IN THE SUPREME COURT OF JUDICATURE OF JAMAICA

COMMERCIAL DIVISION

CLAIM NO. 2010 HCV02413

BETWEEN	**OCEAN CHIMO LTD**	**CLAIMANT**
AND	**ROYAL BANK (JAMAICA) LTD (RBC)**	**1ST DEFENDANT**
AND	**ROYAL BANK (T &T) LTD (RBC)**	**2ND DEFENDANT**
AND	**ROYAL BANK OF CANADA**	**3RD DEFENDANT**
AND	**SAMUEL BILLARD**	**4TH DEFENDANT**
AND	**RAYMOND CHUNG**	**5TH DEFENDANT**
AND	**GREG SMITH**	**6TH DEFENDANT**

IN CHAMBERS

Mr. John Vassell, Mr. William Panton and Mr. Emile Leiba instructed by Dunn Cox for the Applicants/ Defendants.

Mr. Roderick Gordon and Mr. Anthony Levy instructed by Gordon McGrath for the Claimant/Respondent.

HEARD: 13TH May, 10th July and 31st July 2014

COMPANY–CLAIM BROUGHT BY COMPANY DIRECTORS AGAINST DEBENTURE HOLDERS-COMPANY LATER PLACED IN RECEIVERSHIP–APPOINTMENT OF RECEIVER BY DEBENTURE HOLDERS-DIRECTORS CONTINUING CLAIM WITHOUT CONSENT OF RECEIVER–DEBENTURE HOLDERS APPLYING TO HAVE CLAIM STRUCK OUT FOR FAILING TO SECURE RECEIVER'S CONSENT-CONCURRENT POWER IN RECEIVER AND DIRECTORS TO BRING ACTION IN THE NAME OF THE COMPANY-WHETHER CONSENT OF RECEIVER REQUIRED-WHETHER INDEMNITY NECESSARY IF NO CONSENT IS GIVEN -WHETHER CLAIM SHOULD BE STRUCK OUT IF NO SECURITY FOR COSTS IS PROVIDED-APPLICABILITY OF SECTION 388 OF COMPANIES ACT.

Edwards J.

THE APPLICATION

[1] The Defendants filed a Notice of Application for Court Orders on November 5, 2013 seeking an Order of the Court that the Claimant's claim be stayed until it provided proof of consent by the receiver, appointed by them, to continue the claim before the court; failing which the Claimant be ordered to provide indemnity or undertaking from a third party for the costs which it may incur in this claim and any costs which it may be ordered to pay the Defendants in this claim. The Defendants also sought an order that if neither the consent of the receiver nor the indemnity or undertaking is provided then the claim against the Defendants stand struck out.

[2] The Claimant was placed in receivership on August 19, 2011 pursuant to mortgage debentures issued by it on September 16, 2005 and April 28th 2008 as part of the security for loans made to the Claimant by the 1st and 2nd Defendants. Pursuant to the mortgage debentures, the Claimant's assets were charged as security for all the monies due and owing from it. The debenture dated April 28, 2008 was in essence the same as the one made in 2005.

Background

[3] The breakdown of the relationship between the Claimant and 1st and 2nd Defendants (between whom no distinction will be made for the purposes of this application) has spawned a great deal of litigation and countless contested interlocutory applications have been made before this court. As a result, costs orders have been made against the Claimant and future costs orders are not improbable. The origin of the relationship involved a loan agreement between the Claimant and the predecessor banks to the 1st and 2nd Defendants, secured by a debenture over the assets of the Claimant and a guarantee provided by Mr. Delroy Howell, himself a Director and Chairman of the Claimant. The company defaulted on the loan and the 1st and 2nd Defendants exercised powers under the debenture to appoint a receiver and also sued

the guarantor to recover the sums amounting to almost thirty-five million dollars ($35,000,000.00).

[4] The Claimant had commenced separate proceedings against the 1st and 2nd Defendants in the year 2010 seeking damages based on allegations of breaches of the loan agreement, fraudulent manipulation of the interest rates and conspiracy. The 1st and 2nd Defendants who are successors of the banks holding the debentures over the Claimant's properties since September 16, 2005, appointed a receiver in August of 2011. The Defendants placed the Claimant Company in receivership after several formal demands for repayment of the loan were not met. Following the appointment of the receiver, the Claimant applied to amend the claim to commence proceedings against the 3rd to 6th Defendants who are servants and or agents of the 1st and 2nd Defendants. Since the receiver was appointed he has not filed any applications in this matter or commenced any proceedings in relation to his appointment.

[5] The main issue raised by this application is, firstly, whether the directors of Ocean Chimo have the power to commence or continue litigation without the consent of the receiver and secondly, if no consent is required, are the directors obliged to provide an indemnity against any possible liability for costs to protect the assets of the Claimant which are in receivership against a possible cost award in favour of the Defendants. In the affidavit from Julianne Mais-Cox filed in support of the application, it was averred that the institution and continuation of the proceedings against the 3rd, 4th 5th and 6th Defendants, since the appointment of the receiver, placed the assets of the Claimant at risk. It was also averred that it prejudicially impinged on the 1st and 2nd Defendants by imperilling the Claimant's assets in the event that cost orders are made against the Claimant in favour of the Defendants. The Defendants' application is therefore for an order that the Claimant provides security for costs, on the basis that the assets of the company may not be sufficient to satisfy the debenture, in the event that its assets are dissipated by its costs of litigation and any costs orders made against it in favour of the Defendants.

THE APPLICABLE LEGAL PRINCIPLES

[6] The first issue to be determined is whether the consent of the receiver is required for the claim to be allowed to continue in these courts. There is common ground between the parties that the directors of a company do not lose their power to conduct the company's affairs upon the appointment of a receiver/manager. In the case **Moss Steamship Company Ltd v Whinney** [1912] AC 254, Lord Atkinson explained that the valid appointment of a receiver would ordinarily supersede but not destroy, annihilate or dissolve a company's power, through its own organs, to conduct its own affairs; both continue to exist. However, because the receiver supersedes the company in relation to the conduct of its affairs, whilst a receiver is in place the organs of the company cannot enter into contracts, sell, pledge or otherwise dispose of property in possession of or under the control of the receiver.

[7] In **Newhart Development Ltd v Co-operative Commercial Bank Ltd** [1978] 2 All ER 896, it was held that the appointment of a receiver did not divest the directors of their power to institute proceedings in the company's name provided they do not interfere with the receiver's job of realizing the company's charged assets nor prejudicially affect the debenture holder by imperilling the assets. Part of the head notes to the judgment also reads:

> *"..the directors were under a duty to bring an action which was in the company's interest because it was for the benefit of creditor's generally, and to pursue that right of action did not amount to dealing with the company's assets so as to require the receiver's consent or concurrence. Since the plaintiffs' action would not stultify the receiver's function of gathering in the assets, the plaintiffs were not required to obtain his consent to bring the action..."*

In **Newhart's** case the directors of the company undertook to meet any award of cost made against the company, if litigation failed, so as not to dissipate the company's assets.

[8] In **Tudor Grange Holding Ltd and another v Citibank and another** [1992] Ch 53, Lord Browne-Wilkinson VL felt himself bound by the decision in **Newhart's** case

where it exactly covered the points in issue before him. Although he held doubts about the receiver and the directors having the same set of powers to bring proceedings, he was clear that company directors did not have the power to bring an action in the name of the company where to do so would prejudice the receiver's position. He noted that the action commenced by the directors directly impinged on the company's asset in receivership in that when the directors commenced proceedings they held no indemnity against the liability of the company's asset to satisfy a cost order against it. In that regard he distinguished **Newhart's** case from **Tudor Grange**. He did, however, note that given a late indication that an indemnity to protect the possibility of dissipation of assets could be forthcoming, the claim would not be struck out only for want of consent from the receiver.

[9] In **Pan Caribbean Financial Services Ltd v Western Cement Company Ltd** (in receivership) [2011] JMCA Civ. 2 the Court of Appeal of Jamaica examined both **Newhart** and **Tudor Grange** cases and accepted the principle that although the directors had the power to bring an action on behalf of the company even after the appointment of a receiver, they had no right to do so where the result would be to prejudice the position of the receiver. In the case of **Pan Caribbean Financial Services Ltd**., the director had indicated a willingness to indemnify the company against any cost attendant on the litigation.

ANALYSIS

[10] Counsel for the Defendants contended that even though the directors retained the power, as an organ of the company, to bring an action in the name of the company, this power was subject to conditions. It was argued that one such conditionality was that, in the absence of the receiver's consent, the directors must provide an indemnity against the dissipation of company assets and the action must not interfere with the receiver's function of getting in the company's assets.

[11] The Claimant contended that there was no evidence from the applicants that the company's assets were in peril or that they were in danger of dissipation brought on by

the action. In **Newhart's** case Shaw LJ, in looking at the function of the receiver and his powers under the debenture trust deeds, ruled that:

> *"..the provision in the debenture trust deed giving him that power is an enabling provision which invests him with the capacity to bring an action in the name of the company. It does not divest the directors of the company of their power, as the governing body of the company of instituting proceedings in a situation where so doing does not in any way impinge prejudicially on the position of the debenture holders by threatening or imperilling the assets which are subject to the charge."*

Two obvious question that would arise therefore, if this statement of the law is correct, which I accept it is, are firstly; whether the position of the receiver will be prejudiced if the claim is allowed to continue and secondly whether the assets of the Claimant would be imperilled or threatened.

[12] In this case the Claimant Ocean Chimo Ltd**.** took a loan from the 1st Defendant. The action arises from that agreement. Ocean Chimo claimed that due to conspiracy in the Defendants, breach of contract, negligence, fraud and the action of the 1st Defendants in manipulating the interest rate at which the loan was agreed, it resulted in the company being unable to pay its debts. It is this failure to collect on the debt which resulted in the receiver being appointed.

[13] The charge for the loan was Ocean Chimo's only asset, the hotel which consists of the pure real estate and the business as a going concern. Ocean Chimo is the holding company whose sole business is to hold the asset, the subject matter of the charge. The receiver was appointed by the 1st Defendant, the other Defendants are connected parties, being the parent company and the servants and/or agents of the 1st Defendant.

[14] The claim is therefore brought against the said entity that appointed the receiver. For the receiver to give his consent to the continuation of this action it would place him in the invidious position of suing his own master. In actual fact the Claimant had averred

that it was challenging the appointment of the receiver and has brought action in this court against the receiver for failures in the performance of his duties and in regard to his obligation to the Claimant Company.

[15] This case is an unusual one and in some respects an incestuous one. The Defendants are the debenture holders and their connected parties. The Claimant is the holding company for the single asset which was the subject of the charge. The receiver was brought in to realize this single asset. The receiver was appointed by the debenture holders. The debenture holder has also sued on the guarantee for the loan. That guarantor is a director of the Claimant Company.

[16] The receiver was appointed under the debenture in the usual form at paragraph 23a which stated:

> *23 "A receiver so appointed shall have the authority and be entitled to exercise any general power conferred upon him by common law or statute and in addition and without limiting or excluding any such powers, the receiver and the bank (so far as the loan permits) shall have power.*
>
> *(a) To enter upon and to take possession of, collect and get in the charged properties, or any part thereof, exercise in respect of the shares all voting or other powers or rights available to a registered and/or beneficial owner thereof (as appropriate) in such manner as he may think fit and to take, defend, or abandon any proceedings in the name of the chargor or otherwise as may seem expedient."*

[17] I started out by asking whether the consent of the receiver was really required. It is clear from the law that the consent of the receiver is not required. The debenture provided for a receiver to be appointed and if necessary, to enter upon and take possession of; collect and get in the charged properties and to take defend or abandon any proceedings in the name of the chargor. The receiver has been in place since 2011 and is already in control of the Claimant's asset, the subject of the charge. There is no evidence that this action brought by the directors would stultify or frustrate the receiver's action in realizing the assets of the company.

[18] What we have here is the clash of two duties. On the one hand there is the duty of the receiver to protect the interest of the mortgage or debenture holder in realizing the assets which are the subject of the charge and on the other there is the duty of the organs of the company to protect the company and its shareholders. In so far as the duty of the receiver involves the necessity to bring proceedings in the course of realizing the assets of the company, he is so empowered by the debenture. I agree with the reasoning in **Newhart** that the provisions in the debenture so empowering a receiver is an enabling provision which does not divest the directors of their duty of care towards the company or of their powers as the organ of the company to bring proceedings on its behalf. Both powers can co-exist as long as they are not so diametrically opposed as to come into conflict and the exercise of the director's powers does not impinge prejudicially on the position of the debenture holders by imperilling the assets which are the subject of the charge. In such a case no consent is required as the powers are individually distinct.

[19] In this case, the directors have taken the view that there is a right of action which could result in substantial damages accruing to the company from the debenture holders themselves. This right of action is a valuable asset to the Claimant Company. If the receiver chooses to ignore this right of action in favour of those who appointed him, or decides it's not worth the risk, there is no authority to suggest that the directors ought to ignore their independent duty to the company. They have a duty to aggressively pursue such action, if they legitimately feel it is in the best interest of the company and its shareholders. Debenture holders ought not to be allowed to hide behind the receiver when the action is against them for breach whether of contract or duty of care. See the case of **Viola v Anglo American Cold Stores** [1912] 2 CH 305. The receiver has the power to stop proceedings if he so wishes, if he feels his position is prejudiced or the assets are threatened. In such an event, the direction of the court may be sought. There has been no such application or evidence emanating from the receiver.

[20] In so far as there is any conflict with the case of **Newhart** and **Tudor Grange**. I only have this to say; **Tudor Grange** is at first instance. In **Tudor Grange** no indemnity was provided for any order for costs made in favour of the defendants against the plaintiff company. Sir Browne-Wilkinson V-C, at first instance, expressed doubt about the correctness of the **Newhart** decision, made at the Court of Appeal, on the basis that that court ignored the difficulties of two concurrent rights of action in two different sets of persons (why that appeared to be a difficulty to him was left unstated). There was also in **Tudor Grange** the question of a counter claim against the plaintiff company by the defendant company. The court was therefore preoccupied with the question of who would defend the counterclaim against the company whether it would be the receiver or the directors. But the court was bound to follow the decision where, as stated, "it exactly covers the point in issue". The learned judge decided the principle did not cover the point in **Tudor Grange** because when the plaintiff began proceedings in the name of the company, they began proceedings which would directly impinge on the property which was subject to the receiver's powers and there was no indemnity provided against an order for costs made against the company in the event of a loss of suit. This, the court felt prejudiced the receiver's position. However, he found that the possibility of an indemnity being forthcoming in favourable terms would save the case from being struck out on that ground.

[21] That position is different than this case because in the present case, the claim was begun long before the Claimant Company was placed in receivership. In the case of **Arawak Woodworking Establishment Ltd. v Jamaican Development Bank** [1987] 24 JLR 15 it was held that, provided they did not imperil the assets, the directors of any company in receivership not only had the power but also the duly to initiate proceedings on behalf of the company where such proceeding is in the company's interest or on behalf of creditors. This case was considered and approved in the consolidated appeals in **Pan Caribbean Financial Services Ltd v Robert Cartade et al and Jamaica Redevelopment Foundation Inc. v Robert Cartade et al** [2011] JMCA Civ. 2 which also affirmed the decision of Brooks J, at first instance, to allow a case to proceed by company in receivership without the consent of the receiver where the possibility to

provide an actual indemnity to the company against the costs of the action existed. The cases of **Newhart** and **Tudor Grange** were also referred to and applied without distinction.

[22] The receivers function is to gather in the assets of the Claimant in order to discharge his function to his appointees. This he has done as the assets of the Claimant are fully under his control. The debenture deed also gives him the power to bring proceeding if he so thinks it necessary, in the name of the company. In doing so he is protected from liability for costs in the event of a loss. He has chosen not to exercise those powers.

Are The Assets of the Company Imperilled?

[23] Counsel for the Defendants submitted that the company's assets are imperilled by the possibility of costs orders being made against it in the likelihood the suit is lost. The Claimant's counsel on the other hand, submitted that the Defendants were protected by the receivership and the debenture, as the physical asset of the company was in the hands of the receiver. Further, it was argued that the debenture provided a full indemnity for all legal fees and other costs for this litigation if the Defendants were successful. The question for this court is whether this is sufficient to answer the question of whether the company's assets are imperilled. Any costs order in favour of the Defendants would have to be paid by the Claimant Company. No doubt it is the receiver who will be called upon to pay it. The indemnity in the debenture, from my point of view, is for the benefit of the debenture holder should it have been forced to bring any claim in respect of the debenture.

[24] It is clear that a loss of the claim resulting in a cost order against the Claimant in favour of the Defendants would result in diminishing the assets if the costs are to be paid by the Claimant Company. The costs would have to be paid by the Claimant from its sole asset which is the subject of the charge. The claim was commenced before the company was placed in receivership and with the asset now under the control of the receiver there is no evidence of how this suit is being financed. The possibility of costs

orders against the Claimant must not only be considered in light of the 1st and 2nd Defendants, as debenture holders but all the Defendants if they succeed would be individually entitled to their costs. This really begs the question whether a diminution of the assets equates to imperil or threat. Certainly if costs are to be paid from the assets its value will be lessened. But in my view this does not mean it is under threat or peril if the value is substantially more than the likely costs and the extent of the debenture put together. The debenture holders are only concerned about the repayment of the debt and the availability of sufficient funds in the charge to recover the debt. There is no peril or threat if the assets are substantial to cover both.

[25] This then takes me to the next question as to whether an indemnity is necessary in light of the indemnity contained in the debenture. If the Claimant succeeds in damages the amount it recovers may be sufficient to cover its debts to the 1st and 2nd Defendants. In **Awarak** Morgan J, espoused the principles in **Newhart** as follows:

> *"The general principle as enunciated in **Newhart's** case is that the directors of the company have the power and here a duly to institute proceedings on behalf of a company provided they do not imperil the assets and provided also that the action is in the company's interest and the suit is for/and on behalf of the creditors. This can be done without the receivers consent and concurrence. What they cannot do is to file an action which by itself will threaten or imperil the assets which are subject to the charge. This principle, however, is alterable. There were special circumstances in this case to which his Lordship referred but which were not then material. They were –*
>
> *(a) That a director Dr. Hartley along with others had provided an indemnity for the plaintiff company;*
>
> *(b) The company was not financing the action out of its own resources;*
>
> *(c) The company would not have to meet any claim for cost;*
>
> *(d) The directors of the company at the time started the action were a duly constituted board; and*

(e) Nothing in the course of the proceedings threatened the interest of the debenture holders."

Is An Indemnity Necessary?

[26] In all the cases cited where the directors have been allowed to continue a claim on behalf of a company in receivership, an indemnity was thought necessary to secure the assets. I accept that implicit in such an approach is the recognition that the possibility exists of diminution in the assets if a "hostile" costs order is made against the company in receivership in favour of the winning Defendants.

[27] In this case counsel for the Claimant indicated that an indemnity already exists. The court is bound to examine firstly, if such an indemnity does so exist and whether it is sufficient to protect the assets of the company in receivership. The appointment of the receiver dated August 19, 2011, appointed him to exercise all powers of a receiver given by the debentures. It also declared that he was to be an agent of the company and the "company alone shall be responsible for his acts and default". The debenture issued by the company in favour of the 1st and 2nd Defendants on September 16, 2005 provides in paragraph 22 for the appointment of receiver; said receiver to be agent of the chargor. Paragraph 23 speaks to the powers of the receiver. The powers listed there do not exclude the powers exercisable by the organs of the company. This is unlike Rule 51 of the Civil Procedure Rules 2002, where the court appoints a receiver and the powers of the court appointed receiver is expressly made to be to the exclusion of the powers of the judgment debtor.

[28] The only indemnity I have found in the debenture deed is at paragraph 38 entitled "indemnity to bank and receiver". It states:

> *"The chargor hereby agrees to indemnify the Banks and the receiver against losses, actions, claims, expenses, demands and liabilities whether in contract, tort or otherwise now or hereafter incurred by* ***the banks*** *or the* ***receiver or by any manager, agent, officer or employee*** *for whose liability, act or omission the banks or the receiver may be answerable or for anything done or omitted to be done by the bank or the*

> *receiver or by any manager, agent, officer or employee of the banks or the receiver, in the execution or purported execution of any of the powers, trusts, authorities or discretions vested in it or him under this debenture under any of the securities or otherwise,* ***or occasioned by any breach by the chargor of any of its covenants or other obligations to the banks. The chargor shall so indemnify the banks and the receiver on demand*** *and shall pay interest on the sums demanded at the rate of interest applicable from time to time by the banks on unauthorized overdrafts." (**My emphasis**)*

[29] As can be clearly seen, whilst the clause in the debenture does provide an indemnity to the banks and the receiver and their agents, managers and employees, it's an indemnity for actions conducted under the debenture including the exercise of powers under the receivership occasioned by the chargor's breach of its covenants and obligations to the banks. This is an indemnity provided by the chargor, the Claimant Company, in favour of the banks and the receiver for the costs of any actions it has to take resulting from the chargor's breach. What is requested in this case, for the action to be allowed to continue, is an indemnity by the Claimant, to protect its own assets in receivership. So on the one hand, the indemnity in the debenture provided for the chargor to bear the cost of any loss or expenses occurred by the banks or receiver as a result of their breach of covenant or obligations. On the other hand, the indemnity requested in this case is for the directors of the Claimant Company, the said chargor, who are exercising their independent power to act on behalf of the company without the consent, agreement or joinder of the receiver, to indemnify the assets in receivership against diminution resulting from a cost order against it. In other words, the value of any litigation cost awarded by the court should not be paid from the assets of the Claimant's Company in receivership, to the extent that this would jeopardize the claim of the debenture holder and in the event the obligation to pay the costs of the other defendants cannot be met.

[30] The director, Mr. Delroy Howell also executed a deed of Guarantee and Indemnity in favour of the 1st and 2nd Defendants. I have also considered whether this provided sufficient protection over the charged assets being diminished to the detriment

of the debenture holder. If the Claimant Company loses this suit, it must pay cost as the losing party. It only has one asset. The receiver in whose hands the Claimant's asset lies will be obliged to pay the costs out of that asset. The guarantee, guarantees the debt to its value and interest thereon. So the 1st and 2nd Defendants can either, realize the asset and try to reclaim the sums due or try to collect from the guarantor. They have already sued the guarantor. If the asset is diminished then there will be less to realize to cover the debt. If the guarantor has no funds to cover the debt then the creditor also will not recover full value. In such a case the Guarantee and Indemnity would not protect the asset of the Claimant Company and therefore the debenture holders.

[31] However, he who avers must prove. The Defendants have not shown that the asset of the Claimant is imperiled by this claim to the extent that they, as debenture holders are in jeopardy. They have not shown that the assets are insubstantial or that the Guarantor is a bankrupt. They have not shown that the Claimant will be unable to meet its costs and those of the defendants if the suit is lost. This claim is distinguishable from the authorities cited in that the claim was brought before the receiver was appointed. He has not sought to discontinue it. The asset is in his hand and under his control. There is no evidence from him of impending peril. Furthermore, the 1st and 2nd Defendants also have the personal guarantee of Delroy Howell and the right of action against him for the full amount of the debt. It follows therefore, that the Claimant need not provide any indemnity in order to continue with this claim. The application is not based on any allegation or evidence or even assertion that the claim is ill conceived and doomed to fail and that costs in such a case would be substantially higher than the value of the asset. The debenture holder does not own the assets the subject of the charge. Their claim is only in respect of the value of the debt. There is no evidence of what the likely costs to the defendants would be or what level of indemnity is required.

[32] I am made bold in coming to this decision by the reasoning of the court in **Viola v Anglo-American Cold Storage Company.** Though the facts were somewhat different the reasoning is quite enlightened. In that case it was held that the fact that a debenture holder has a charge on all the assets of the company does not give him a

right to prevent the receiver being allowed to carry on proceedings commenced by the company against him, in another capacity, at the costs of the assets over which he has a charge. The court held that the assets of the company were not those of the debenture holders, they simply had a charge over the asset to the extent of the amount due to them. The court also found that the debenture holder had brought an ordinary debenture holder action for appointment of receiver for the simple purpose of preventing the company from bringing action against it for an impeached contract. The debenture holder did not deny this fact and simply claimed that the assets in receivership should not be applied by the company against it as the chargee. The court allowed the receiver, appointed by the court at the request of the debenture holder, to continue the action commenced by the company and allowed the costs to be paid from the assets in the hands of the receiver. Significantly the court found that the assets were more than sufficient to cover the costs without imperiling the rights of the debenture holder. The court also held that debenture holders were not in a position to dictate whether proceedings should continue neither did they have any right to say the assets of the company should not be employed to get in other valuable assets of the company. That decision is for the courts.

[33] In this case there is no evidence that the assets of the company are insufficient to pay off the debt or that the guarantee cannot be enforced. It is only the appointment of the receiver after the commencement of this action which prevents the company from using its own assets to carry on its action against the Defendants.

[34] The directors have a duty to act bona fide in the interest of the company and may not incur expenses and liabilities exceeding the company's assets. If the receiver is of the view that pursuing the action may put the Claimant Company in a position where it is placed in a "hostile" liability for costs or would have to finance the action to the prejudice of the debenture holders, the receiver has the power under the deed to take steps to prevent that catastrophe from occurring.

[35] On the 10th of July when I was to initially dispose of this matter my research into another matter took me to the Companies Act where I came upon section 388. Although no initial submission had been raised by either side on the applicability of section 388 of the Companies Act to this particular case, the section having come to my attention it seemed necessary and prudent to have the parties make submissions in this regard. I take this opportunity to thank both sides for the accommodating stance taken by them.

[36] Section 388 of the Companies Act states:

> *"Where a limited company is plaintiff in any action or other legal proceeding, any judge having jurisdiction in the matter may, if it appears by credible testimony that there is reason to believe that the company will be unable to pay the costs of the defendant if successful in his defence, require sufficient security to be given for these costs, and may stay all proceedings until security is given."*

There is no dispute that the Claimant is a limited liability company. Although what was applied for by the Defendants was an indemnity or guarantee against any possible costs in this claim to protect the debenture holder being prejudiced by the dissipation of the Claimant's assets, in my view the request is also tantamount to security for costs for any possible costs orders in favour of the defendants which the Claimant may be unable to meet and the considerations are identical. In my view this is a question of a "Rose by any other name." The Defendants application is really for security to be provided in the form of an indemnity or guarantee for costs from a third party. Under the section, the question of whether there should be an order for security of costs can only be answered by the consideration credible testimony or evidence that a plaintiff that is a limited liability company would be unable to pay the defendant's cost if they were the successful party in this suit.

[37] The provision vests in the judge presiding over the matter, the discretion, to be employed after and only after considering credible testimony, whether to make an order for sufficient security for costs to be given. Counsel for the Claimant took the view that the section had not been relied on by the Defendants in their application and therefore

ought not to form any part of the courts consideration. Bluntly put, the Claimant's respectfully submitted that the section was irrelevant to this application. In the alternative counsel, also took the view that even if the court felt it necessary to consider the section applicable, the Defendants had not provided any credible evidence that security for costs was necessary.

[38] Counsel for the Defendants reminded the court that what the Defendants sought in their application was an indemnity or undertaking issued by a reputable financial institution to pay the costs which the Claimant will incur in this claim and for all costs which the Claimant may be ordered to pay the Defendants. Counsel for the Defendants was of the view that based on what was sought in the application it was squarely within the bounds of section 388 and was properly to be considered by the court.

[39] It seems to me that this application raises two issues to be determined by two separate but equal principles. On the one hand, the 1st and 2nd Defendants as debenture holders having appointed a receiver, are entitled to claim that they would be prejudiced as debenture holders if the assets of the company are frittered away by the directors as a result of the costs of the claim and of costs orders against the Claimants in this suit brought by them. In that regard an application for indemnity or undertaking to pay the claimant's costs and any award of costs made against it is entirely appropriate and the principles applicable to that situation must and has been considered by the court. In the case of the 3rd to 6th Defendants, they are not debenture holders so they would not be prejudiced in that regard. Therefore any application on their behalf for indemnity or an undertaking by a reputable financial institution to pay the costs which the Claimant may be ordered to pay to them, is an application for security of costs. It is therefore, the principles applicable to that situation as provided under section 388 of the Companies Act which must be considered. So the 1st and 2nd Defendants are entitled to claim indemnity and security for cost both as debenture holders who may be prejudiced and defendants who may be successful in the claim brought against them and the 3rd to 6th Defendants are entitled to claim indemnity or security for cost as defendants who

may be successful in the claim brought against them. Therefore, I find section 388 is applicable to this application.

[40] In this application therefore, the court would not only have to consider whether the Claimant in continuing this claim is in fact imperilling its assets to the detriment of the debenture holder but also whether it would be able to satisfy any costs orders made against it in favour of all the defendants and its own costs.

[41] In their submissions counsel relied on the case of **C & H Property Development Company Limited v Capital and Credit Merchant Bank Limited** [2012] JMCC Comm. No. 6 to ground their submissions. This was a decision of Mangatal J (as she then was) sitting in the Commercial division. In that case the learned Judge had to decide whether to grant an order for security of costs under Section 388 of the Companies Act. Mangatal J took the view that the issue of the Claimant's insolvency or impecuniosity was an important consideration under Section 388 and unlike applications for security of costs under Part 24 of the Civil Procedure Rules 2002 (where issues such as whether the claimant has sufficient assets in the jurisdiction is considered), insolvency was expressly and directly the foundation for such applications. However, other factors were also to be considered in arriving at that decision; such as whether the claim would be stifled if security for costs were to be ordered. Mangatal J relied on the case of **Northampton Coal, Iron and Wagon Company v. Midland Wagon Co.** Vol. VIL L.R**.** 500. That case was decided on the basis of section 69 of the UK Companies Act 1862, which is similar to section 388. That case decided that a company being in liquidation was sufficient reason to believe the assets to be insufficient to pay its costs unless contrary evidence was given.

[42] Mangatal J adopted the approach taken in that case. However, in **Keary Developments Ltd. V. Tarmac Construction Ltd** [1995] 3 All ER 534 one of the authorities cited by counsel for the Defendants, Lord Justice Gibson noted that the court has a complete discretion whether to order security for costs and accordingly it will act in light of all the relevant circumstances. That case was decided on the basis of section

726 of the UK Companies Act of 1975 which is identical to section 388. The principles outlined in that case are in summary that;

a) the possibility or probability that the claimant company will be deterred from pursuing its claim by an order for security is not without more a sufficient reason for not ordering security as the legislature must have taken this into account;

b) the court is to carry out a balancing exercise weighing the relative injustice of granting or refusing the application;

c) The court must also balance (i) the possibility of the order being used oppressively (e.g. to stifle a genuine claim) against (ii) the insolvent company using its inability to pay costs as a weapon to put unfair pressure on the defendant;

d) In considering all the circumstances, the court will have regard to the claimant's company's prospects of success. But it should not go into the merits in detail unless it can clearly be demonstrated that there is a high degree of probability of success or failure.

e) Before the court refuses to order security on the ground that it would unfairly stifle a valid claim, the court must be satisfied that in all the circumstances, it is probable that the claim would be stifled.

f) the court must consider whether the Claimant company can raise the amount needed as security for costs from its directors, shareholders or other backers or interested persons and as this is likely to be peculiarly within the knowledge of the plaintiff company, it is for the plaintiff to satisfy the court that it would be prevented by an order for security from continuing litigation.

[43] Counsel for the defendants asked the court not to consider whether the Claimant would be deterred from pursuing its claim but rather to consider its impecuniosity which would raise a prima facie case that it cannot pay its debts. The court was reminded that each Defendant was individually entitled to their costs and as the Claimant's assets continue to be diminished by litigation costs, there was no guarantee that the assets will be sufficient to meet the indebtedness to the debenture holders, the costs of the receivership and any legal costs which may become due to the Defendants. Counsel also argued that based on **Keary Developments Ltd,** the burden rests with the Claimant to show that it will be unable to pursue litigation if an order was made. It was pointed out that no such evidence was given and that in any event, in keeping with the

principle in **Keary Developments Ltd**, the fact that its claim might be stifled should not be the main consideration

[44] Counsel further argued that credible testimony had been presented to the court which showed that there was reason to believe the company would be unable to pay its costs if the Defendants were successful in their defence. Once again counsel pointed the court to the affidavit evidence of Julianne Mais-Cox which showed that demands were made for payment on the loan accounts and such demands remain unmet. That evidence, it was pointed out, remains unchallenged as no affidavit evidence was filed by the Claimant in response to the application. There was therefore, no evidence from the Claimant to rebut the prima facie case raised by the fact of the receivership.

DISPOSITION

[45] In the round then the court holds that the directors of a company in receivership, as the governing organ of the company, still retain a residual power to bring action on behalf of the company in the interest of the company and its shareholders. This power exists alongside and in tandem with the independent power to do so which also resides in the receiver and no consent is required of a receiver to do so. However, if the receiver consents or joins with the organs of the company in bringing an action, then the claim by the directors will be deemed to be a claim by the receiver.

[46] Where the directors take action independently of the receiver without his consent or participation and there is evidence that the assets of the company would be imperilled to the detriment of the debenture holders, the directors of the company in receivership may be required to provide an indemnity against any diminution in the value of the assets under receivership, before such a claim will be allowed to proceed. The onus is on the applicant to show, by credible evidence, that, the assets of the company are insufficient to satisfy the debt and any costs orders which may be made against it and that the rights of the debenture holder would be in jeopardy if no indemnity was provided.

[47] The receiver has the power to take or continue an action at the expense of the assets of the Claimant Company and the debenture holder would not be in a position to prevent the receiver from continuing the said action against them at the costs of the assets. It therefore follows that they should not be able to prevent the Claimant's actions against them continuing unless they can show that the costs of the action would far exceed the value of the debenture. The only thing standing between them and the Claimant's case is the appointment of the receiver by them.

[48] Where, as in this case, the loan from the 1st and 2nd Defendants was fully guaranteed and the guarantee is enforceable, they, as debenture holders, will not be entitled to prevent the company from bringing a claim against them by depriving the company of the means of prosecuting the claim by the appointment of a receiver and the application to prevent the company from using its assets to pursue what it perceives to be a further valuable asset. If the receiver is of the view that the right of action is worthless or the company's assets are indeed in peril he has the power, under the debenture deed appointing him, to seek the courts direction to prevent the assets being dissipated to the detriment of the debenture holders.

[49] In the circumstances of the requirements under section 388 of the Companies Act, the affidavit of Julianne Mais-Cox does not provide sufficient credible evidence upon which this court may exercise its discretion in ordering the Claimants to provide security for any potentially hostile cost award. In the case where the receiver was appointed by the debenture holder under the deed, it does not raise a prima facie case that the Claimant was insolvent and unable to meet its debts. The onus does not shift in those circumstances to the Claimant to show that it can in fact pay its debts. No amount for the indemnity was even put forward by the Defendants for consideration by the court. It is true that demands for payment were made on the Claimant (and the guarantor of the loan) which were not met. However, the claimant is disputing the amount demanded and the basis for its calculation. In such a case, I hold the firm view that the appointment of the receiver in those circumstances would not prima facie mean the claimant was insolvent or unable to meet its debt. The asset held by the receiver is

of considerable value although the amount owed to the 1st and 2nd defendants is also a considerable amount. I also consider that the asset is not bare land but a hotel which was a going concern at the time it went into the hands of the receiver. There is no evidence from the Defendants that there are any other charges on the assets.

[50] I also have to take account of the fact that there is no evidence from the Claimant that it will be able to pay its debts and any costs order made against it. I believe it to be a true statement of the law that where the balance of justice tilts in favour of the Defendants the onus is on the Claimant to provide evidence that the grant of the order would prevent it from continuing with the litigation. However, it cannot be over emphasized that the asset is in the hands of the receiver appointed by the Defendants yet there is no evidence from the receiver that the company is unable to pay its debts and meet any costs order against it as they fall due. Who, other than the receiver at this time, is better able to so state.

[51] I agree with the authorities that the exercise of this kind of discretion is little more than a balancing act although I would add that it is in fact a delicate balancing act; balancing the injustice to the Claimant if its claim is stifled by a requirement to provide a guarantee or indemnity as a security for its own costs and any costs orders which may be made against it, against the injustice to the Defendants if the order is not made. The Defendants have not made any assertions in this application that the Claimant's case is bound to fail. The likely prospect of success or failure of the Claimant's case is too an important consideration.

[52] I find that there is no credible evidence apart from the bare assertion that the Claimant is unable to pay its debts and will not be able to meet its costs orders which would become a debt to the 3rd to 6th Defendants and an additional debt to the 1st and 2nd Defendants. Taking into consideration all the relevant factors I do not believe it is in the interest of justice to exercise my discretion in favour of the Defendants. The balance of justice weighs in favour of the Claimant and in the absence of credible evidence from

the Defendants it need not show that its claim will be prevented from continuing if the order applied for is granted.

ORDERS

[49] The court therefore orders that:

(1) The Notice of Application for Court Order is dismissed.

(2) The Costs of this application is to the Claimant against the Defendants to be taxed if not agreed.