising in this case is whether the Report is *already* in the public domain by virtue of its disclosure to the Trustee.

11. The Court's discretionary power to order that a document which has been or is required to be placed on the Court file should be sealed can be exercised only if both limbs of the test contained in CWR O.24 r.6(1) have been met. The Court must be satisfied that –

> "(a) the information in question is of a confidential nature and will not come into the public domain unless and until the document containing such information is filed in Court; and
> (b) the publication or immediate publication of the information contained in the document will harm the economic interests of the creditors or contributories of the company".

12. In my judgment the first limb of this test is not satisfied in this case. By disclosing the Report to the Trustee, the Official Liquidators have already put the information contained in it into the public domain. The final Report was given to the Trustee only on 13th January 2012 but he has been in possession of a draft since March of last year and I have no means of knowing what he has done with the document in the meantime or how he has made use of the information contained in it.

13. Notwithstanding that BLMIS must be a net debtor of Harley for at least US$1.07 billion, the Trustee is asserting claims against Harley. This is the basis upon which he is being allowed to make and/or be heard on applications in the liquidation proceeding. In this regard, he is in no different position from any other actual or contingent creditor. The recipients of official liquidator's reports are not subject to any implied duty of confidentiality and may use such reports and the information contained in them in whatever manner they think fit. This is well understood by official liquidators. By giving the Report to the Trustee, the Official Liquidators have already put it in the public domain. The Trustee was not asked to give any express undertaking to keep it confidential. Nor does the law impose any implied undertaking. The fact that the Trustee is a court appointed trustee who is exercising

statutory powers under the supervision of the United States Bankruptcy Court does not alter the fact that he was given the Report in his capacity as a claimant or contingent creditor. This Court has no jurisdiction give directions to the Trustee about the way in which he uses the Report. I assume that he will use it in whatever way he considers to be in the best interests of BLMIS and its investors/creditors, including Harley. It follows that the first limb of the test is not satisfied and, for this reason alone, I must dismiss the Trustee's application.

14. Even if the Trustee had entered into a confidentiality agreement on the basis of which it could be said that the information contained in the Report will not come into the public domain unless and until it is put on the Court file and accessed by some other creditor or shareholder of Harley, I would not have been satisfied that its publication or immediate publication will harm the economic interests of Harley's creditors and/or shareholders. The Trustee's case on the second limb of the test is put in a number of ways.

15. First, he asserts that the Report "is a private document between the [Official Liquidators], the Court and the Trustee". This reflects a misunderstanding of the Trustee's position in this liquidation. He is in no different or better position than any other claimant or contingent creditor, let alone the actual creditors. The Trustee's counsel was unable to explain why this Court should discriminate against all the other stakeholders by denying them access to a report which has been given to the Trustee. The purpose of the Report is to inform the stakeholders of the Official Liquidators' decision whether or not to commence proceedings against Fortis IOM. This is important information which they are entitled to know. If they disagree with the decision reflected in the Report, they would be entitled to make a sanction application for the purpose of asking the Court to direct the Official Liquidators to take a different course of action. I can see no proper justification for allowing the Trustee the opportunity to challenge the Official Liquidators' decision, but denying the same opportunity to all the other stakeholders.

16. Second, the Trustee says that "publication of the information would harm the economic interests of creditors and contributories as it would give an unfair litigation advantage to Fortis (or any other service provider) who would have access to a detailed analysis of any potential claim against them". I make a number of observations about this argument. It assumes that the Official Liquidators' decision will not be allowed to stand, but the Trustee did not explain why I should make this assumption apart from saying he has recently obtained some new evidence. It also

assumes that Fortis IOM will have an absolute right to inspect and take a copy of the Report which is not in fact the case. It is also wrong to say that the Report contains "a detailed analysis" of potential causes of action against service providers. To the contrary, it contains only a high level summary of the reasons why the Official Liquidators came to the conclusion that they will not commence proceedings against Fortis IOM.

17. Third, it is said that "a document in the nature of this Report, prepared for the purposes of litigation, would ordinarily enjoy absolute privilege". This argument ignores the fact that the Report was not prepared for the purposes of litigation. It was prepared for the purpose of informing the Court and Harley's stakeholders about the Official Liquidators' decision not to commence an action against Fortis IOM. No doubt being mindful of the fact that the Report will be put into the public domain, the Official Liquidators have omitted all reference to any legal advice which may have been obtained. It is not uncommon for official liquidators of failed companies to commence litigation against former professional service providers, in which case they will have to make sanction applications and report upon the progress and outcome of the litigation to the creditors and/or shareholders, who are entitled to be heard on whether such litigation should be commenced, continued or settled. It is incumbent upon official liquidators to prepare their reports in a way which does not unnecessarily include information, the publication of which would be counter-productive. However, creditors and/or shareholders are entitled to have the information which is necessary to enable them to make informed judgments about the course of action proposed by their official liquidators. In my judgment these Official Liquidators have drafted their Report in an appropriate way. It explains the reasons for their decision without unnecessarily disclosing a detailed analysis of the evidence and legal advice.

18. Fourth, the Trustee argues that "Although the Report was produced by the [Official Liquidators] pursuant to an order of the Court, in no other way does it bear the characteristics of a report produced in the context of a liquidation". I do not understand this argument. Reports of this kind are routinely produced in connection with a high proportion of the liquidation proceedings pending before this Court. The Trustee also makes the point that this particular report was produced pursuant to an order made as a result of his Section 114 application. This is true, but the investigation was done for the benefit of the Harley estate and the report was prepared for the purpose of informing the stakeholders (including the Trustee) about the outcome. When the Court makes a direction on the application

of a creditor or shareholder that an official liquidator shall carry out an investigation or any other kind of work, the applicant has no special proprietary interest in the work product. The applicant has no right to receive a copy of the consequential report to the exclusion of all the other creditors or shareholders, which is exactly what the Trustee is trying to achieve in this case.

19. Finally, I was told that the Trustee has recently obtained new evidence which is relevant to the Official Liquidators' decision. This evidence has not been disclosed to the Official Liquidators and the Trustee's counsel declined to give the Court any indication of its nature or the reason why it has only recently come to light. On this basis counsel for the Official Liquidators submitted that the decision reflected in the Report should now be treated as a provisional one which is subject to change. Whilst the Trustee's reluctance to explain the point does seem rather unsatisfactory, this Court should not substitute its own judgment for that of the Official Liquidators. However, the fact the Official Liquidators have decided to reconsider their decision in the light of whatever additional evidence may be forthcoming, does not lead to the conclusion that it will harm the economic interests of Harley's creditors or shareholders for this report to be published to them now.

Conclusion

20. The Trustee's application is dismissed. I direct that the Official Liquidators shall prepare and file a final report within 30 days. Whether or not the Official Liquidators should in the meantime file an addendum to the Report stating that it is subject to change is a matter for their judgment in the light of what they are told by the Trustee. Since this ruling raises a point about the meaning and effect of CWR O.24, r.6, it will be treated as having been delivered in open court.

Dated 5th March 2012

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