

**Judgment 3/2009**

**Flightlease Holdings (Guernsey) Ltd v Flightlease  
(Ireland) Ltd – Royal Court (Civil Action File 812) –  
14 January 2009**

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**Companies (Guernsey) Law, 2008 – both parties are in voluntary liquidation – effect of Plaintiff's claims for indemnity in respect of liability under guarantees relating to the Defendant's liability to third party creditors – the rule in Cherry v Boulton ("the fund ascertainment principle") – review of statutory provisions for liquidation of companies in Guernsey – rule against double-proof – law of set-off in Guernsey and pre-Napoleonic France – law of set-off in Jersey and in Scotland - adoption by Guernsey Law of English equitable principles in appropriate cases – the fund ascertainment principle is to be applied in the circumstances of the present case – ordered that no dividend be paid in the liquidation of the Plaintiff in respect of the Defendant's agreed claim**

**IN THE ROYAL COURT OF THE ISLAND OF GUERNSEY**

Civil 812

The 14<sup>th</sup> day of January 2009, before Richard Charles Southwell Esquire, QC Lieutenant Bailiff, sitting alone

**IN THE MATTER OF SECTION 426  
OF THE  
COMPANIES (GUERNSEY) LAW, 2008**

**FLIGHTLEASE HOLDINGS (GUERNSEY) LIMITED  
("FL Holdings")**

**Plaintiff**

**and**

**FLIGHTLEASE (IRELAND) LIMITED  
("FL Ireland")**

**Respondent**

Whereas on 24<sup>th</sup> and 25<sup>th</sup> November 2008 the Lt Bailiff considered an application made under section 426 of the Companies (Guernsey) Law 2008 (the 2008 Law), and/or under the inherent jurisdiction of this Court, for an order that no dividends be paid in the liquidation of FL Holdings in respect of FL Ireland's Agreed Claim and heard thereon Advocates J M Wessels and I C Swan counsel for the Plaintiff and Respondent respectively the Lieutenant Bailiff this handed down judgment in the terms attached hereto and

1. DECLARED that Flightlease (Ireland) limited is not entitled to receive in the liquidation of Flightlease Holdings any dividends in respect of Flightlease (Ireland) Limited's Agreed Claim of US\$5,984,763.00.
2. ORDERED that each side bear its own costs.

S M D ROSS  
HM Deputy Greffier

**Approved Judgment  
14 January 2009**

**IN THE ROYAL COURT OF GUERNSEY  
(ORDINARY DIVISION)**

**IN THE MATTER OF SECTION 426 OF THE COMPANIES (GUERNSEY) LAW, 2008**

**Between:**

**FLIGHTLEASE HOLDINGS (GUERNSEY) LIMITED  
("FL Holdings")** **Plaintiff**

**and**

**FLIGHTLEASE (IRELAND) LIMITED  
("FL Ireland")** **Respondent**

**Before:**

**Lieutenant Bailiff Richard Southwell QC**

**Hearing date: 24<sup>th</sup> & 25<sup>th</sup> November 2008  
Judgment handed down: 14<sup>th</sup> January 2009**

**Advocate for the Plaintiff: J M Wessels  
Advocate for the Respondent: I C Swan**

**Introduction**

1. Flightlease Holdings (Guernsey) Limited (FL Holdings) is a wholly owned subsidiary of Flightlease AG, a company incorporated in Switzerland and in Nachlassliquidation ordered on 17 April 2003 in that jurisdiction. FL Holdings went into voluntary liquidation on 9 January 2004 in Guernsey, its place of incorporation, and its liquidators are Mr S J Akers and Mr N Wood.
2. Flightlease (Ireland) Limited (FL Ireland) is also a subsidiary of Flightlease AG. FL Ireland is an Irish incorporated company which went into voluntary liquidation in Ireland on 13 July 2004, and its liquidators are Mr Akers and Mr P McCann.
3. FL Holdings, FL Ireland and Flightlease AG have as their ultimate parent company, SAir Group AG, another Swiss company. The group of companies as a whole was known as "Swissair", that being the name of the airline which was part of the group. Both FL Holdings and FL Ireland (and a number of other companies, including several incorporated in Guernsey) were involved in the leasing of aircraft for use by Swissair.
4. FL Holdings and FL Ireland find themselves on opposite sides of the present matter in dispute, and so the interests of FL Ireland in this matter are being looked after by Mr McCann alone.

5. The liquidation of FL Holdings followed long negotiations with and between its creditors. Those negotiations resulted in an agreement dated 22 December 2003 (the FL Guernsey Agreement).
6. Similarly the liquidation of FL Ireland followed negotiations which resulted in an agreement also dated 22 December 2003 (the FL Ireland WDA).
7. These agreements have some similarities in their terms, and were linked by common conditions precedent which were satisfied. I shall have later in this judgment to consider in detail some of the provisions of the FL Guernsey Agreement for the purpose of deciding the matters now in issue.
8. In the course of previous business FL Holdings and FL Ireland incurred liabilities to each other, and in the FL Guernsey Agreement it was agreed that FL Ireland is a net creditor of FL Holdings in the "Agreed Claim" of US\$5,984,763.00, but subject to certain provisos to be considered later. This was but one of the Agreed Claims of most of the creditors of FL Holdings provided for in the FL Guernsey Agreement. The total Agreed Claims amount to US\$689,024,400.00 and so FL Ireland's claim is 0.86% of the total.
9. FL Holdings has large debts amounting to US\$214,304,373.00 arising from guarantees given by FL Holdings in respect of liabilities of FL Ireland to third party creditors (31% of the Agreed Claims against FL Holdings). These give rise in turn to potential claims by FL Holdings to be indemnified by FL Ireland in respect of FL Holdings' liabilities under the guarantees. FL Holdings cannot prove for these claims in the liquidation of FL Ireland because of the principle of law barring a proof by a guarantor, in addition to a proof by the creditor (the principle barring double proof), as is common ground between the parties. It will be necessary for me later to consider some relevant terms of these guarantees.
10. The purpose of this application by the liquidators of FL Holdings is to establish the effect (if any) of its claims for indemnity in respect of its liabilities under the guarantees, and in particular whether FL Holdings can rely on these claims as entitling the liquidators of FL Holdings not to pay any dividend in respect of FL Ireland's Agreed Claim of nearly US\$6million.
11. The position as regards dividends in the liquidation of FL Holdings is that two interim dividends totalling 16.5% have been paid to creditors on 17 February 2005 and 30 November 2006. This has resulted in the creditors guaranteed by FL Holdings receiving interim dividends totalling US\$34,919,530.73 (after adjustments). But these dividends have been withheld from FL Ireland pending determination of the issues raised by this application. The total amount of potential dividends for FL Ireland which has been withheld is US\$ 947,485.90. If FL Ireland succeed on this application, that sum (less a potential deduction of US\$10,424.00 unconnected with the present issues) would be paid with interest. It is unlikely that any further dividends will be paid for some time by the liquidators of FL Holdings.
12. The application is made under section 426 of the Companies (Guernsey) Law 2008 (the 2008 Law), and/or under the inherent jurisdiction of this Court, for an order that no dividends be paid in the liquidation of FL Holdings in respect of FL Ireland's Agreed Claim.
13. Notice of the application was ordered to be given to the liquidators of FL Ireland. As regards other creditors of FL Holdings, it appears from the affidavit of Mr Akers that all the creditors of FL Holdings would certainly be worse off if dividends were paid to FL Ireland except for three creditors, of which Credit Lyonnais, now Calyon, would probably be better off in any event, and Deutsche Bank and HSBC Bank might or might not be better off, through enhanced dividends in the liquidation of FL Ireland. Though notice has not been ordered to

be given formally to these three creditors, each has been informed about the application, and has been given the opportunity to make its own submissions to the Court. I understand that each is content that the case against the application of the liquidators of FL Holdings should be as put forward by Mr McCann as one of the liquidators of FL Ireland.

14. On the hearing of this application, the liquidators of FL Holdings have been represented by Advocate Jeremy Wessels, and Mr McCann as one of the liquidators of FL Ireland by Advocate Ian Swan. I am much indebted to both Advocates for the considerable help each has given to the Court in this far from simple matter.

### The Guarantees

15. The guarantees given by FL Holdings in respect of liabilities of FL Ireland are summarised in the following table:

1	2	3	4	5
msn	Original Creditor counterparty	Date	Creditor with Agreed Claim	Agreed Claim (US\$)
E3355	Jeremy Limited	21 July 1999	HSBC	4,536,473
E3360	Jeremy Limited	11 October 1999	HSBC	4,787,281
E3361	Jeremy Limited	22 October 1999	HSBC	4,720,671
				<b>14,044,425</b>
1132	Magnus Limited	22 December 1999	Crédit Lyonnais now Calyon	11,285,210
1162	SL Zermatt Limited	28 February 2000	Crédit Lyonnais now Calyon	19,680,497
1179	SL Zermatt Limited	14 March 2000	Crédit Lyonnais now Calyon	19,621,136
1244	SL Zermatt Limited	14 June 2000	Crédit Lyonnais now Calyon	19,355,727
1308	SL Zermatt Limited	5 October 2000	Crédit Lyonnais now Calyon	19,304,619
1322	SL Zermatt Limited	31 October 2000	Crédit Lyonnais now Calyon	19,096,068
				<b>108,323,257</b>
0353	CLJ Avenue Limited	20 October 2000	Deutsche Bank	16,081,606
0362	CLJ Avenue Limited	20 October 2000	Deutsche Bank	15,060,744
0367	Outremer Finance Limited	9 November 2000	Deutsche Bank	22,425,975
1259	SL Eiger Limited	29 September 2000	Deutsche Bank	38,368,364
				<b>91,936,691</b>
			<b>TOTAL</b>	<b>214,304,373</b>

Column 1 contains the relevant manufacturer's serial number of an aircraft, Column 2 the name of the creditor (the lessor of the aircraft to FL Ireland) to whom the guarantee was given by FL Holdings, and Column 4 the name of the bank which is the assignee of the relevant guaranteed claim under the financing arrangements. The FL Guernsey Agreement, to which the original creditors and banks are parties, makes it clear that the banks are the correct creditors, since by clause 8.2 all the relevant "Creditors" – both original creditors and banks - confirmed that they had no claims other than the "Agreed Claims" which include claims by the banks.

16. In the case of Jeremy Ltd and HSBC, the three guarantees are in the same form. Taking the first (dated 21 July 1999), Jeremy Ltd is called "the Owner", FL Ireland "the Lessee", and FL

Holdings “the Guarantor”. By clause 16 the guarantee is governed by English law and the Guarantor submits irrevocably and unconditionally to the non-exclusive jurisdiction of the English High Court. It is clause 7 (the disclaimer clause) which is of primary relevance and this provides:

**“Waiver of Guarantor’s Rights**

*The Guarantor shall, until such time (the “Discharge Time”) as all sums whatsoever payable by the Lessee under the Agreements have been finally paid in full, exercise only in accordance with the Owner’s instructions:*

- (a) *its rights of subrogation, contribution and indemnity;*
- (b) *its right to take the benefit of, share in or enforce any security or other guarantee or indemnity for the Lessee’s obligations held by the Owner;*  
*and*
- (c) *its right to prove or claim in the bankruptcy, liquidation, administration or other insolvency proceedings of the Lessee.*

*Any amount recovered prior to the Discharge Time as a result of the exercise of such rights shall be held on trust for the Owner and paid to the Owner on demand. The Guarantor warrants to the Owner that it has not taken any security from the Lessee in relation to this Guarantee and agrees not to do so until the Owner receives all sums payable by the Lessee under the Agreements. Any security taken by the Guarantor in breach of this provision and all moneys at any time received in respect thereof shall be held in trust for the Owner.”*

17. In the case of Magnus Ltd, SL Zermatt Ltd and Crédit Lyonnais/Calyon the guarantees are more elaborate, but the relevant clauses are to similar effect, except that by clause 8.2 the English courts are to have exclusive jurisdiction, subject to the Lessor’s right under clause 8.3 to bring proceedings elsewhere. The disclaimer clause (clause 2.10) provides:

**“2.10 Waiver of Guarantor’s Rights**

*Until all the Facility Guaranteed Liabilities have been paid, discharged or satisfied in full (and notwithstanding payment of a dividend in any liquidation or under any compromise or arrangement) the Guarantor agrees that, without the prior written consent of the Lessor, it will not:*

- 2.10.1 *exercise its rights of subrogation, reimbursement and indemnity against the Lessee or any other person liable;*
- 2.10.2 *at any time after a valid demand has been made hereunder and for so long as such demand remains outstanding, demand or accept repayment in whole or in part of any indebtedness now or hereafter due to the Guarantor from the Lessee or from any other person liable for the obligations of the Lessee or demand or accept any Collateral Instrument in respect of the same or dispose of the same;*
- 2.10.3 *take any step to enforce any right against the Lessee or any other person liable in respect of any Guaranteed Liabilities; or*
- 2.10.4 *claim any set-off, contribution or counterclaim against the Lessee or any other person liable or claim or prove in competition with the Lessor in the*

*liquidation of the Lessee or any other person liable or have the benefit of, or share in, any payment from or composition with, the Lessee or any other person liable or any other Collateral Instrument now or hereafter held by the Lessor for any Guaranteed Liabilities or for the obligations or liabilities of any other person liable but so that, if so directed by the Lessor, it will prove for the whole or any part of its claim in the liquidation of the Lessee or any other person liable on terms that the benefit of such proof and of all money received by it in respect thereof shall be held on trust for the Lessor and applied in or towards discharge of the Guaranteed Liabilities in such manner as the Lessor shall deem appropriate.”*

18. In the case of CLJ Avenue Ltd, Outremer Finance Ltd, SL Eiger Ltd and Deutsche Bank, the guarantees are in elaborate terms. Clauses 11.2 and 11.3 are similar to clauses 8.2 and 8.3 in the Crédit Lyonnais guarantees, and clause 2.9 – the disclaimer clause – provides:

“2.9 **Waiver of Guarantor’s Rights**

*Until all the Guaranteed Liabilities have been paid, discharged or satisfied in full (and notwithstanding payment of a dividend in any liquidation or under any compromise or arrangement) the Guarantor agrees that, without the prior written consent of the Head Lessor, it will not:*

- (a) *exercise any right of subrogation, reimbursement and indemnity against the Lessee which may arise as a consequence of the performance by the Guarantor of its obligations under this Guarantee;*
- (b) *take any step to enforce any right against the Lessee which may arise as a consequence of the performance by the Guarantor of its obligations under this Guarantee; or*
- (c) *claim any set-off, contribution or counterclaim against the Lessee or claim or prove in competition with the Head Lessor in the liquidation of the Lessee or have the benefit of, or share in, any payment from or composition with, the Lessee or any other Collateral Instrument now or hereafter held by the Head Lessor for any Guaranteed Liabilities.”*

19. Though these disclaimer clauses are in somewhat different terms, it seems to me that in the context of this application little will turn on those differences.

### **The FL Guernsey Agreement**

20. The FL Guernsey Agreement was made by deed on 22 December 2003 between (1) the secured creditors (which included most if not all of the bank creditors of FL Holdings); (2) the unsecured creditors (three companies in the Swissair group including FL Ireland), (3) the “JOL Parties” (CLJ Avenue Ltd, SL Zermatt Ltd, SL Eiger Ltd, and Crédit Lyonnais Leasing Japan Co Ltd); (4) Flightlease AG; and (5) the Liquidators.
21. In the Recitals it was stated, at (B), that the creditors parties to the agreement were believed to be the only persons with claims against FL Holdings and the other Guernsey companies (and one Bermuda company) – the Group companies, though at (D) a few other potential claimants were mentioned. These included a potentially substantial claimant (ILFC) which brought proceedings in Guernsey, but subsequently abandoned these proceedings.

22. The Definitions in clause 1.1.2 included the term “Creditors” as meaning the Secured and Unsecured Creditors, the JOL Parties, Flightlease AG and their assignees (and for clauses 7 and 8 only, also the Group companies with Agreed Claims).
23. “Agreed Claims” were defined as the claims of some of the Creditors set out in Schedule 7 as adjusted under clause 8 (subject to clause 8.7, the Agreed Claims being indebtedness of the relevant Group company and of the named Group company guarantor as set out in Schedule 7).
24. All the conditions precedent in clause 2 were satisfied.
25. By clause 4.1

*“The affairs, business and property of FL Holdings shall be administered by the FL Holdings Liquidators in accordance with Guernsey law and the provisions of this deed.”*

There was a similar provision in clause 5.1 relating to the Group companies except for FL Holdings and a Bermudan subsidiary.

26. Clause 8 dealt with the Agreed Claims. It is necessary to quote the following:

*“8.1 This clause applies to Agreed Claims by and against the Group companies including, for the avoidance of doubt, Agreed Claims against FL Holdings resulting from its liability (whether as surety or otherwise) for any indebtedness of FL Ireland. Whereas FL Ireland’s position generally as a debtor of the other Creditors is the subject of the FL Ireland WDA, FL Ireland is only bound generally by this deed in its capacity as one of the Unsecured Creditors and is bound as a debtor only in relation to the application of clause 8.7.”*

The “FL Ireland WDA” is the equivalent agreement with the creditors of FL Ireland: see paragraph 6 above.

*“8.2 Subject to the provisos to this sub-clause and the remaining sub-clauses of this clause 8, it is agreed that each Creditor’s Agreed Claims together with such other sums as may be payable under the terms of this deed, are a final quantification of the liabilities of the Group companies to it and that it has no other claims [1] Provided that nothing in this deed shall affect any rights of contribution or indemnity, resulting from payments made after the date of this deed, which any Group company and/or FL Ireland may have against another Group company and/or FL Ireland (whether arising out of the Agreed Claims or liabilities to third parties) if and in so far as such rights would not offend the rule against double proof and [2] Further Provided that, in the case of the Agreed Claim of FL Ireland against FL Holdings (but no other Agreed Claims), (i) the liability of FL Holdings and (ii) its admission as a provable debt in the liquidation of FL Holdings shall be subject to such rights of set-off (if any) as may be applicable under Guernsey law arising out of or in connection with the Agreed Claims against FL Holdings which result from FL Holdings’ liability (whether as surety or otherwise) for indebtedness where FL Ireland is the principal debtor (whether alone or as co-obligor) and whether in respect of rights of indemnity arising in respect thereof or any other rights of recourse of whatever description.” (The numbers [1] and [2] I have inserted)*

“8.7 *This sub-clause applies whenever either:*

8.7.1 *an Agreed Claim against FL Holdings results from its liability as a surety for the liability of another Group company or FL Ireland (as appears from the fourth column of Schedule 7); or*

8.7.2 *an Agreed Claim against any Group company results from a liability where either another Group company of FL Ireland is a co-obligor or has a matching liability arising out of the same transactions (which includes, without limitation, liabilities arising out of or in connection with headleases and the sub-leases granted out of such headleases) (as appears from the third column of Schedule 7).*

*For the purposes of this sub-clause “Debtor A” means the payer and “Debtor B” means any Group company against whom an Agreed Claim lies arising out of the same underlying liability. Any payments received by a Creditor from Debtor A shall as between the Creditor and Debtor B be treated as if the same were being held on a suspense account whether or not that is actually the case and shall not reduce the ranking for dividend of the Agreed Claim against Debtor B unless and until the Creditor has been paid in full. No Creditor shall be entitled to receive from Debtor A and Debtor B payments which exceed in aggregate 100% of the amount for which they are both liable. If and in so far as the aggregate dividends would exceed 100% of the Agreed Claim, then the Creditor shall receive an undiminished dividend from the principal debtor and a dividend from the surety shall only be paid in so far as necessary to fund the balance of the Agreed Claim if clause 8.7.1 applies, and all liabilities falling within clause 8.7.2 shall be borne equally by the debtors concerned. In applying the provisions of this clause 8.7 to FL Ireland payment received pursuant to the provisions of the FL Ireland WDA shall be brought into account whether or not received by way of dividends on Agreed Claims as such.”*

27. Clause 11 provides:

“11 **Choice of law and submission to jurisdiction**

11.1 *This deed shall be governed by and interpreted in accordance with English law.*

11.2 *Subject to clauses 11.3 and 11.4 and the express provisions of this deed, each Party submits to the non-exclusive jurisdiction of the High Court of Justice in England and the Parties agree that the High Court of Justice in England is the most appropriate and convenient court to settle any dispute arising out of or in connection with this deed.*

11.3 *Any question of law other than English law may be referred to the courts of the relevant jurisdiction.*

11.4 *In so far as clause 11.3 applies, each Party submits to the non-exclusive jurisdiction of the courts of the relevant jurisdiction and agrees that they are the most appropriate and convenient courts to settle such questions of law.”*

28. Schedule 1 contained a list of the Group companies, including FL Holdings and Flightlease International Ltd (which was a Bermudan company, and the only one of the Group companies to be a non-Guernsey company); and Schedule 2 was a Structure Chart of these Group

companies. The Creditors were listed in Schedule 3, in Part 1 the Secured Creditors, and in Part 2 the Unsecured Creditors (of which there were only three, including FL Ireland). The JOL Parties were listed in Schedule 4. Material Assets of the companies including unencumbered aircraft were set out in Schedule 5. In Schedule 6 there were lists of Encumbered Aircraft and Sub-Leases.

29. The Agreed Claims were listed in Schedule 7. Of the Agreed Claims, thirteen were claims against both FL Ireland as principal debtor and FL Holdings as guarantor. The Agreed Claim by FL Ireland against FL Holdings for US\$5,984,763 was included.
30. Schedule 10 contained proposed directions of the Royal Court, which were made on 9 January 2004. The second direction required all the relevant companies' liquidators to accept in full the Agreed Claims (subject to adjustments as provided for in the FL Guernsey Agreement). Provision for such adjustment was made in clause 8 and Schedule 11.

### **FL Ireland WDA**

31. The provisions of this agreement so far as relevant are in many respects similar to those of the FL Guernsey Agreement. Recital (D) referring to the Agreed Claims against FL Ireland includes these words:

*“Finally, there are contribution and indemnity obligations to FL Holdings and certain of its subsidiaries which are expected to be excluded from proving in the liquidation of FL Ireland by the rule against double proof.”*

Clause 9 relates to the Agreed Claims against FL Ireland, and sub-clause 9.5 provides:

*“9.5 This sub-clause applies whenever an Agreed Claim against FL Ireland results from a liability where either FL Holdings or one of its subsidiaries (the “Other Debtor”) is either a surety for FL Ireland or is a co-obligor or has a matching liability arising out of the same transactions (which includes, without limitation, liabilities arising out of or in connection with headleases and the sub-leases granted out of such headleases). Any payments received by a Creditor from the Other Debtor shall as between the Creditor and FL Ireland be treated as if the same were being held on a suspense account whether or not that is actually the case and shall not reduce the computation of the Agreed Claim against FL Ireland unless and until the Creditor has been paid in full. No Creditor shall be entitled to receive from the Other Debtor and FL Ireland payments which exceed in aggregate 100% of the amount for which they are both liable. If and in so far as the aggregate dividends would exceed 100% of the Agreed Claim:*

*9.5.1 if FL Ireland is the principal debtor, the Creditor shall receive an undiminished dividend from FL Ireland and the dividend from the surety shall only be paid in so far as necessary to fund the balance of the Agreed Claim; and*

*9.5.2 where FL Ireland is a co-obligor or there is a matching liability, the liabilities shall be borne equally by the debtors concerned.”*

By clause 12, the FL Ireland WDA is governed by English law, the parties submit to the non-exclusive jurisdiction of the English High Court, but any issue governed by Irish law may be referred to the Irish Courts.

32. In an affidavit sworn by Mr Hamish Anderson, a partner in the London solicitors Norton Rose LLP acting for the FL Holdings Liquidators, Mr Anderson sets out the history of the drafting of clause 8.2 of the FL Guernsey Agreement, and in particular the further proviso which I have numbered [2]:see para.26 above.

### The Issues

33. As indicated in paragraph 12 above, the application to this Court by the Liquidators of FL Holdings is for an order that no dividends be paid in the liquidation of FL Holdings in respect of FL Ireland's Agreed Claim of US\$5,984,763.
34. The issues relating to this application revolve round a principle of English law often referred to as the rule (or principle) in *Cherry v Boulton* (1839) 4 My & Cr 442 Cottenham LC, and in particular whether Guernsey law relating to the insolvency and winding up of companies is to be developed by the adoption of this principle. The principle can perhaps best be described as the "fund ascertainment principle" ("the Principle"). A simple example may help at this stage. Suppose there is a fund with £4,000 in its bank account to which four persons (A, B, C and D) are entitled. Suppose also that D owes the fund £500. The Principle requires the debt owed by D to be brought into account, so that the total of the fund is treated as being £4,500, not £4,000. The entitlement of each of the four is therefore £1,125. So out of the sum of £4,000 A, B and C each receive £1,125, and D receives £1,125 minus £500 i.e. £625.
35. In English law this principle of equity (based on the more fundamental principle that he who seeks equity must do equity) was described by Sargant J in *Re Peruvian Railway Construction Co Ltd* [1915] 2 Ch 144 at p.150 (affirmed by the Court of Appeal: [1915] 2 Ch 442) as

*"where a person entitled to participate in a fund is also bound to make a contribution in aid of that fund, he cannot be allowed so to participate unless and until he has fulfilled his duty to contribute."*

This Principle has been applied in England and Wales in (inter alia) the distribution of deceased persons' estates, in trust law, in bankruptcy and in the liquidation of companies.

36. The issues for the Court's determination as stated by Mr Wessels are these:
- (1) Is Guernsey law the applicable law? (It is in fact common ground that Guernsey law, as the law relating to the liquidation of FL Holdings, is the law to be applied.)
  - (2) What is the rule in *Cherry v Boulton*, which I call the fund ascertainment principle?
  - (3) Is that Principle consonant with the principles of Guernsey law so as to permit its application in a case such as this in which Guernsey law applies?
  - (4) If so, is FL Ireland under an obligation to FL Holdings such that the Principle can be applied by the FL Holdings liquidators?
  - (5) Or is the application of this Principle precluded by the terms of the FL Guernsey Agreement and/or the guarantees?

## Liquidations of Companies in Guernsey

37. Before coming to deal with these specific issues, it is necessary to deal with the generalities of the liquidation of companies in Guernsey. Liquidation is principally a statutory creation. The first Guernsey statute in the 1880s was based on the first English company law statute, the Companies Act 1862. There has been a number of subsequent Guernsey statutes down to the Companies (Guernsey) Law 1994 which in turn was replaced by the 2008 Law. It is the 2008 Law to which (it is common ground) this Court is to refer. Provision is made in the 2008 Law for winding up in sections 391 to 426. Sections 391 to 405 deal with voluntary winding up, sections 406 to 418 with compulsory winding up, and sections 419 to 426 contain provisions of general application in winding up. The only section dealing directly with the distribution of the property of a company in liquidation is section 419, which provides:

- “419 (1) Subject to the provisions of –
- (a) this Law and any rule of law as to preferential payments,
  - (b) any agreement between the company and any creditor thereof as to the subordination of the debts due to that creditor to the debts due to the company’s other creditors, and
  - (c) any agreement between the company and any creditor thereof as to set-off,

*the company’s assets in a winding up shall be realised and shall be applied in satisfaction of the company’s debts and liabilities pari passu.*

- (2) *Any surplus shall thereafter be distributed (unless the memorandum or articles provide otherwise) among the members according to their respective rights and interests in the company.*

Section 419 recognises that a creditor may agree to subordinate its debt, and that the company may make an agreement with a creditor in relation to set-off. In other respects any principles as to the distribution of a Guernsey company’s assets have to be decided in accordance with Guernsey law as developed by the Courts.

38. On one rule relating to bankruptcies and liquidations the Advocates were agreed that it forms part of Guernsey law. This is the rule against double proof. If a creditor proves for its debt in the liquidation of the principal debtor, the guarantor of that debt is not permitted to prove also in that liquidation in respect of the right to be indemnified by the principal debtor. This applies even if the guarantor has paid part of the debt to the creditor. The guarantor can prove in the principal debtor’s liquidation only if the guarantor has paid the whole of the debt to the creditor, so that the creditor cannot prove in the principal debtor’s liquidation (or if the creditor and the guarantor have agreed that the guarantor, and not the creditor, is to prove). The rule against double proof also bars the guarantor from using the right of indemnity by way of set-off in respect of a cross-claim by the principal debtor against the guarantor. Thus it was common ground in this matter that FL Holdings (despite having paid, by reason of the guarantees, dividends amounting to nearly US\$35 million to FL Ireland’s creditors who have proved for the guaranteed sums in FL Holdings’ liquidation) cannot prove in FL Ireland’s liquidation for the dividends so far paid, nor can FL Holdings claim to set those dividends off in extinguishment of FL Ireland’s Agreed Claim of nearly US\$6 million. It will be for consideration on some other occasion whether the application of such a blanket bar on double

proof, including set-off, is consistent with a just distribution of the assets of a company in liquidation.

39. Neither of the Advocates spelled out the precise basis on which this agreed view of Guernsey law was founded. But it appeared that Mr Wessels accepted the rule against double proof as having become part of Guernsey law by analogy with English law (on which the Guernsey statutory provisions as to liquidation are based), whereas Mr Swan submitted that recognition of this rule as part of Guernsey law should be based on assimilation from the law of Scotland. Because Mr Swan's prime submission is that any development of Guernsey law in this field should be by analogy with the law of Scotland, it will be necessary for me to consider at some length the evidence of the two Scots lawyers adduced by the parties.

### **The Law of Set-Off in Guernsey**

40. Only one Guernsey case has been cited (by Mr Swan) dealing with set-off. This is *Beachcomber Hotels Ltd v Beaucette Yacht Marina* (21 April 1989, unreported) Frossard Bailiff. It is clear that set-off, or rather "compensation", has been recognised as part of Norman law since early times. It is referred to relatively briefly in Terrien's Commentaires (in a passage dealing with assignment: Book VII, Chapter VI, page 234), in Bérault's Commentaires (at pages 99, 308 and 312), in Basnage's Commentaires, 3<sup>rd</sup> ed (at pages 80-82), in Pesnelle's commentary, 2<sup>nd</sup> ed (at pages 32-33), and in Houard's Dictionnaire Analytique, 1<sup>st</sup> ed (at pages 314-315). Pothier in his Treatise on Obligations (Martin translation), pages 92-115, dealt with compensation in pre-Napoleonic France in some detail, as did Domat (Book IV, Titre II, pages 908-914).
41. Pothier's description of compensation was as the extinction of debts of which two persons are reciprocally the debtors, one to the other, by the credits of which they are reciprocally creditors, one to the other (at page 92). He said (at page 93):

*"The equity of a set-off is evident. It is established upon the common interest of the parties between whom the set-off is made. It is evident that they have each an interest to make the set-off, rather than to be obliged to draw from the pocket to pay what they owe and bring suit for the payment of what is due to them."*

42. According to Pothier (and indeed the older writers on Norman customary law) the main features of compensation were:
- (1) It took effect only between parties who were creditor and debtor in the same right. Thus a guarantor could set off, against what was claimed from him by the creditor, any sums due from the creditor to the principal debtor. But the principal debtor could not claim set off for sums owed by the creditor to the guarantor. The guarantor's position was that, as he could not be asked to pay more than the debtor, he could avail himself of any defences against the creditor available to the debtor.
  - (2) The debts had to be of the same kind: if one was of money, then both had to be only of money.
  - (3) Both debts had to be "certaines" and "liquides" so that a genuinely disputed claim could not be set off against an undisputed claim, and an unliquidated sum could not be relied on as a set-off. A disputed claim was not "certaines" or "liquides" unless it could readily be proved.
  - (4) Since set-off was based on a reciprocal payment of debts by each party to the other, both debts had to be presently due and payable.

- (5) Compensation took place “ipso facto” and “de plein droit”, in theory without being pronounced by a judge or even having been advanced by either of the parties. In reality, no doubt, compensation had to be advanced as a defence by one party to a claim of the other party. But this factor in the customary law of compensation meant that, from the date when the right of compensation arose, interest could be claimed only on the balance (if any) after set-off.
43. All these writers on Norman and pre-Napoleonic law were dealing with compensation as part of the general law, and as “cash flow issues”, as Mr Wessels described them, and they did not deal with the position or effect of compensation in the context of bankruptcy (or of the insolvency of companies, which were a much later invention).
44. The characteristics of compensation in the Norman law sources which I have described were similarly described in a decision of the Privy Council on appeal from the Royal Court of Jersey: *Dyson & anor v Godfray* (1884) 9 App Cas 726, in which the Privy Council adopted Pothier’s description of a “dette liquide” – a liquid demand.
45. The only statutory development of the Guernsey law of set-off is to be found in section 1 of the *Law of Property (Miscellaneous Provisions) (Guernsey) Law 1979* (the 1979 Law). The background to the inclusion of section 1 in the 1979 Law lay in uncertainty amongst banks in Guernsey as to the effect and enforceability of contracts either between banks and customers, or between banks, allowing for the setting-off of different account balances and contingent and other liabilities: see the helpful article by Advocate P R Collas in (1985) 2 GLJ 29-37. Advocate Collas concluded (as did the Privy Council in *Dyson* for Jersey law) that the customary law as stated particularly by Pothier was part of the law of Guernsey.
46. Section 1 provides as follows:
- 1(1) It is hereby declared for the removal of doubt that where there is for the time being in force an agreement (whether written or oral and whether express or implied) whereby, in respect of mutual dealings between them, any debt from one party is to be set off against any debt from the other party, the effect of that agreement is, unless the parties have expressly or by implication agreed to a different effect, that the only action which may be taken at any time in relation to what would otherwise be those mutual debts (whether by or at the instance of either party or any third party, and whether by way of enforcement, assignment, arrest, restraint or otherwise) is in respect of the balance (if any) then due after that set off; but*
- (a) in a case where the affairs of one party have been declared in a state of “désastre” at a meeting of his arresting creditors held before a Jurat as Commissioner of the Royal Court, this is subject to subsection (2) of this section; and*
- (b) in ascertaining the balance due as described in this subsection (but only for the purposes of this subsection), if a contingent liability is to be taken into account the contingency is to be treated as having occurred, and if a future liability is to be taken into account it is to be treated as if presently payable.*
- (2) [This gives the Jurat the power to declare an agreement as mentioned in subsection (1) to be fraudulent and void as against the other creditors of the debtor.]*

- (3) *Where, in winding up a body corporate which is insolvent, the liquidator is satisfied that:*
- (a) *any such agreement as aforesaid was entered into by the body corporate less than six months before the commencement of the winding up; and*
  - (b) *the agreement was entered into with a view of giving to the other party a preference over the other creditors of the body corporate;*
- he shall treat the agreement as being fraudulent and void as against the other creditors of the body corporate.*
- (4) *Any person aggrieved by a decision of a liquidator under the last foregoing subsection in a voluntary winding-up of a body corporate may appeal therefrom to the Court, and the Court may thereupon confirm, reverse or modify that decision and make such order in relation to the matter of the appeal as it thinks just.*
- (5) *In this section “debt” includes all debts and liabilities, present or future, certain or contingent, but does not include demands in the nature of unliquidated damages arising otherwise than by reason of contract or breach of trust.”*

47. Though section 1 of the 1979 Law deals only with contractual set-off, some of its provisions show that the principles of English law relating to bankruptcy and liquidation were in the minds of the draftsmen, for example:

- (1) the recognition that future and contingent liabilities are to be taken into account (see sub-sections (1)(b) and (5));
- (2) the use of the phrase “in respect of mutual dealings between them” in sub-section (1) which is an echo of the statutory provisions in the English law of bankruptcy and liquidation.

However, the freedom of contract (subject to voidability as a fraudulent preference) given by section 419(1) of the 2008 Law and section 1 of the 1979 Law shows an approach different from the mandatory provisions of the English statutes.

48. Subject to these Guernsey statutory provisions of limited scope it is for the Courts of Guernsey to fill the interstices which remain to be filled even after the 2008 Law.

### **Jersey Set-Off in Insolvency**

49. I have already referred to the Privy Council’s recognition of the customary law of compensation in *Dyson*. Since it was cited by the Advocates I ought to mention the decision of the Royal Court of Jersey in *Guidon Investments Ltd v Malet de Carteret* [1980] JJ 109. In that case *Guidon Investments Ltd* was in *désastre*. The defendant as guarantor had paid off debts owing by the company to a London firm of stockbrokers, Joseph Sebag & Co, and he sought to set-off his complete settling of the company’s debts to the stockbrokers against debts which he owed to the company. The Royal Court held that the defendant was not entitled to such a set-off. Despite referring to the English Bankruptcy Act 1914 and its provisions in respect of mutual dealings, and English cases such as *In re Fenton (no.1)* [1931] 1 Ch 85, the Royal Court declined to follow English law, in holding that no such set-off was possible in Jersey law, and that the defendant was entitled to no more than a dividend. I have

not been able to achieve certainty as to the grounds on which the Jersey Royal Court reached this decision, since the reasoning of the Court is far from clear (and in any event is entirely inconsistent with the position in English law).

50. Jersey statute law – Article 34 of the Bankruptcy (Désastre) (Jersey) Law 1990 – now provides for full set-off of all mutual dealings, being modelled on section 31 of the English Bankruptcy Act 1914; and Article 34 has been applied to company insolvencies pursuant to Article 166(1) of the Companies (Jersey) Law 1991. Contractual set-off has also been dealt with by the Bankruptcy (Netting, Contractual Subordination and Non-Petition Provisions) (Jersey) Law 2005, which allows freedom of contract in this respect.
51. Except for the freedom of contract just mentioned, it is clear that policy in Jersey has been generally to follow the guidance of English law, both statutory and judge-made, in this field. That is not at all surprising. English law offers a more sophisticated body of law developed in the light of the demands of a sophisticated modern economy. International financial services are a speciality of Jersey, as of Guernsey. So there is much sense when developing Jersey law in this field to look for guidance to the English law developments. Whether this should be the way in which Guernsey law develops is an issue to which I will come later in this judgment.

### **Set-Off in the Law of Scotland**

52. The ultimate derivation of compensation (or set-off) in Scotland from Roman law developments is similar to that of Guernsey (and Jersey) in the coutumes of Normandy, which themselves owe much to the centuries of Roman law as subsequently transmitted during the mediaeval period by the kingdoms which succeeded to the Roman Empire. I emphasise that there was a long period of transmission and change in Roman law principles, throughout about 1,000 years of Roman dominance, and thereafter through centuries of rule by non-Roman kings. It is unwise to place too much reliance on supposedly immutable doctrines of Roman law, which in truth were changing throughout the period of Roman dominance (as, for example, study of Justinian's Digest shows) and even more after Roman dominance was replaced by the successor kingdoms of Western Europe. This was part of the concern expressed by Lord Wilberforce for the Privy Council in the Guernsey appeal of *Vaudin v Hamon* [1974] AC 569 at pages 581 et seq.
53. I have had the advantage of two affidavits adduced by FL Holdings as to the law of Scotland of David Bennett, a solicitor and Writer to the Signet, who holds, amongst other qualifications, a Visiting Professorship of Company Law in the University of Edinburgh, and an affidavit adduced by FL Ireland of Alastair Macdonald Clark QC, an advocate who has been a Senior Lecturer in Law in the University of Strathclyde. Both are authors of or contributors to a number of legal academic works. At this stage I intend merely to try to set out the matters relating to the law of set-off in Scotland on which they are agreed. These are contained in paragraphs 9-17 of Professor Bennett's first affidavit, which for convenience I quote:

#### ***“Compensation and retention in Scots law***

9. *The right of retention (retainer) arises out of a particular contractual relationship, where the purchaser/debtor claims the right to withhold all or part of the price on the ground of non-performance by the seller/creditor. In this context the creditor's claim is liquid and that of the debtor is illiquid (a contingent claim of damages for non-performance). Retention does not extinguish either party's obligations, which remain until extinguished by payment or performance.*

10. *Compensation does not depend on a particular contractual relationship but arises where the parties have one or more non-contractual claims against each other. If the necessary conditions are satisfied the lesser claim is extinguished and the higher claim is reduced to the net amount. Compensation does not arise automatically but must be pleaded in defence of a claim. It can be excluded by agreement.*
11. *As between solvent parties, compensation requires that both claims be liquid. If, however, either party is insolvent an illiquid claim may be compensated against a liquid claim (or two illiquid claims against each other). The mandatory “set-off” required in English corporate insolvencies by r4.90 Insolvency Rules 1986 does not apply in Scotland; there is no equivalent in the Insolvency (Scotland) Rules 1986.*
12. *In certain circumstances the effect of retention and compensation may be identical, and this has sometimes resulted in both terms being employed to describe the same situation.*

### ***The development of Scots law***

13. *Scots law is often described as a “mixed system” in that it derives from both common law and customary rules and Civil (Roman) Law. Those rules were “received” by Scots law in a modified form during the early period after the establishment of the separate Scottish Kingdom in the 14<sup>th</sup> Century. Historically this arose from the practice, in the formative period of the 16<sup>th</sup> and 17<sup>th</sup> Centuries, of Scottish lawyers studying the subject in Continental Europe, particularly France and Holland where the system taught was civil law. Relations with England were often hostile in this period and English common law therefore had little influence.*
14. *Until late in the 17<sup>th</sup> Century there was no attempt to articulate the principles of Scots law as it was then understood and applied. This problem was addressed by a number of jurists (now known as ‘Institutional Writers’ to signify their importance) starting with Stair, whose Institutions of the Law of Scotland was published in 1681, and followed by inter alia [sic : alios] George Joseph Bell whose works were first published in the early 19<sup>th</sup> Century. These writers are still regarded as important sources of Scots law and they are regularly quoted in the courts where their exposition of the law remains valid.*

### ***Development of the concept of compensation***

15. *Initially Scots law followed the strict civil law rule which permitted compensation only where both debts were liquid. This was given statutory effect by the Compensation Act 1592 of the Scottish Parliament. However, it was realised that the result of a strict application of this rule gave rise to inequitable results if one of the parties was insolvent. Unlike Acts of the UK Parliament, Acts of the pre-1707 Scottish Parliament are given a liberal interpretation and are regarded as having been repealed or modified if shown to be in desuetude or contrary to current practice. This allowed the law to qualify the impact of the 1592 Act so as to permit compensation to operate in respect of debts arising prior to insolvency whether liquid or illiquid.*

16. *This development can be seen in the contrast between the account of compensation given by Stair (Institutions, Book 1 Title 18.6) where he quotes both the Digest and Code of Justinian on the point “which is constantly followed by our custom” that both debts must be liquid, and the views of George Joseph Bell which are quoted by Lord President [sic] Hope in Secretary of State for Trade and Industry v Frid [2004] 2 AC 506 at paragraph 33. Bell expounds the doctrine that compensation only operates where both debts are liquid but goes on to say that:*

*“This, however, does not hold as to the balancing of accounts in bankruptcy. If one party have failed, and a demand be made on the other, he will not be obliged to pay the liquid debt, and come in as creditor only for a dividend. The immediate necessity for payment of the liquid debt is taken away by the bankruptcy; and there is no impediment to the equity which holds the one debt an extinction of the other.”*

17. *It is, of course, necessary for the operation of compensation that the parties are indebted to each other in the same capacity (see para 38 of Lord Hope’s Opinion in Frid).”*

Mr Clark agrees with this passage in paragraph 8 of his affidavit.

54. It is helpful also, I believe, to quote here more of two parts of Lord Hope’s opinion in *Frid* at paragraphs 31-33 and part of 38:

*“31...Rule 4.90 of the Insolvency Rules 1986, which reproduces the provisions regarding mutual credit and set-off in bankruptcy that are set out in section 323 of the 1986 Act (which do not extend to Scotland), has no counterpart in the Insolvency (Scotland) Rules 1986 (SI 1986/1915). In Scotland the question of set-off (or compensation, as it is usually referred to in Scots law) is regulated, both in personal bankruptcy and in the winding up of a company, by the common law.*

32. *In Scotland it is well established that, while in compensation both debts must be due at the same time, this rule is applied only when both parties are solvent: Goudy, The Law of Bankruptcy in Scotland, 4<sup>th</sup> ed (1914), p 550-553. As Goudy puts it, at p 551, the term compensation as applied in insolvency has generally to be understood in a sense very closely akin to that of retention. It is based on a principle of equity which is designed to prevent the hardship of a debtor who is also a creditor being forced to pay in full, while he only receives a dividend for his debt. So every kind of claim may be set off in a case of insolvency, the only general restriction being that the debt sought to be set off against the bankrupt estate must be one that is capable of being ranked for.*

33. *Bell, Commentaries on the Law of Scotland, 7<sup>th</sup> ed (1870), vol 2, p 122 sets out the qualification that applies in the case of insolvency in this way:*

*“2. In compensation the debts must both be due at the same time. One who is due money presently payable, cannot defend himself against the demand by setting off money due to him six months after, or the payment of which depends on a condition. But this is a rule which holds strictly only while the parties are solvent. If one of them becomes bankrupt, the other may defend himself*

*against a present demand, by setting off a debt that is future or contingent, although the term be after the bankruptcy. He cannot so plead, however, on a debt arising after bankruptcy.*

3. *In compensation the debts must both be liquid, or capable of immediate liquidation. A debt is deemed liquid when it is actually due and the amount ascertained, 'Cum certum an et quantum debeatur.' But if the debt itself be contested, and the creditor has not his proof ready; or if the amount is disputed, and it depend on a long discussion what is to be adjudged due; the debtor will not be allowed to avoid the payment of what is liquid and due till that litigation be terminated. This, however, does not hold as to the balancing of accounts on bankruptcy. If one party have failed, and a demand be made on the other, he will not be obliged to pay the liquid debt, and come in as a creditor only for the dividend. The immediate necessity for payment of the liquid debt is taken away by the bankruptcy; and there is no impediment to the equity which holds the one debt an extinction of the other.'"*

"38 *It is a general rule of the doctrine that allows for one debt to be set off against another that each of the two parties be both creditor and debtor in his own right. This is as true under the law of Scotland as it is under the English common law. As Bell, Commentaries on the Law of Scotland, vol 2, p 124 puts it:*

*"Compensation can be pleaded only when the demands are mutual; and this whether the plea be strictly compensation, or the more extended remedy of the balancing of claims in bankruptcy. To constitute this mutuality of debt and credit, the sums reciprocally due must be owing to the parties in their own right respectively."*

....."

55. The English law rule against double proof (e.g. by creditor and guarantor in the insolvency of the principal debtor) is mirrored by the rule in Scots law against "double ranking".
56. Thus it can be seen that the law of Scotland has many features in relation to set-off and insolvency which it shares with either English law or Guernsey law. One feature in this field which seems not to be shared with either English or Guernsey law is the doctrine of retention: see paragraphs 9 and 12 of Mr Bennett's affidavit (above) and paragraph 32 of Lord Hope's opinion in *Frid*.

### **Relevance of Scots Law**

57. The primary relevance of the law of Scotland to the issues in this matter will arise in this way:
- (1) Mr Swan submits that the law of Scotland is derived from a similar civil law background to Guernsey law, and is therefore the appropriate law to look to by analogy when developing the law of Guernsey
  - (2) Mr Wessels, while accepting that the laws of Scotland and Guernsey have some commonality of background in the civil law, submits that in this field

Guernsey has already drawn on English law by analogy, and should do so in the present matter as regards the Principle.

- (3) Mr Swan submits that this Principle is unknown in Scots law, that (relying on the affidavit opinion of Mr Clark) Scots law would not adopt the Principle, and that accordingly Guernsey law should not be developed so as to include the Principle.
- (4) Mr Wessels rejects the suggested analogy with Scots law, as already stated, but goes on to submit that, even if the analogy with Scots law is to be preferred to one with English law, Scots law would be developed by adopting this Principle (relying on the affidavit opinions of Professor Bennett); and so whether the right analogy be with English law or Scots law, either way it is appropriate for Guernsey law to be developed by incorporating the Principle.

### The Fund Ascertainment Principle

58. It is common ground between the parties that FL Holdings

- (1) cannot claim in the liquidation of FL Ireland an indemnity for either (a) the totality of the amounts owed by FL Ireland to creditors guaranteed by FL Holdings (in excess of US\$214 million); or (b) the dividends paid to the guaranteed creditors of FL Ireland (nearly US\$35 million), because of the rule against double proof, which it is agreed applies in Ireland, in Guernsey and in England and Wales;
- (2) cannot set off any such indemnity in the liquidation of FL Holdings against the net Agreed Claim of FL Ireland, because of the same rule against double proof.

Accordingly FL Holdings seeks to rely on the fund ascertainment principle. After the above, far from brief, introduction, I turn therefore to the Principle as long established in English law, i.e. the second issue in paragraph 36(2) above.

59. The Principle has a long history in English law. It was recognised in embryonic form in *Jeffs v Wood* (1723) 2 P Wms 128; 24 ER 668, and was not then a new principle in proceedings in chancery. Early in Queen Victoria's reign it was applied by Cottenham LC in *Cherry v Boulton* (see paragraph 34 above). In *Cherry* (a case involving bankruptcy) the Lord Chancellor distinguished this Principle from set-off, though recognising that in earlier cases it had sometimes been so described. Since 1839 it has been adopted on numerous occasions, especially in relation to insolvent liquidations of companies. The Principle has been recently re-considered in the judgment of the English Court of Appeal (delivered by Chadwick LJ) in *In re SSSL Realisations (2002) Ltd* [2006] Ch 610 (*SSSL*), making reference to the earlier cases for the most part unnecessary.
60. In *SSSL* a company (G plc) traded as a retailer of petrol which it bought from suppliers and sold on to petrol stations owned by one of its subsidiaries, *SSSL (S) Ltd*. G plc was also in charge of bank borrowing for its whole group of companies, and lent on to its subsidiaries the funds they needed to trade. The supply of petrol gave rise to liabilities for duty payable to Customs and Excise, which were deferred by the giving of a bond by *AIG Europe (UK) Ltd* (*AIG*), against a deed of indemnity provided to *AIG* by six of the group companies including G plc and S Ltd. A number of issues were raised, including some raised for the first time on appeal. The first issue considered in detail by the Court of Appeal was whether the liquidators of F plc were entitled to disclaim the deed of indemnity provided to *AIG* as being "onerous property", and the Court of Appeal held that such disclaimer was not to be

permitted. The second issue was whether the liquidators of S Ltd could bar proof by G plc in the liquidation of S Ltd in reliance on clause 8.2 of the indemnity, which (in terms not dissimilar to the clauses of the guarantees in the present case) provided for the indemnitors – including G plc – to be prevented from proving in competition with AIG (and indemnitors) in the liquidations of other indemnitors – including S Ltd – unless and until all the money owing to AIG had been irrevocably paid in full. This second issue also raised the question whether AIG could waive reliance on this clause unilaterally. The Court of Appeal held that unilateral waiver by AIG was not permissible, and that S Ltd could rely on the clause to prevent G plc proving in competition with AIG and other indemnitors in the liquidation of S Ltd. As Chadwick LJ made clear in paragraph 55 of his judgment (page 636) this second issue would not have arisen (in practice) unless, notwithstanding the Principle, G plc would receive a dividend in the liquidation of S Ltd if G plc were permitted to prove in that liquidation.

61. The third issue decided by the Court of Appeal in *SSSL* involved the application of the Principle, and whether on such application in S Ltd’s liquidation, G plc if permitted to prove would receive any dividend on its proof. It was submitted to me by Mr Swan that the part of the judgment dealing with this third issue was obiter, and not an essential part of the reasoning of the Court of Appeal. In my judgment paragraph 68 of the judgment of Chadwick LJ makes it clear that this was a third head under which G plc’s attempt to prove in S Ltd’s liquidation was rejected by the Court of Appeal, and was not mere obiter dicta.
62. I start with citation of an earlier passage in Chadwick LJ’s judgment in which he described in general terms “the rule in *Cherry v Boulton*” which I am calling “the fund ascertainment principle”:

“12. *The rule in Cherry v Boulton is applied in equity to the distribution of a fund. Put very shortly (at this stage) equity requires that a person cannot share in a fund in relation to which he is also a debtor without first contributing to the whole by paying his debt. The operation of the rule may be illustrated by an example. Suppose A is indebted to B in the sum of £1,000. B dies leaving his residuary estate to be shared equally amongst four beneficiaries, of which A is one. After the payment of B’s debts, administration expenses and specific legacies (but before A has paid the £1,000) the amount of the residuary estate in the hands of B’s executors is £10,000. A must bring his debt into account before he can receive his share. So the amount which he will receive will be £1,750 (¼ of {£10,000 + £1,000} - £1,000). The other three beneficiaries will each receive £2,750. It can be seen that, if A’s debt were greater than his aliquot share of the whole, he would receive nothing in the distribution ( $\{1/n(x+y)-y\} < 0$  if  $x/(n-1) < y$ ).*

13. *The rule is displaced in bankruptcy (and in corporate insolvency) by the statutory requirement that mutual debts and credits be set off; so that only the balance is provable as a bankruptcy debt: see, now, section 323 of the Insolvency Act 1986 and rule 4.90 of the Insolvency Rules 1986. So, if B has four creditors to each of whom he owes, say, £3,000 but one of whom (A) owes him £1,000, A can only prove in B’s bankruptcy for the balance of his debt after set-off (2,000). If the assets to be distributed in the bankruptcy are £10,000, A will receive £1,818 (2/11 of £10,000). And, in such a case, B could not prove in A’s bankruptcy. B’s debt (£1,000) would be extinguished by set-off in both bankruptcies. Had the rule in *Cherry v Boulton* applied in such a case, A would have received £1,750 (3/12 of {£10,000+£1,000} - £1,000).*

14. *The statutory requirement does not extend to a case where one of the debts is not provable in the bankruptcy of the debtor by virtue of the rule against*

*double proof. That rule prevents a surety from proving in the bankruptcy of the principal debtor until the creditor has been paid in full. So, if (in the example given) A's claim against B (£3,000) is for an indemnity in respect of A's liability as surety for a debt owed by B to C, A cannot prove in the bankruptcy of B in competition with C: In re Oriental Commercial Bank; Ex p European Bank (1871) LR 7 Ch App 99, 103-104 and In re Polly Peck International plc [1996] 2 All ER 433, 442H. And, further, A's claim for an indemnity (£3,000) cannot be set off (so as to extinguish) B's debt (£1,000) when B proves in the bankruptcy of A: Secretary of State for Trade and Industry v Frid [2004] 2 AC 506, para 13.*

15. *The first new point raised by the liquidators of [S Ltd] in their respondent's notice is whether, in a case where the rule against double proof prevents the surety from setting off, in his own bankruptcy, his claim for indemnity against the debt which he owes to the principal debtor - and so prevents the surety from proving in the bankruptcy of the principal debtor - the surety's insolvent estate must be administered so as to give effect to the rule in Cherry v Boulton 4 My & Cr 442. Again put shortly (at this stage), it is said that, in such a case, the equitable rule is not displaced by the statutory requirement that mutual credits and debits be set off - because the rule against double proof prevents the application of the statutory requirement - so that there is no reason why it should not be given effect. And, it is said, that is what the decision of this court in In re Melton [1918] 1 Ch 37 requires.*
16. *The relevance of the new point is that [S Ltd] as a party to the deed of indemnity, is in the position of surety vis-à-vis [G plc] in respect of the debt owed by [G plc] to AIG. Further, [S Ltd] (it is said) is in the position of surety vis-à-vis [G plc] in respect of the debts owed to the banks. As surety [S Ltd] would have claims for indemnity against [G plc]. But the effect of the rule against double proof is that [S plc] cannot set off its claims for indemnity against [G plc] proof of debt in its liquidation. So, if [G plc] is entitled to prove for its debt in the liquidation of [S Ltd] (in competition with AIG), it will prove for the whole of that debt. But, it is said, if the rule in Cherry v Boulton applies, [G plc] will have to bring into account in the liquidation of [S Ltd] - not by way of set-off, but as a contribution to the whole of the distributable fund - the value of [S Ltd's] claims to indemnity. And, it is said, the effect of that (on the figures) is that [G plc] would receive nothing in the distribution. (The figures are set out in para 68, post.)"*

What this passage makes plain for the purposes of applying the Principle is that application of the Principle does not run counter to the rule against double proof: on the contrary its application will usually become necessary only in the cases in which set-off is barred by the rule against double proof. It also makes plain that the statutory mutual dealings provisions in English law do not displace the application of this Principle.

63. Paragraph 68 of Chadwick LJ's judgment shows the effect of the Principle on the facts of SSSL:

*"68. The liquidators of [S Ltd] contend that, in the light of the debts owed to the banks (£60m) and to AIG (£10m) in respect of which, vis-à-vis [G plc], [S Ltd] is surety, [S Ltd] has a right of indemnity amounting to approximately £70m. The assets remaining for distribution in the liquidation of [S Ltd] amount to £39m, or thereabouts. The debt owed by [S Ltd] to [G plc] is of the order of £127m. Debts to trade creditors amount to some £6m. It is*

*accepted that the indemnity claims cannot be set off against [G plc's] proof of debt. But if on those figures – which I adopt only for the purpose of illustrating the point – [G plc] were required to bring [S Ltd's] claims for indemnity into account as a contribution to the whole fund distributable in the liquidation of [S Ltd], the dividend which would be payable on [G plc's] proof (£68m) would be less than the amount of that contribution (£70m). On the basis of those figures the whole fund distributable in the liquidation of [S Ltd] would be £109m (£70m+£39m). The provable debts would amount to £203m (£127m+£60m+£10m+£6m). So the dividend payable on [G plc's] proof would be £68.2m (109/203 of £127m). So [G plc] would receive nothing in the liquidation of [S Ltd]. That would provide a further reason why (absent disclaimer) [G plc] should not be permitted to prove in the liquidation of [S Ltd] in breach of clause 8.2(b) of the deed of indemnity: to permit [G plc] to prove in [S Ltd's] liquidation would be pointless. On the other hand, if the conclusions which I have reached on the first two issues are correct, it must follow that the Cherry v Boulton point 4 My & Cr 442 will not arise. [G plc] could not prove in the liquidation of [S Ltd] even if, by proving, it would receive a dividend. But the point has been fully argued in this court and, as it seems to me, it is sensible to address it.”*

64. The main earlier authority relied on by the Court of Appeal in *SSSL* was *In re Melton* [1918] 1 Ch 37 C of A. I need not set out the facts of *Melton* which were far from those of *SSSL* and of the present matter. One important point for present purposes is that in *Melton* the English Court of Appeal unanimously held that the rule against double proof is not a bar to the application of the Principle (rejecting as wrongly decided the first instance decision of *In re Binns* [1896] 2 Ch 584 North J). A long citation was made from the trenchant judgment in *Melton* of Scrutton LJ (see [2006] Ch at pages 644-646) which I treat as incorporated in my judgment for its precision and clarity (always a noteworthy feature of the judgments of one of the best commercial judges in England and Wales in the 20<sup>th</sup> century).

65. I continue citation of *SSSL* with Chadwick LJ's summary of the principles laid down in *Melton*:

“79. *In my view the following principles can be derived from the judgments of this court in In re Melton* [1918] 1 Ch 37.

(1) *The general rule applicable in the distribution of a fund is that a person cannot take an aliquot share out of the fund unless he first brings into the fund what he owes. Effect is given to the general rule, as a matter of accounting, by treating the fund as notionally increased by the amount of the contribution; determining the amount of the share by applying the appropriate proportion to the notionally increased fund; and distributing to the claimant the amount of the share (so determined) less the amount of the contribution. The rule can be expressed in the form:  $D = I/n \text{ of } (A + C) - C$ , where  $I/n$  is the proportion which the aliquot share bears to the whole,  $A$  is the amount of the assets to be distributed before taking account of the contribution due to the fund from the claimant,  $C$  is the amount of the contribution, and  $D$  is the amount which the claimant is entitled to receive in the distribution. It can be seen that the claimant will receive nothing by way of distribution if  $C > I/n \text{ of } (A + C)$ .*

(2) *That general rule is applicable not only where the claimant (X) is indebted to the fund but also where the fund has a right to be*

*indemnified by X against a liability which the fund may be required to meet in the future, as surety for a debt owed by X to a creditor (Y). It is not necessary that the liability to Y has been satisfied out of the fund: it is enough that it may have to be satisfied in the future.*

.....

- (3) *The general rule – as applicable to a case where the fund has a right to be indemnified by X – is not displaced in a case where the claimant (X) is in bankruptcy. Application of the general rule, in such a case, is not inconsistent with the rule against double proof, which would prevent the fund from proving in the bankruptcy of X in competition with the creditor Y.”*

66. Chadwick LJ next dealt with three issues which had not arisen for decision in *Melton*:

*“The first is whether the general rule to which I have referred has any application in the distribution of a fund in the course of an insolvent administration. As I have said, the rule must yield to the principle of mutual set-off – now enacted (in the context of bankruptcy) as section 323 of the Insolvency Act 1986 and reflected (in corporate insolvency) in rule 4.90 of the Insolvency Rules 1986. But the question remains whether the rule is applicable in a case where – by reason of the rule against double proof - there is no set-off between X’s claim against the fund, on the one hand, and the fund’s right to be indemnified by X on the other hand.*

81. *The second question is whether – if the rule does remain applicable in such a case – the amount which is to be brought into account (as X’s contribution to the whole) is the full amount of the fund’s liability (as surety) to the creditor Y; or some lesser amount to reflect the fact that (by reason of the fund’s insolvency) the liability to Y will not be met in full.*

82. *The third question is whether – if the rule is applicable – the amount which would otherwise have to be brought into account by X is reduced in a case where X is insolvent and that insolvency commenced before the point at which X (or his trustee or assignee) became entitled to claim his share in the fund.”*

67. Chadwick LJ, before answering those questions, dealt with the first instance decision of Luxmoore J in *In re Fenton (No.2)* [1932] 1 Ch 178, in which it was held (without reference to *Melton*, though that case was cited) that, in an insolvency, for the trustee to rely on the Principle would infringe the rule against double proof. In *SSSL* the Court of Appeal held that the reasoning in *Fenton (No.2)* could not be reconciled with the judgments in *Melton*, and was based on a misunderstanding of the Principle and the object of the rule against double proof (paragraphs 91-92 of the *SSSL* judgment).

68. I quote paragraphs 93-96 of Chadwick LJ’s judgment to show the reasoning by which *Fenton (No.2)* was overruled:

“93. *The basis of the rule against double proof was explained by Robert Walker J in In re Polly Peck International plc [1996] 2 All ER 433, 442:*

*“Much the commonest situation in which the rule against double proof applies is that of suretyship. Indeed it has been said that it applies only in a situation which actually is, or is analogous to, that of suretyship (the latter category includes the old cases on*

*negotiable instruments considered in In re Oriental Commercial Bank; Ex p European Bank LR 7 Ch App 99). It is therefore convenient to set out some very elementary rules as to suretyship, shorn of complications arising from the provision of security or from the Ellis v Emmanuel (1876) 1 Ex D 157 distinction” – the distinction between the guarantee of a part of a debt and the guarantee of the whole debt subject to a limitation on the guarantor’s liability: see Ellis v Emmanuel (1876) 1 Ex D 157, discussed in Barclays Bank Ltd v TOSG Trust Fund Ltd [1984] AC 626, 643-644. “In what follows, C is the principal creditor, D the principal debtor, and S the surety (and all are companies).*

“(1) *So long as any money remains due under the guaranteed loan, C can proceed against either D or (after any requisite notice) S.*

“(2) *If D and S are both wound up, C can prove in both liquidations and hope to receive a dividend in both, subject to not recovering in all more than 100p in the pound.*

“(3) *S’s liquidator can prove in D’s liquidation (under an express or implied right of indemnity) only if S has paid C in full (so that C drops out of the matter and S stands in its place).*

“(4) *As a corollary of (3) above, S’s liquidator cannot prove in D’s liquidation in any way that is in competition with C; though S has a contingent claim against D (in the event of C being paid off by S), S may not make that claim if it has not in fact paid off C.*

*“The situation in (2) above is what insolvency practitioners call a ‘double dip’, which is permissible; the situation in (4) above is the simplest case of what would be double proof, which is not permissible.*

*“So far as the basis of the rule needs (or indeed allows of) further explanation it is that the surety’s contingent claim is not regarded as an independent, freestanding debt, but only as a reflection of the ‘real’ debt – that in respect of the money which the principal creditor had loaned to the principal debtor.”*

94. *The rule against double proof protects the principal creditor (C, in Walker J’s nomenclature) from the competing claim of the surety (S) in respect of the same debt in the liquidation of the principal debtor (D). It also protects the other creditors in D’s liquidation from two claims (those of both C and S) in respect of the same debt. The object of the rule is not to swell the assets available for distribution in the liquidation of D; it is to limit the claims that can be made in the distribution of those assets by ensuring that there is no more than one proof in respect of each debt. There is no reason in principle why the rule against double proof should have the effect of enabling the liquidator of D to collect an asset which he could not collect under the general law. In particular, there is no reason why the rule against double proof should have the effect of enabling the liquidator of D to collect an asset the collection of which would otherwise be subject to the rule in Cherry v Boulton 4 My & Cr 442.*

95. *By contrast, the rule in Cherry v Boulton – as applied in In re Melton [1918] 1 Ch 37 – protects the creditors in the liquidation of S (which will, or*

*may, include the principal creditor, C) from the claim of the principal debtor (D) to share in the distribution of the assets distributable in that liquidation without bringing into account his contribution to those assets. If D is to share in the assets distributable in the liquidation of S, he must contribute, under the express or implied indemnity, to those assets. He must do so, because the burden of C's claim in the liquidation of S should fall primarily on D to the relief of the other creditors proving in that liquidation.*

96. *Allowing both the rule against double proof and the rule in Cherry v Boulton to have effect in a case where both principal debtor (D) and surety (S) are insolvent strikes a fair balance, as it seems to me, between the interests of the creditors in both liquidations. The right of the principal creditor (C) to prove in both liquidations is unaffected. C does not compete against S in the liquidation of D; and, in the liquidation of S, C's share is not diminished, but the burden of his claim falls primarily on D to the relief of the other creditors. The other creditors of D are not required to compete with two claims in respect of the same debt. The other creditors of S benefit to the extent that, if D claims in the liquidation of S, the burden of C's claim falls primarily upon D. It is, I think, important to remember that, if D and S have separate creditors, the separate interests of those creditors must be respected. ...."*

69. I have set out these passages at some length, because Mr Swan invited me to accept *Fenton (No.2)* as correctly, and *SSSL* as incorrectly, decided. With great respect this is not a sustainable submission, not least because in *Fenton (No.2)*, a case at first instance, the decision on appeal in *Melton* was ignored, and because the full and detailed reasoning in *SSSL* is not only binding in English law, but in my judgment clearly right, and leads to a fair result.

70. Chadwick LJ then sought to answer the three questions not decided in *Melton* (paragraph 66 above) as follows. As to the first question, it was held that, where set-off is not available, the Principle is applicable. Reference was made to several English cases from 1866 onwards, to a recent case in Hong Kong, and to the observation of Lord Chelmsford LC in *In re Overend, Gurney and Co: Grissell's Case* (1866) LR 1 Ch App S28 at pp.536-537 to the effect that where there is no set-off under the statute "it necessarily follows in the last place" that equitable principles must fill the gap. Chadwick LJ in paragraph 100 answered this first question:

"100 *It follows that I would hold that the general rule, to which I have referred in para 79 [see paragraph 65 above of this judgment] has application in cases in which there is no set-off between a claim by the fund in liquidation against the creditor and the debt provable by the creditor in the liquidation. Those cases include cases where mutual set-off is prevented by the rule against double proof.*

71. As to the second question (paragraph 66 above) this was answered by holding that it is the full amount of the fund's liability as guarantor (here FL Holdings') which must be brought into account under the Principle. This was the reasoning:

"103 *The principle that it would be inequitable to allow the contributor to compete against the other persons entitled to share until the fund has been made whole requires that – as between the contributor and the other persons entitled to share in the fund – those others should not have to bear any part of the debt for which the contributor is liable as principal debtor. That requirement can be met only if the amount which the contributor has to*

*contribute (before he can share in the fund) is the whole amount of the debt for which the creditor has proved.*

*104The point can be illustrated by an example. Suppose that X, a creditor of the fund (S) in respect of a debt of £3,000, is debtor to Y in the sum of £1,000 and that S is surety for that debt; and suppose that there are two other creditors of the fund (P and Q) each in respect of a debt of £2,000. Each of the four creditors P, Q, X and Y prove for their debts against the fund. Suppose that the amount of the fund (before taking into account any contribution from X) is £4,000. If the fund were distributed without regard to the rule in *Cherry v Boulton* 4 My & Cr 442, each of P and Q would receive a dividend of £1,000 (2/8 of £4,000), X would receive a dividend of £1,500 (3/8 of £4,000) and Y would receive a dividend of £500 (1/8 of £4,000). But the effect of the rule in *Cherry v Boulton* – as explained in *In re Melton [1918] Hope I Ch 37* – is that X cannot receive a dividend without bringing in a contribution to the fund. What is the amount of the contribution that can be required of X? If X were to make a full contribution, equal to the amount of Y's proof (£1,000), each of P and Q would receive a dividend of £1,250 (2/8 of {£4,000 + £1,000}), Y would receive a dividend of £625 (1/8 of {£4,000 + £1,000}) and X would receive £875 net (3/8 of {£4,000 + £1,000} - £1,000). The whole burden of the dividend which Y receives will fall on X (£1,500 - £875 = £625). If, on the other hand, X were required to contribute only the amount of the dividend which Y would have received if X had not proved (1/5 of £4,000 = £800), each of P and Q would receive £1,200, Y would receive £600 and X would receive £1,000. Part of the burden of the dividend which Y receives will fall on P and Q. (The £600 which Y receives is shared as to £500 by X (£1,500 - £1,000 = £500) and as to £100 by P and Q – as to £50 each £1,250 - £1,200 = £50.)*

*105It follows that I would hold that the answer to the second question is that the amount which is to be brought into account (as X's contribution to the whole) is the full amount of the fund's liability (as surety) to the creditor Y."*

It is not in every case that the equitable and fair nature of the Principle as applied will be as clear and obvious as in the examples given by Chadwick LJ. But I am satisfied that in the great majority of cases the Principle will if applied achieve a much fairer result than if it is not applied.

72. Turning to the third question (paragraph 66 above), Chadwick LJ showed that in *Melton* it had been decided that where the insolvency of the claimant postdates the insolvency of the fund (here, by the liquidation of FL Holdings before FL Ireland was wound up), the full amount of the indemnity must be brought into account.
73. Though not strictly material in this case, I should add that he went on to hold that where the insolvency of the claimant predates the insolvency of the fund in double corporate insolvency cases, the full amount of the indemnity again must be brought into account. He relied for this conclusion on a number of English cases including *In re Leeds and Hanley Theatres of Varieties Ltd* [1904] 2 Ch 45 Buckley J, and *In re National Livestock Insurance Co Ltd* [1917] 1 Ch 629, and the Hong Kong case of *In re Kowloon Container Warehouse Co Ltd* [1981] HKLR 210, and he rejected the dicta to the contrary in *Fenton (No.2)* above.
74. Standing back here to look more broadly at the Principle as described and reasoned at length in *SSSL*, in my judgment the Principle is both logical and fair to the body of creditors, both the creditors who have the benefit of the insolvent company's guarantees, and the other

creditors who are not so guaranteed. As examples can readily show, where the debt owed by the guarantor company to the principal debtor is a much larger proportion of the guarantor's total liabilities (unlike here where FL Ireland's debt of nearly US\$6million is dwarfed by the total Agreed Claims of nearly US\$690 million), justice requires the total indemnity amount to be brought into account. Thus in *SSSL*, if G plc's indemnity liability to S Ltd was brought into account (£70 million), the dividend payable on G plc's claim for the debts owed by S Ltd would be less (at £68 million), and G plc would receive nothing in the liquidation of S Ltd. But if G plc's indemnity liability were not to be brought into account, G plc would have received a substantial dividend in S Ltd's liquidation, to the detriment of the other Creditors, including the guaranteed creditor *AIG*, a result which in my judgment would have been unjust and inequitable.

75. The Principle as defined in *SSSL* now has to be considered as to whether it should be held to be part of Guernsey law.

### **Is the fund ascertainment principle to be applied as part of Guernsey law?**

76. It is convenient to start consideration of Mr Wessels' third issue (paragraph 36(3) above) with the submissions of Mr Swan that the development of Guernsey law in this field should be by reference to Scots law.
77. Neither Professor Bennett nor Mr Alistair Clark QC has identified any case in Scotland in which the Principle (or any similar principle) has been considered or indeed argued. On the question whether the courts of Scotland would adopt such a principle in a future case, their opinions are opposite. In paragraphs 18-20 of his first affidavit Professor Bennett has stated;

*“18. As I understand it the rule in Cherry v Boulton is to the effect that, where a person is indebted to a fund and is also entitled (with others) to a share of that fund, in order to calculate his due share of that fund he is required (notionally) to contribute the amount of his debt to the fund. The total amount of the fund as thus augmented is then divided among those entitled to it (including the debtor) according to their due shares.*

*19. In Re SSSL Realisations (2002) Ltd [2006] Ch 610 at paras.101-105, the court upheld the above principle and also decided that if, in the above circumstances, the debtor is insolvent the amount he must 'contribute' to the fund for the purposes of the calculation of parties' entitlements is the actual amount of his debt, not what the fund might receive by way of dividend on the insolvent estate. I note that there appears to have been no previous authority in English law on the point (SSSL at para.102).*

*20. Although I have not been able to identify a Scottish authority on the principles stated in paragraphs 18 and 19 above, in my opinion Scots law would apply them in like circumstances; to do otherwise would not result in a correct accounting between the parties in respect of their respective claims, nor in relation to the claims of other creditors.”*

Mr Clark agreed that in no Scots case or law textbook has any reference been made to the Principle. In paragraphs 24 and 25 of his affidavit, he stated:

*“24. The rule is accordingly one relating to the ability to collect assets, which forms part of “the general law” and it therefore appears, on the face of it, to be of application to many other factual circumstances than those involving cautionary obligations. I am not aware of it having been argued or applied in such other circumstances in Scotland, in my view, if a rule or principle of*

*that width and general applicability, dating from 1839, had been viewed as an appropriate rule or principle by the Scottish courts, it would have been the subject of decision before now.*

25. *In my opinion, the Scottish courts have dealt with circumstances such as those in the present dispute by applying the rule against double ranking so as to exclude any right of set off. They have regarded protection of the creditors, of in this case FL Ireland, from the effects of double ranking as the key principle. They have done so without apparently finding it necessary to use the rule in Cherry v Boulton to adjust or deal with the position of the paying cautioner.”*

Professor Bennett in his reply affidavit stated (inter alia):

- “10. *The argument is advanced, in paragraph 24 of the Clark affidavit, that the principle known in England as the rule in Cherry v Boulton is not known to Scots law. Clearly, if that is the case, insolvency compensation in Scotland is limited to what in England is insolvency set-off in the narrow sense – a result which Lord Hope’s comments in paragraph 34 of his judgment in Frid suggest that he would find unsatisfactory.*
11. *Unsurprisingly, the “rule in Cherry v Boulton” is not referred to in Scots law as such. However, the principle that, in order to achieve the just and equitable distribution of a fund in medio, a party who is indebted to the fund is required to bring that indebtedness into account (even if it is not in fact sought to be recovered, or recoverable, by the fund) is recognised in the Scots doctrine of “collation” (which is known in England as hotchpot). In my opinion, the reliance upon the retention cases cited in the Clark affidavit is misplaced because the court in those cases was not being called upon to decide the point now in issue..... The issue to be decided in the present case, and which confronted the English Court of Appeal in SSSL, is divorced from any attempt to effect a recovery. It concerns the proper administration of the cautioner’s own estate and is not, therefore, truly a retention issue at all.*
12. *The real question arises entirely within the liquidation of FL Holdings; it is whether the claims of that company’s other creditors should be abated by the payment of a dividend to FL Ireland even though those claims are already abated because some of FL Holdings’ assets, in the form of its claims against FL Ireland, are irrecoverable due to the rule against double proof (in other words, whether FL Holdings’ other creditors should be doubly prejudiced). This concerns the just and equitable distribution of what there is to distribute in the FL Holdings estate. Rules of law may be particular to different jurisdictions; principles of justice tend to be universal.*
13. *I therefore adhere to the opinion previously expressed that, confronted by the facts which faced the English Court of Appeal in SSSL, the Court of Session would reach the same conclusion in order to do justice. I do not consider that the modern Court of Session would feel constrained to deliver an unjust judgment by a nineteenth century decision on retention where the court did not have the benefit of argument about the interaction of the rule against double ranking with the general principles applicable to the distribution of funds.”*

78. In my judgment it would be inappropriate for me, sitting in the Royal Court of Guernsey, to reach a firm decision as to whether the Courts of Scotland will, when and if a suitable case arises for decision, adopt the Principle, or adapt the doctrine of “collation” in Scots law to achieve a similar result. Though Professor Bennett’s opinion as to the justice of the Principle coincides with my own judgment, I cannot proceed in this case on the basis that the Court of Session will agree. Accordingly I find it necessary to deal with this issue taking a broader approach, in considering whether any development of Guernsey law in this field is more appropriately made by reference to Scots law, or to English law, or otherwise.
79. The Principle was developed by the courts of equity in England and Wales which exercised a jurisdiction independent of the common law courts. The division between these courts was not a necessary fact. Equitable principles could have been developed by the common law courts themselves. By the Supreme Court of Judicature Acts 1873 and 1875 the rules of common law and equity were thereafter to be administered in the same courts, though remaining separate rules: see Snell’s Equity, Chapter 1.
80. The Royal Court of Guernsey, in developing Guernsey law to deal with new and more complex cases, has not infrequently used the analogy of English equitable (and common law) principles for this purpose, except when such principles clash with the fundamentals of Guernsey customary law. Thus in *Roger v Roger* (2003, Unreported) the Guernsey Court of Appeal said in paragraph 16 (per Rokison JA):

*“Guernsey law has, as we understand it, generally followed and applied English equitable principles in appropriate cases, and we see no reason to exclude the possibility of proprietary estoppel being involved in an appropriate case.”*

Proprietary estoppel is a doctrine by which rights over another’s land may be acquired, not through the usual methods of transfer of real property, but by the acquiescence or encouragement of the landowner. The Court of Appeal recognised this doctrine as being capable of application in Guernsey, while in *Roger* finding the necessary factual basis for proprietary estoppel did not exist. This followed earlier statements by the Royal Court, as for example in *Beachcomber* (above) the Bailiff (Sir Charles Frossard) in summing up to the Jurats stated that

*“the Courts of Guernsey have recognised equitable principles over the centuries.....”*

81. So in *Stuart-Hutcheson v Spread Trustee Co Ltd* (15 July 2002, unreported) the Court of Appeal per Clarke JA dealt with trusts in Guernsey law, looking at the time before the Trusts Law (Guernsey) 1989 was registered, in these general terms:

*“19. Trusts do not form part of Norman law from which Guernsey customary law is, in part, derived. The trust is, in origin, an English law concept, developed by English judges and, subsequently, by the Courts of those countries whose law is, or is derived from English law. But well prior to 1989, the concept of a trust and the concomitant duties of a trustee and rights of a beneficiary had been recognised in Guernsey. As the Deputy Bailiff said in the present case:*

*“Without undertaking any comprehensive review of what I believe is overwhelming evidence for such statement (that the concept of trusts was, in principle, recognised in Guernsey prior to 1989) one need only look at a variety of facts:- the large number of statutory trusts, either created or envisaged on subjects ranging from testamentary matters in the 19<sup>th</sup> century to social insurance matters in the 1970s (coincidentally the Law immediately following the Trust Law in volume XXXI of the Ordres en Conseil is the Saint*

*Peter's Church Hall (Trust) (Guernsey) Law, 1989); the number of trusts administered by the Royal Court itself; the widespread practice of many decades, at the least, of creating trusts, either testamentarily or inter vivos; and (perhaps most pertinently) the jurisprudence of the Royal Court itself in recognising the existence of trusts (for recent examples of which, see the observations of Frossard DB in C K Consultants (Plastics) Limited and Frossard B in Beachcomber Hotels Limited)."*

*Further information as to the history of the development of trust law may be found in an article of Advocate Robilliard: "Foundations of Guernsey as a Trust Jurisdiction" Vol 2 No 8 Trust and Trustees (1966) pp 6 – 10.*

20. *That, prior to the 1989 Law, trusts had become part of Guernsey law is not in dispute; what is in issue is the extent to which the general law of trusts in England had become part of the law of Guernsey. To that question the answer is, in my judgment, to be found by a consideration of the process by which trusts came to be part of Guernsey law. They did so because settlors established trusts, whether inter vivos or by will, the validity of which was recognised and, where necessary, enforced by the Royal Court. In addition the Legislature in a number of Laws recognised and adopted the notion of trusteeship. In thus importing, as it were, the English concept of a trust and trustees those concerned must be regarded as having intended to introduce the trust concept with its usual incidents, unless they were inconsistent with some provision of Guernsey customary or statute law or otherwise inapposite or inapplicable. The trustee's obligation to account for his execution of the trust is a characteristic of a trust, as is recognised by Article 2 of the Hague Convention on the Law Applicable to Trusts and on their Recognition: see the Schedule to the English Recognition of Trusts Act 1987.*
21. *I find support for this view in the observations of Frossard, DB, in CK Consultants (Plastics) Limited v Vines & Barnet Christie Finance Limited (1982). In that case the question arose as to whether or not constructive trusteeship was recognised in Guernsey. The argument was that, even if Guernsey recognised trusts, it did not recognise the notion of constructive trusts. The Deputy Bailiff said:*

*"Before I refer to those cases I must consider Mr van Leuven's submission as to whether and to what extent the law of trusts and, in particular, the doctrine of constructive trusts is part of the law of Guernsey..... It is of interest to note that this very Court is trustee of various charitable funds and Pothier, a very learned author of the customary law, himself, in Volume VII p.547 recognises a fideicommiss which is, of course, translated a trust. I accept that our law of trusts has not progressed as in England and we do not have the many statutes on trust as England has. Nevertheless, I am of the opinion that trusts are recognised in Guernsey and for guidance we seek reported decisions in other jurisdictions but disregard their statutes....."*

*I now turn to the more difficult question and that is, is the concept of constructive trusts part of our law. In my opinion, I answer, yes, because we recognize trusts".*

*In other words, the recognition and acceptance of trusts in Guernsey carried with it the need to seek guidance from jurisdictions, which have a law of*

*trusts, and recognition of the concept of constructive, as well as express trusteeship, as an integral part of the law of trusts.”*

82. Express and constructive trusts, and proprietary estoppel, were imports from English law to fill undoubted gaps in Guernsey jurisprudence, in so far as Guernsey statutes and customary law previously developed by the Guernsey Courts had not already filled such gaps, in whole or in part.
83. The Court’s attention was, however, rightly drawn by Mr Wessels and Mr Swan to some observations of mine in delivering the judgment of the Court of Appeal in *Pirito v Curth* (10 April 2003, unreported) in which, when considering the position of a man and a woman who have lived together unmarried for many years, I said:

*“34. The Court of Appeal [in a previous case] did not express its conclusion in terms of an irrebutable presumption, in my respectful view, correctly. In my judgment it is important that there should not be imported into the law of Guernsey the presumptions of advancement and the like which have caused so much difficulty in English law, and which have ossified English law despite the changes in social circumstances. I have already given one example of direct relevance to this case: in English law there is a presumption of advancement by a man to his fiancée, even if they never marry, but no such presumption in the case of a man and a woman who live together for 25 years, never become engaged and never marry. Such presumptions are a bad example of lazy thinking in English law.*

*35. Mrs Haskins argued that equitable principles of English law form part of the law of Guernsey, and must be applied in the same way as in English law. For my part I do not consider that such principles can be imported wholesale into the Guernsey law of real property, which is derived from Norman not English origins, and which is in many respects very different from English law, particularly English statute law from the major statutory reforms of 1925 onwards.”*

But I should emphasise that what I said in *Pirito* was not intended to detract from the helpful assimilation of principles of English law, both equitable and of the common law (and sometimes from English statutes), where these assist in the wise development of Guernsey law to meet new challenges (see for example *Morton v Paint* (1996) 21 GLJ 36 Guernsey Court of Appeal) and the requirements of justice.

84. Mr Wessels also stressed in his submissions that Guernsey customary law is itself founded on principles of fairness, for which the French term “*équité*” was used, for example, by De Férière in his *Dictionnaire de Droit et de Pratique* of 1771, under this title:

*“ÉQUITÉ, est un juste tempérament de la Loi, que en adoucit la rigueur, en considération de quelques circonstances particulieres du fait. Ainsi cette équité est un juste retour au droit naturel, en retranchant les fausses & rigoureuses consequences qu’on veut tirer de la disposition de quelque Loi, par une trop rigoureuse explication des termes dans lesquels elle est conçue, ou par de vaines subtilités qui sont évidemment contraires à la Justice, & à l’intention du Législateur.*

*Cette, équité, qui doit être la régie de la Justice, doit être préférée à la disposition de la Loi même, lorsque la question qui se présente à juger n’est pas expressément*

*décidée par la Loi, ou que le sens & les paroles de la Loi peuvent, à cause de leur ambiguité, recevoir quelque interprétation.”*

I should, however, add that “équité” in this context means “fairness” or “justice” and is not synonymous with the separate set of English legal principles called “equity”.

85. My conclusions as to whether the Principle should be recognised as part of the Guernsey law of insolvency are these:

- (1) the concept of a limited company was imported into Guernsey law from English law;
- (2) since its importation into Guernsey law in the 1880s it has naturally been appropriate to look to English law to help in the solution of problems concerning companies which are not covered by Guernsey statutes or customary law;
- (3) I reject Mr Swan’s submission that in this field Guernsey should look to Scots law for guidance, because Scots law is less clearly developed in this field, and because the analogy with Scots law as being based on civil law is of little real assistance in developing a field of law which is not based on Civil law but on English law;
- (4) in relation to insolvent companies the Principle affords a fair solution which is just and equitable for creditors of insolvent companies, whether they have proved on the basis of guarantees by the insolvent company of debts owed by the primary debtor, or on debts which are not so based;
- (5) though this Principle can be seen to have been developed in English law as an equitable principle, that is simply a matter of history, as it is a principle which could equally well have been developed as a principle of English common law;
- (6) in any event such an equitable principle can sensibly be adopted in Guernsey law because it is in no way incompatible with Guernsey statutes or customary law, and it adds to Guernsey law concerning insolvent companies the element of fairness and équité which I have described;
- (7) Guernsey, as a significant centre for financial services of many kinds, needs to develop its commercial laws in ways which provide just solutions in the relatively complex situations which arise, for example, in liquidations of commercial companies. English law provides, in my judgment, a more developed system of insolvency law for use by analogy, than the relatively undeveloped solutions in similar situations in Scots law.

86. So my answer to the third issue is that the Principle is consonant with the existing principles of Guernsey law, and is to be applied in the circumstances of this case. I should add that in this case I am considering only the insolvent liquidation of companies: whether the Principle is to be applied in other contexts in Guernsey law will be a matter for consideration in subsequent cases.

**Is FL Ireland under an obligation to FL holdings such that the Principle can be applied by the FL Holdings Liquidators?**

87. In my judgment FL Ireland is under an obligation to indemnify FL Holdings in respect of the liability of FL Holdings under its guarantees of FL Ireland’s debts. Accordingly the Principle

can be applied by FL Holdings liquidators. FL Ireland's liability in this respect to FL Holdings amounts to over US\$214 million, and this is the figure which would be brought into account in accordance with the Principle as explained in *SSSL*, resulting in no dividend being paid to FL Ireland. Even if only the dividends paid by FL Holdings to those who were guaranteed in respect of FL Ireland's debts (nearly US\$35 million) were brought into account, that sum would result in no dividend being paid to FL Ireland. But all this is subject to the fifth issue (paragraph 36 above) – whether the Principle is barred from application by the Guarantees or the FL Guernsey Agreement.

**Is the application of the Principle precluded by the terms of the FL Guernsey Agreement and/or the Guarantees?**

88. The relevant terms of the Guarantees are set out above in paragraphs 16-18. These are relatively standard non-competition clauses usually to be found in banking guarantees. The essence of them is that FL Holdings is not to exercise its rights of subrogation, reimbursement or contribution, or indemnity as against FL Ireland without the consent of the guaranteed creditors. The question is whether reliance by FL Holdings on the Principle involves the exercise of such rights without the required consent.
89. Mr Wessels' first submission is to ask rhetorically whether, assuming that the Principle can be excluded by a clear agreement that it should not apply (as Mr Wessels accepts), it can be excluded by an agreement between FL Holdings and one or more of the guaranteed creditors, not being an agreement with **all** FL Holdings' creditors. Mr Wessels' answer is that such an agreement with one or some but not all of the creditors offends the principle established by the House of Lords in *British Eagle International Airlines Ltd v Compagnie Nationale Air France* [1975] 1 WLR 758. *British Eagle* was a test case which turned on a statutory provision (section 302 of the English Companies Act 1948); this required the property of a company on its being wound up to be applied in satisfaction of its liabilities *pari passu*. This was similar to section 419 of the 2008 law (except for the matters to which the operation of that section is made subject). The airlines (two of which were the plaintiff claiming a sum and the defendant to that claim) had entered into a clearing house agreement under which debits and credits arising when member airlines performed services for one another were processed by the clearing house (IATA), and the airlines could not claim any payment directly from each other, but only from IATA. By a majority the House of Lords held that it was contrary to public policy for the provisions of section 302 to be contracted out of, and the legal requirements of liquidation must prevail over the clearing house agreement, which otherwise would have resulted in debts owing to British Eagle being applied not for the benefit of all its creditors but exclusively for the benefit of the clearing house members, thereby infringing section 302 and giving the clearing house members an unlawful preference (see the opinion of Lord Cross). Mr Wessels submitted that FL Ireland's reliance on an exclusion of the *pari passu* requirement contained in section 419 of the 2008 Law was equally an attempt to secure a preference, thereby infringing the Principle (which is, as Mr Wessels submitted, and I have held above, a principle applicable in insolvent liquidations in Guernsey).
90. Mr Swan responded to this point by relying on *Re Griffin Trading Company* [2000] BPIR 256, per Arden J at pages 267-268, where the rule in *Cherry v Boulton* was stated to give way "to contrary intention", relying on *Harvey v Palmer* (1851) 4 De G & Sm 425 and a passage in Derham on Set-Off. That seems to me not to be material, because Arden J was not there considering the Principle in connection with the statutory insolvency rules which the House of Lords considered in *British Eagle*; and further Arden J was not invited to consider whether a specific agreement with one or some of the creditors could be relied on, rather than all the creditors, which was also a relevant point in *British Eagle*.

91. The figures set out in paragraphs 8 and 9 above show that the guaranteed debts form only 31% of the Agreed Claims, so that there are parties to the FL Guernsey Agreement who were not parties to the Guarantees. It also appears from the FL Guernsey Agreement, Recital D, that there are claimants in the liquidation of FL Holdings who are not parties to that agreement (though one major claimant, ILFC, has abandoned its claims). It seems to me to be reasonably strongly arguable that reliance on the non-compete provisions of the Guarantees to bar the operation of the Principle would infringe section 419 of the 2008 Law, on the analogy of *British Eagle*. But for reasons given below, it is not necessary for me to reach a final conclusion on this argument.
92. Mr Wessels had a range of other arguments to which I turn. He submitted that the FL Guernsey Agreement (to which the original beneficiaries of the Guarantees and their assignees – see the table in paragraph 15 above – were all parties) made the Guarantees subject to that Agreement, and the Agreement amounted to an instruction or consent for the purposes of the Guarantees. He also submitted that the Agreement had, with the consent of all the relevant parties, superseded the Guarantee provisions, so that it is only the Agreement which is now material for this purpose. Mr Wessels relied on the totality of the provisions of the Agreement, but primarily on clauses 4.1, 8.1 and 8.2, Schedule 7, and paragraph 2 of Schedule 10 which formed part of this Court’s order of 9 January 2004. He submitted that clause 4.1 (para.25 above) requires the FL Holdings liquidators to act in accordance with Guernsey law and the Agreement – not any provisions to different effect in the Guarantees. As to clause 8.2 (para.26 above), the first proviso preserves the right of indemnity in respect of payments after the date of the Agreement if and in so far as not offending against the rule against double proof: the Principle does not offend against the double proof rule, and so clause 8.2 recognises that, as regards the dividends paid to the guaranteed creditors, FL Holdings can rely on the right to indemnity by FL Ireland. The second proviso in clause 8.2 preserves rights of set-off (if any) under Guernsey law in respect of rights of indemnity against FL Ireland, and in this context “set-off” should, he submitted, be interpreted broadly as including the Principle.
93. Mr Wessels also referred to the non-compete provisions considered in *SSSL*: see paragraph 3 of the judgment quoting clauses 8.2 and 8.3 of the deed of indemnity. The Court of Appeal in considering the second issue in *SSSL* at paragraphs 55-65 upheld the non-compete restriction in those clauses and would if necessary have granted an injunction to restrain an attempt to prove for the indemnity debt. But, as Mr Wessels emphasised, the Court of Appeal did not treat the *Cherry v Boulton* principle as relevant to this issue in *SSSL*, and by necessary implication treated the Principle as not barred from being relied on by the liquidators of S Ltd, a reliance which the Court of Appeal upheld in paragraphs 68-117 despite the non-compete provisions (which were not even mentioned in those paragraphs). This was, he submitted, a logical conclusion, because the non-complete clauses in *SSSL* (like those in the Guarantees in the present matter) were directed to S Ltd’s pursuit of indemnity claims against the principal debtor G plc, and not to the administration of S Ltd’s fund or the ascertainment of the amount of such fund. FL Holdings could not be said to be exercising any rights of contribution, reimbursement or indemnity contrary to the terms of the Guarantees.
94. Mr Swan rejected all these propositions. As regards the Guarantees he submitted that to apply the Principle at all there must be an underlying cross-claim by FL Holdings against FL Ireland giving rise to the liability of FL Ireland which is to be taken into account by the liquidators of FL Holdings. For FL Holdings to rely on such a cross-claim without the consent of the guaranteed creditors is one of the steps prohibited by the Guarantees.
95. Mr Swan distinguished *SSSL*, submitting that Mr Wessels’ arguments were mistaken, since the analogy drawn between G plc and S Ltd on the one hand and FL Ireland and FL Holdings on the other was incorrect. Mr Swan submitted that whereas G plc was a debtor, FL Ireland is a creditor and the roles are reversed (see paragraph 82 of Mr Swan’s skeleton). I should

state here that in my judgment this point of Mr Swan is not well founded. True it is that FL Ireland is an agreed creditor for nearly US\$6 million, but the reality and substance is that FL Ireland is a large debtor to FL Holdings in a total of about US\$214 million.

96. In relation to the FL Guernsey Agreement Mr Swan stressed that the claims provided for are “Agreed Claims”. He submitted that the “concept of Agreed Claims appears to have been intended, in short, as a substitute for the proof of debt process” and that, subject only to the effect of the two provisos in Clause 8.2, the amount of an Agreed Claim was intended to represent the net balance as between FL Holdings and the Creditor (or debtor). The evidence of Mr Hamish Anderson (which both sides accepted as admissible and relevant) is that clause 8.2 with the two provisos was drafted by him to keep open the question whether FL Ireland should be paid dividends on its Agreed Claim against FL Holdings, which question could not be settled in the pre-Agreement discussions. Mr Swan submitted that the second proviso has the effect that FL Holdings can rely on FL Ireland’s liability to FL Holdings only if FL Holdings is entitled to set off such liability under Guernsey law. In my judgment this is not the correct interpretation of the second proviso, because the application of the Principle does not involve a set-off, and the second proviso simply does not relate to the application of this Principle.
97. In my judgment the answer to this issue turns on the fact that neither the wording of the Guarantees nor the wording of the FL Guernsey Agreement deal at all with the process of ascertainment of the fund, the assets, of FL Holdings, which involves (inter alia) application of the *Cherry v Boulton* Principle. FL Holdings is not seeking to rely on that Principle to the detriment of the guaranteed creditors, or to “exercise ..... its rights of subrogation, contribution and indemnity” thereby infringing the terms of the Guarantees. What FL Holdings is seeking to do is to ascertain the true amount of the fund which should be available in its liquidation, so as to be able to determine what dividends are to be available for payment to its creditors, including those such as FL Ireland which have Agreed Claims under the FL Guernsey Agreement. That Agreement does not bar application of the Principle. FL Ireland has its Agreed Claim of nearly US\$6 million, but that claim is outweighed by its liability in so far as that liability has to be brought into account for the ascertainment of the size of the fund of FL Holdings. On this ground (which accords with the approach of the Court of Appeal in *SSSL*), I answer the fifth issue by deciding that application of the Principle is not precluded by the terms of the Guarantees or the FL Guernsey Agreement.

### **My conclusions**

98. Mr Wessels has urged what in the course of the oral submissions I described as “a jury point”. His point is that it would be an affront to commonsense and to a sense of justice that FL Ireland should be enabled to collect dividends from FL Holdings on its Agreed Claim of nearly US\$6 million, when FL Ireland is liable to FL Holdings for over US\$214 million, and FL Holdings has paid to FL Ireland’s creditors under the Guarantees dividends of nearly US\$35 million. I agree with Mr Wessels that it would be such an affront. But that is not the basis on which this Court is required to determine the application by FL Holdings. That depends on Guernsey law principles, and the effect of applying those principles to the facts of this case.
99. For the reasons which I have tried to set out reasonably fully above, I allow the application for an order that no dividends be paid in the liquidation of FL Holdings in respect of FL Ireland’s Agreed Claim.
100. The precise terms of the Court’s order can be decided when this judgment is formally handed down.

101. I hope that in this judgment I have dealt adequately with the main submissions on each side. Though I have not mentioned all the submissions of Mr Wessels or Mr Swan, I have tried to take all of them into account in reaching this decision.

### **Files for the Royal Court**

102. In *Pirito v Curth* (above) when delivering the judgment of the Court of Appeal, I made some practical suggestions in paragraph 41 as to the way in which files of documents should be presented to the Court of Appeal. For the Royal Court, Practice Direction No.1 of 2008, particularly paragraph 7.2.4, sets out how documents are to be presented to the Court. I offer only these suggestions as to how the file or files are prepared:-

- (a) File A needs to be complete, so that the Judge has a full picture of the way in fact the matter has developed, including copies of judgments as well as the other documents mentioned;
- (b) In file C, duplication of exhibits should be avoided by inserting, not a second copy of the same document, but rather a single sheet indicating the nature of the document and where it is to be found in the file;
- (c) In file E, duplication needs to be avoided; and in each separate section it is best to put the authorities in chronological order;
- (d) In file F, as for file C (above).

103. The defendant/respondent should avoid duplication, and can instead insert further authorities and other documents in files A – F. In the present matter, the Court has, as already stated been much assisted by Advocates Wessels and Swan.