IN THE GRAND COURT OF THE CAYMAN ISLANDS

CAUSE FSD 16 OF 2009 ASCJ

IN THE MATTER OF THE COMPANIES LAW (2007 REVISION)

AND IN THE MATTER OF THE SPHINX GROUP OF COMPANIES (IN OFFICIAL LIQUIDATION) AS CONSOLIDATED BY THE ORDER OF THIS COURT DATED 6TH JUNE 2007 ("SphinX")

IN CHAMBERS
BEFORE THE HON. CHIEF JUSTICE
THE 26TH MARCH 2013

Appearances: Mr. Thomas Lowe QC and Mrs. Cherry Bridges for the Joint Official Liquidators of SphinX ("the JOLs")

Mr. Alan Turner for the Liquidation Committee ("the LC")

JUDGMENT

1. The JOLs apply for an increase in the hourly rates that they may charge to the SPhinX Liquidation Estates for their services. These increases are sought to be effective retroactively from 1st July 2012. The application requires a review of the history.

2. The rates agreed between the JOLs and the LC for the period 27 July 2006 (the commencement of the liquidation) to 1st January 2010 are in the second and third columns of the Table following.

3. The current rates, which were set by the Court effective as from 1st January 2010[1] are set out in the fourth column.

[1] See Judgment of 29th November 2010 in this Cause.

4. The proposed rates, to be effective from 1st July 2012, are set out in the fifth column and the proposed percentage increases which they involve, in the sixth column.

GRADE	Agreed Rate as at 27 July 2006 US$	Agreed Rate as at 27 July 2008 US$	Rate set by the Court as at 1 January 2010 US$	Proposed new rate	Proposed Percentage Increase
Managing Director	495	585	655	790	21%
Director	N/A	440	492	625	29%
Senior Manager	360	400	448	550	23%
Manager	275	350	392	460	17%
Senior Accountant/ Analyst	210	245	274	340	24%
Junior Accountant/ Analyst	105	125	140	210	50%
Administrator	N/A	65	106	106	-
Consultant	N/A	125-245	284	284	

5. As justification for the increases, the JOLs posit the increased costs of doing business. These they identify as the increase in work permit fees; the costs of IT Services and equipment and other overheads such as rent.

6. The JOLs also argue that the increases are also justified by reference to the statutory rates set by the Insolvency Practitioner Rules (IPRs).

7. For the following reasons, I do not consider it appropriate to grant an increase in rates by reference to the JOLs' increased costs of doing business. A primary reason is that those costs would not provide an objective basis for approval of fees. An obvious consideration is that the IPR rates upon which the JOLs' rate have been set and approved, were themselves set as a benchmark having regard to a compendium of relevant factors central to which were the acknowledged costs of doing insolvency business in the Cayman Islands. And, as one would expect, it was then recognised that as those costs will increase from time to time so should the IPR rates be revised

to ensure that they continue to be an appropriate basis for the remuneration of liquidators.

8. By contrast to that objective approach, the kind of enquiry into their subjective costs of doing business now proposed by the JOLs would be a departure from the IPR rates as an objective benchmark generally for the setting of fees for insolvency work.

9. The foibles of such a subjective approach are also readily identified by reference to the present context.

10. Apart from anything else, as the LC argues through Mr. Turner, the SPhinX engagement is one that has earned the JOLs something in the order of $35 million in fees so far; all paid in a timely manner from the available assets by virtue of their highly liquid state from near the outset of the liquidation process. It would therefore be quite meaningless to consider the JOLs' costs of doing business as a basis for increasing fees without considering how those costs translate into the JOLs' work for the SPhinX estate itself and so into the level of profitability of the engagement. It has not been denied by the JOLs that the SPhinX engagement has been and will continue to be, even at the current rate of fees, a profitable engagement.

11. Thus, the JOLs may not rely on their costs of doing business for the SPhinX estate without also disclosing the extent of the profitability of their engagement, but the latter is precisely the kind of information that they (and all other liquidators) have steadfastly refused to disclose; citing their proprietary right to business confidentiality.

12. This exactly is the kind of debate that the IPR rates were designed to avoid. They are based on considerations which are intended to render them acceptable as representing

the rates of remuneration that liquidators might reasonably and objectively expect to be paid for their services in this jurisdiction. Before the IPR rates were first set, there was full consultation with the insolvency practitioners whose representatives served on the rule making body – the Insolvency Rules Committee – which is established under section 154 of the Companies Law. The IPR rates are therefore to be regarded as having been set by reference, among other things, to the costs of conducting liquidation work in this jurisdiction, with an uplift for a reasonable margin of profit for liquidators.

13. The IPR rates are however expressed as bands of rates, leaving it to the liquidators, and their respective liquidation committees, to agree on the correct points within the band or failing agreement, for the Court to decide on the correct points.

14. A number of factors go into making that decision, not least the anticipated complexity and longevity of the particular liquidation engagement. Also considered is the availability of liquidity for ready payment of the liquidators' fees and so, the absence of delay in payment and risk of non-payment.

15. As to the longevity of the assignment, the JOLs now also express the view that the SPhinX engagement –now more than six years old – could well come to an end within the next few months. Thus, they say that expected ongoing longevity of the engagement should not be a factor going to discount their fees rates.

16. I do not share that view. Apart from anything else, there is still on foot complex litigation brought by the JOLs with the leave of this Court before the New York Court and for which no final trial date has been set. When it does get underway, the trial itself could run for a number of months.

17. As to the complexity of this engagement, that has been a factor taken into account from the outset when the JOLs' fees were first set in 2006 and when it resulted in the setting of the fees at a point within the band commensurate with the rates allowed for other complex assignments undertaken in this jurisdiction.

18. Longevity is a factor that usually operates to reduce the level of fees in a complex engagement where large volumes of work would be undertaken for a long period to time. As such, it was not, however, taken into account until 1st January 2010[2]. Only effective as of that date did this Court determined that a volume discount of 10% should apply to the level of fees to be charged to the estate, a determination made after it was conceded by the JOLs that some level of discount (albeit proposing only 5%) was appropriate.

19. The 10% rate of discount was then set having regard not only to volume of work but also, among other considerations, to the fact that the liquidity of the estate had benefitted the JOLs from very early in the liquidation process ensuring that their fees had always been paid immediately. In fact, in keeping with the IPRs, the JOLs have paid themselves 80% of their fees as soon as invoiced, with the remaining 20% paid after final approval is obtained from the Court (in the absence of agreement with the LC).

20. These are all factors which lead me further to conclude that the proposed increases are excessive. The reference point must, of course, be the existing IPR rates. By reference to them, the proposed increases would average more than 27% above the fees to be charged, effective 1st January 2012, for the six categories of personnel proposed (as shown in column 6 in the Table above).

[2] As decided and explained in the Judgment delivered on 19th October 2012 in this Court.

21. Although such increases would still keep the rates within the bands of the current IPR rates, I can find no justification for such large percentage increases in the context of this liquidation where the JOLs have enjoyed since commencement, the benefit of reasonably high rates of remuneration paid in a timely fashion for large volumes of work from sources of income which are under their immediate control and so without any risk of non-payment. The JOLs have also had the benefit of timely, regular and significant increases in their charge out rates since 27 July 2006 (also as shown above in the Table for 2008 and 2010).

22. A final but equally important basis for objecting to the proposed increases is that they would effectively avoid the volume discount of 10% approved in the Judgment of 19th October 2012.

23. It is in this regard very telling that Mr. Krys, one of the JOLs, seeks to explain at paragraph 30 of his 113rd Affidavit filed in support of this application, that "*the commercial effect of the volume discount applied to the period 1 January 2010 to 30 June 2012 has resulted in the JOLs' rates being below the IPR in one fee category and well below the mid-point across all fee rate categories*".

24. This view reveals a misunderstanding of the reason for the discount. The discount was not applied by reference to its relationship to the IPR rates. They were justified and applied because of the very large volume of work which has been provided to the JOLs by the estate under the favourable circumstances and rates mentioned above; all as explained more fully in the judgment of the 19th October 2012. Allowing an increase in charge out rates now even in part to offset "*the commercial effect*" of the discount, would therefore defeat its purpose. Thus, I think it is fair to assume that the

high average rates of increase of 27% proposed by the JOLs would include at least 10% aimed at achieving that offset and so, to that extent, must be disallowed.

25. I accept, however, that some increase in the charge out rates is justified given the general effect of inflation since 1st January 2010. When an increase to the rates was last allowed.

26. But given the background and context of the matter as discussed above, including the likely ongoing nature of the assignment at relatively high volumes of work, I consider the remaining 17% proposed increase to be still too high.

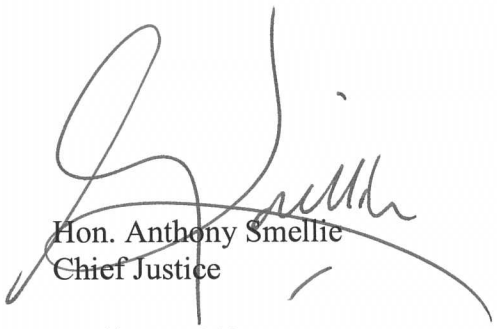
27. I consider an increase of 7.5% - thrice that of 2.5% proposed by Mr. Turner on behalf of the LC referencing the increase recorded in last year's Government C.O.L. indices – to be reasonable. That is the increase that I will allow to be applied to each of the grades of personnel identified by the IPRs bearing in mind that no increase in rates has been allowed in the three years since January 2010.

28. The rates will accordingly be as set out in the Table following; effective 1st January 2012.

Grade	Current Rates US$	Increased Rates as of January 1 2012 US$
Managing Director	625	704
Director	492	529
Senior Manager	448	482
Manager	392	421
Senior Accountant/ Analyst	274	295
Junior Accountant/ Analyst	140	151
Administrator	106	114
Consultant	284	305

29. Mr. Lowe also submitted that the rates to be set now should anticipate the increased rates which are expected to be set shortly by the Insolvency Rules Committee as the IPR rates.

30. In my view, it is better to await the setting of such new rates when the JOLs may again apply for any uplift for the future by reference to them and having regard also to the increases now allowed.



Hon. Anthony Smellie
Chief Justice

April 11, 2013