Re Leveraged Income Fund Ltd

Jurisdiction:	Jersey
Judge:	Deputy Bailiff
Judgment Date:	31 October 2002
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ROYAL COURT

(Samedi Division)

Before:

M.C. St. J. Birt, **Esq**., Deputy Bailiff, **and** Jurats Rumfitt **and** Potter.

In The Matter Of Leveraged Income Fund Limited
And In The Matter Of Part XXI of the Companies (Jersey) Law 1991.

Advocate M Chambers **for the Representors;**

Mrs Melanie Cavey, **on behalf of the Viscount;**

Mr R Henkhuzens, **a Director of Joshua Investments Limited, a Shareholder Company of Leveraged Income Fund Limited;**

Mr John Pallot, **Director of Compliance, Jersey Financial Services Commission**

Authorities

Palmer's Company Law: Chapter 15: 205, 219 – 221.

Pennington's Company Law: Chapter 7: pp 860–865.

In Re Suburban Hotel Company (1867) Ch. App. 737.

In re Representation of Jean (11 December, 1996) Jersey Unreported [1996/237].

Representation of the Directors of Leveraged Income Fund Limited, seeking an Order under Article 155 of the Companies (Jersey) Law 1991, winding up the Company.

Deputy Bailiff

THE

1 We are considering this afternoon an application by the Directors of Leveraged Income Fund Limited, ("the Company") for an order that the Company be wound-up under Article 155 of the Companies (Jersey) Law 1991 on the grounds that it is just and equitable to do so.

2 The Company was incorporated on 12 th March, 1998. It is a collective investment fund and is regulated under the Collective Investment Funds (Jersey) Law 1988. The Company has two classes of shares namely, ordinary income shares, and zero dividend preference shares. Both were quoted on the London Stock Exchange. There is also loan stock in issue. There are some one hundred and forty one million ordinary income shares in issue and some forty-one million zero dividend preference shares. The Company is in effect a closed-ended, split capital, investment fund.

3 As the name of the Company suggests, the stated intention of the Company was to provide greater returns to investors by borrowing. In other words there was to be an element of gearing. Unfortunately, the Company has suffered from the problems which have beset many split capital investment trusts and the value of the Company's assets has declined drastically. The position is that the Company has borrowings totalling some £41,000,000 from the Royal Bank of Scotland International Limited ("RBS").

4 As security for those borrowings RBS held a security interest over all the cash and investments of the Company. On 28 th August, 2002, RBS gave notice of default and it has subsequently exercised its security and taken title to, and control over all the assets of the

Company. As at 28 th September, 2002, these assets totalled just over £25,000,000. As can be seen, therefore, there is a deficit of approximately £15,500,000, which the Company still owes RBS.

5 All the shares in the Company are therefore worthless, and dealing in them was suspended by the London Stock Exchange some time ago. In the knowledge that the Company was insolvent and that the amount owed to RBS far exceeded the Company's assets, the Board of Directors wrote to shareholders on the 19 th August, 2002, proposing a creditor's winding-up. Under the Articles of Association this required the approval of specified proportions of each class of shareholder, as well as a special resolution at an Extraordinary General Meeting of shareholders generally.

6 The necessary resolution was passed by the required majority at meetings of the ordinary income shareholders and the loan stockholders. At the meeting of the zero dividend preference shareholders, the Chairman received an e-mail from an investor, who had originally supplied proxies with instructions to vote against the winding-up resolution in respect of that investor's shares. The e-mail changed that instruction, and instructed the Chairman to cast the proxy votes in favour of the winding-up resolution. However, the advocates to the Company advised the Chairman that, because of the format and late delivery of the purported change of voting instructions, they could not be taken into account.

7 As a result the winding-up resolution was not carried at the meeting of the zero dividend preference shareholders. The votes in respect of the relevant shareholder were counted neither for nor against the resolution. Had the new instructions been accepted, the resolution would have been carried by the required majority. Because the zero dividend preference shareholders had not supported the scheme, the winding-up resolution was not put to the Extraordinary General Meeting of shareholders generally; but on the basis of the proxies supplied to the Chairman, the resolution would have been carried by the required majority had it been put to the meeting.

8 As we have stated the Company is completely insolvent. It now has no assets whatsoever, RBS having exercised its security over all the Company's property. It still owes RBS some £15.5 million. The Board has no funds with which to prepare and circulate again the proposals for winding up and for holding the necessary meetings.

9 In those circumstances the Board now applies for an order that the Company be wound-up under Article 155 of the 1991 Law. RBS has agreed to put in up to £40,000, in order to fund this application and to fund the liquidation if the Court approves of the proposal.

10 Article 155 is based upon a similar provision of the Companies Act of the United Kingdom. English authorities are therefore of assistance. Although the English Courts have developed certain categories of cases where the Court will exercise its power under the just and equitable jurisdiction the Court is not confined to such categories. The words “just

and equitable" are general words. As Palmer's Company Law Vol. 3 para 15.219 puts it:

> ***"It has sometimes been suggested that there is an exhaustive list of situations that may fall within the scope of the "just and equitable" clause, but it now seems that although such classification may be convenient for purposes of presentation, the words "just and equitable" require a more flexible interpretation.*** In the words of Lord Wilberforce: "Illustrations may be used, but general words should remain general and not be reduced to the sum of particular instances.""

11 Nevertheless, one of the categories which has developed in English jurisprudence is where the substratum of the company has gone, i.e. where the main object for which the company was formed has become impracticable (see *In re Suburban Hotel Company* (1867) Ch. App. 737). Pennington on Company Law puts it as follows at page 860:

> ***"A company's substratum is the purpose or group of purposes which it was formed to achieve, in other words, its main objects.*** If the company has abandoned all of these main objects and not merely some of them, or if it cannot achieve any of its main objects, its substratum has gone, and it will be wound up."

Further on in the paragraph it is stated:

> ***"However the mere fact that a company has suffered trading losses will not destroy its substratum, unless there is no reasonable prospect of it ever making a profit in the future, and the court is most reluctant to hold that it has no such prospect"*** .

12 The Court is in doubt that the substratum of this company has gone. The Company was formed to provide an investment vehicle for shareholders. In the events which have happened all the funds have been lost. The Company no longer has any money to invest for its shareholders; on the contrary it is grossly insolvent. There is no prospect whatsoever of the Company ever being able to recommence its investment activities.

13 The Court must clearly take into account that the shareholders, having been given the opportunity of placing the Company in a creditors winding-up, did not do so. It is clear from the evidence that we have received that this was because of a technicality affecting a substantial block of votes which the holder wished to cast in favour of the resolution to wind-up. If those votes had been allowed the resolution would have been carried.

14 The shareholders had been notified of this application and of the fact that they may express their views to the Court. The Court has received a letter from one shareholder opposing the winding-up on the grounds that, if the equity markets were to recover there might eventually be some value for shareholders. The difficulty with this suggestion is that RBS has exercised its security interest over all the Company's assets so that those assets now

belong to RBS not to the Company. The Company no longer has any assets. Accordingly, even if there were to be a substantial revival in the equity markets, this would avail the Company nothing as it has no investments to benefit from such an up-turn.

15 At the original hearing on the 23 rd April, Mr Robert Henkhuzens, a director of Joshua Investments Limited, which holds shares in the Company, appeared and addressed the Court. He referred to the fact that the Company had a management contract with Aberdeen Asset Managers (Jersey) Limited which in turn was advised by Aberdeen Asset Managers Limited in the United Kingdom. The Aberdeen Group manages a number of split capital investment trusts which have incurred very substantial losses. Furthermore, he pointed out that some of the directors of the Company were directors of other split capital trusts managed by the Aberdeen Group. In short he submitted that the Company and/or the shareholders may have a claim against the Aberdeen Group or the directors of the Company. He was concerned that, if only £40,000 were available to the liquidators, they would be unable to investigate and get advice on any potential liability of the directors and Aberdeen, nor would they be able to afford to launch any proceedings even if advised that the Company did have a claim.

16 The Court well understood those concerns. We therefore adjourned the matter until today in order that a representative of the Viscount could attend and address us. Clearly a declaration of désastre might be an alternative route to a just and equitable winding-up if it would offer a better prospect of the Company being able to investigate, and if so advised, pursue action against the directors and advisers of the Company.

17 We have today heard from Mrs Cavey on behalf of the Viscount. It is clear that the Viscount would not be in any better position than the liquidators to pursue such matters, because the Viscount is dependant upon the assets of the company en désastre to fund any litigation. Indeed arguably the Viscount might be in an even worse position because the £40,000 from RBS may not be forthcoming if there is a désastre as opposed to a winding-up under Article 155. It is quite clear that RBS is under no legal obligation to provide any funds for such matters.

18 In the circumstances, we see no advantage in a désastre. The fact is that the Company has no assets with which to pursue any possible litigation. That does not, of course, prevent the shareholders from banding together and taking action against the directors and advisers if they are advised that they have a case. Alternatively, they might agree to fund the liquidators in investigating and possibly bringing such a case.

19 We appreciate this is far from ideal and we can understand the anger and disappointment of the shareholders; but the Company being without assets we see no way of assisting them by means of any order which is within our jurisdiction as a Court sitting to consider whether the Company should be wound-up.

20 We also heard today from a representative of the Jersey Financial Services Commission. We were informed that the Commission is considering the matter and will shortly decide whether to launch a formal investigation as to whether there have been any regulatory breaches in relation to the Company. Their jurisdiction is confined to breaches of the regulatory regime. The Commission has no jurisdiction to bring an action for simple negligence in the performance of their duties by the Directors or advisors.

21 We have concluded that there is no purpose in keeping this Company going. It has no assets and it cannot even pay for routine expenses such as the annual registration fee in order to keep it in good standing. There is no prospect of it ever having any assets again and its substratum has undoubtedly gone. Rather than the Company just being struck-off in due course, it would be preferable for there to be an order winding it up, under the supervision of liquidators, who could prepare final accounts and so on. As we have said, RBS is willing to contribute the necessary funds for this purpose even though it is under no legal obligation to do so.

22 In the circumstances, we order that the Company be wound-up on the grounds that it is just and equitable to do so, and we appoint Mr A Dann and Mr C Legge both of Ernst & Young LLP as joint liquidators of the Company.