

Consideration of Enforceability of Side Letters - Lansdowne Limited & Silex Trust Company Limited v. Matador Investments Limited (In Liquidation) & Ors

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The recent judgment on side letters from the Cayman Islands Grand Court in *Re Medley Opportunity Fund Ltd* (21 June 2012) confirmed that there is a clear distinction between beneficial shareholders and investors of record, for enforcing side letters for investments in Cayman Island domiciled hedge funds. The ambiguity surrounding side letters has been further explored in the more recent Grand Court judgment in *Lansdowne Limited & Silex Trust Company Limited v. Matador Investments Limited (In Liquidation) & Ors* (23 August 2012).

The Matador Decision

It was alleged that, prior to X incorporating the Cayman Islands domiciled fund, Matador Investments Limited (the "Fund"), it had been verbally agreed between X and Y, a beneficial owner of a proposed investor in the Fund, that the gating and suspension provisions of the Articles of Association of the Fund would not apply to Z, the registered owner representing Y's investment in the Fund. Y claimed that this was a verbal 'side letter' with the Fund.

The Fund went into liquidation and Y argued that the side letter was enforceable against the Fund and as a consequence, the liquidator. The Grand Court enforced the privity of contract rule, stating that it was paramount that each signatory and entity be a party to the side letter agreement and clearly in this instance X and Y had the said oral agreement, not Z and the Fund.

The Grand Court also noted that the Articles bound all the registered shareholders and did not contain a provision permitting the Fund to enter into side letters varying the provisions of the Articles in relation to particular investors of record. Therefore the gating and suspension provisions would have applied to Z even if the side letter had been entered into by Z and the Fund. It was stressed that side letters are only valid where the Articles allow for flexibility to enter into such agreements.

The Court further indicated that the manner in which shares are redeemed must be clearly specified in the Articles, and even where terms of a side letter are negotiated, the binding effect may be superseded by

subsequent amendments to the constitutional documents applicable to all investors.

The judgment is a reminder to Funds and investors that in entering into side letters care must be taken to ensure that this is permissible under the Articles of Association, and that if it is permissible both the Fund and the registered shareholder must be parties to the side letter.

This advisory should not be construed as providing specific legal advice. It is intended only as a general guide to clients or prospective clients. We recommend that, in connection with any particular transaction or circumstance, specific legal advice be obtained.

Should you have any queries regarding the above, or if we can be of any assistance, please do not hesitate to contact your usual Campbells contact or any of the following:



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