

Clawback Case Study

INTRODUCTION

The following facts about the Winning Fund and the three redemption scenarios will form the basis for an interactive discussion in the latter part of the clawback claims session on 12 May 2016.

While the applicable legal principles will be covered in the course of the presentations given earlier in the session, those wishing to go beyond familiarising themselves with the case study may also wish to enjoy the following (in some cases rather lengthy) authorities:

- Chief Justice Smellie (17.xi.2014) and the Court of Appeal (20.xi.2015) in *DD Growth Premium 2x Fund*;
- Mr Justice Andrew Jones in *Primeo* (12.vi.2015);
- Mr Justice Clifford in *Weaving* (4.xii.2015).

Each is available on the unreported judgments section of www.judicial.ky. Pdf copies can also be emailed upon request to mmorrison@serlecourt.co.uk.

THE WINNING FUND

The “Winning Fund” is a Cayman Islands exempted limited liability company that operated as an open-ended investment fund.

The Winning Fund was established by Mr Ronald Bump. While Mr Bump declined to hold any form of office in the fund, he was the sole director and shareholder of Bump Financial Services LCC (“Bump FS”) which served as the fund’s investment adviser.

Under the articles of association, investors in the Winning Fund were entitled to redeem their shares on the first day of any calendar month so long as at least 30 days notice in writing had been provided. Upon the redemption date investors became entitled to payment for their shares based on the NAV of the Winning Fund. Determinations of the NAV made by or on behalf of the directors “*in good faith and absent any manifest error*” were said to be binding on all parties concerned.

Directorial services were provided to the Winning Fund by two employees of Sineit & Ope, a corporate services provider. The directors at all times acted on the instructions of Bump FS. Calculation of the NAV was also delegated to Bump FS and not independently verified by the directors.

For a significant number of years prior to 15 December 2015 stellar results were reported for the Winning Fund. This was largely said to have resulted from an extremely high coupon on US\$500m of Bump Bigly Bonds which had been financed with investors’ monies to fund large-scale building projects on the Mexican border. As a result the NAV of the Winning Fund had consistently been calculated as in excess of \$100m.

On 16 December 2015 it was reported that Mr Bump had been arrested on suspicion of fraud. The directors immediately suspended all further redemptions and calculations of NAV. The subsequent investigation revealed that there had been no building work on the Mexican border, and that the Bump Bigly Bonds were wholly fictitious. It was also revealed that all payments that had been made by the Winning Fund to investors, including in respect of redemptions, were from subscription monies.

DISCUSSION SCENARIOS

Investor 1

Investor 1 made a valid request to redeem all of her shares in the Winning Fund prior to the 1 November 2015 redemption date. On 15 November 2015 she received a redemption payment of \$4m based upon a NAV struck as at 1 November 2015. The liquidators approach you to ask whether anything can be done to recover this payment in light of the subsequent revelations that the NAV was wholly fictitious and the Winning Fund in effect operated as a Ponzi scheme.

Investor 2

Investor 2 was an investment manager which held shares in the Winning Fund as a nominee for a client. Investor 2's client elected to redeem half of the shares held on his behalf by serving a valid notice to redeem for the 1 December 2015 redemption date. On the basis of the NAV struck as at that date, investor 2's client became entitled to receive US\$4 million of redemption proceeds.

Investor 2's client had previously invested in a number of other Bump ventures from which he had made a substantial fortune. The client had also come to develop a close relationship with "the Ronald" himself. On 2 December 2015 Mr Bump contacted investor 2's client and told him that he could double his \$4m within a year if he were to invest it in a new Bump venture. Investor 2's client immediately said that he wanted to invest.

Mr Bump emailed the directors of the Winning Fund and instructed them to make investor 2's redemption payment immediately without further explanation. Investor 2 received the \$4m in full on 5 December 2015 and immediately paid it on to its client. The client invested in Mr Bump's new venture and lost the whole of his investment as a result of the events following Mr Bump's arrest on 16 December 2015.

The liquidator of the Winning fund has approached you to inquire as to whether anything can be done to recover these monies from investor 2 or otherwise make good this loss, and what defences investor 2 might be able to raise to any such claim.

Investor 3

Investor 3 served a valid notice to redeem for the 1 December 2015 redemption date and thereon became entitled to payment of redemption proceeds of US\$8 million on the basis of the NAV struck as at that date.

On 2 December 2015 investor 3 contacted the directors asking for immediate payment of this amount. Having received no response by 5 December 2015, investor 3 sent an email to the directors in which he informed them that he had visited the purported building sites in Mexico and found a complete absence of activity. Investor 3 further informed the directors that he had for some time been requesting sight of the Bump Bigly Bond documentation from Bump FS and had received increasingly spurious excuses for their failure to provide this information. Investor 3 told the directors that if he was not paid immediately he would go public with his suspicions that the Winning Fund was a Ponzi scheme.

Fearing that disclosure of this information would cause the immediate collapse of the fund, and wanting time to investigate and safeguard their own position, the directors caused investor 3 to be repaid in full on 8 December 2015.

The liquidator of the Winning fund has approached you to inquire as to whether anything can be done to recover the \$8 million from investor 3 or otherwise make good this loss, and what defences investor 3 might be able to raise to any such claim.