APPENDIX G

BELMONT CUSTOMIZED DYNAMIC GROWTH SPC

ESTIMATED NET ASSET VALUE STATEMENTS

PERIOD JANUARY 1 THRU JULY 31, 2012

(In USD)

STATEMENT OF ASSETS AND LIABILITIES ** ASSETS **	July 31, 2012 Unaudited		June 30, 2012 Unaudited	
Investments, at value:	*cost*	*market value*	*cost*	*market value*
Equities	-	-	-	-
Fund investments	7,949,322	1,662,732	7,949,322	1,673,350
Bonds	-	-	-	-
Discount papers	-	-	-	-
Options	-	-	-	-
	7,949,322	1,662,732	7,949,322	1,673,350
Unrealized gain on financial instruments:				
Contracts for differences	-		-	
Forward contracts	-		-	
Futures contracts	-		-	
		-		-
Cash and cash equivalents:				
Cash at banks	-		-	
Deposits	-		-	
		-		-
Repurchase agreements		-		-
Short term loans		-		-
Due from brokers:				
Balances according to statements	5,442,838		5,447,205	
Receivable gains on forward contracts, expiring after reporting date	-		-	
		5,442,838		5,447,205
Receivable for investments sold		-		-
Prepaid subscriptions		-		-
Accrued interest on bonds		-		-
Overdue coupon interest receivable		-		-
Interest paid in advance on bonds purchased		-		-
Accrued interest on repurchase agreements		-		-
Interest receivable on bank, broker and other balances		-		-
Dividends receivable on shares		-		-
Other receivables and prepaid expenses		-		-
Receivable from Belmont ABL		827,985		827,985
Organizational expenses	-		-	
less: Cumulative amortization	-		-	
Deferred organizational expenses		-		-
Receivable for fund shares sold		-		-
Redemptions paid in advance		-		-
Total Assets		**7,933,554**		**7,948,540**

BELMONT CUSTOMIZED DYNAMIC GROWTH SPC

ESTIMATED NET ASSET VALUE STATEMENTS

PERIOD JANUARY 1 THRU JULY 31, 2012

(In USD)

STATEMENT OF ASSETS AND LIABILITIES ** LIABILITIES **	July 31, 2012 Unaudited		June 30, 2012 Unaudited	
Investments sold short, at value:	*proceeds*	*market value*	proceeds	market value
Equities	-	-	-	-
Bonds	-	-	-	-
Discount papers	-	-	-	-
Options	-	-	-	-
	-	-	-	-
Unrealized loss on financial instruments:				
Contracts for differences	-		-	
Forward contracts	-		-	
Futures contracts	-		-	
		-		-
Due to brokers:				
Balances according to statements	-		-	
Payable losses on forward contracts, expiring after reporting date	-		-	
		-		-
Reverse repurchase agreements		-		-
Short term loans		-		-
Payable for investments purchased		-		-
Redemptions received in advance		-		-
Accrued interest on bonds		-		-
Overdue coupon interest payable		-		-
Interest received in advance on bonds sold		-		-
Accrued interest on reverse repurchase agreements		-		-
Interest payable on bank, broker and other balances		-		-
Dividends payable on shares sold short		-		-
Distribution payable				
Other payables and accrued expenses:				
Management fees	2,829		2,837	
Performance fees	-		-	
Administrative services	1,250		1,250	
Audit fees	8,316		7,751	
Director fees	18		167	
Fund Serv fees	-		-	
Custody fees	242		184	
Cayman fees	168		144	
Distribution fee	3,094		2,980	
		15,917		15,313
Overpayment of redemption FI RX 11/08		-		-
Payable for fund shares repurchased		2,262,900		2,262,900
Total Liabilities		2,278,817		2,278,213
NET ASSETS		**5,654,738**		**5,670,328**
Number of shares outstanding Class A:		187,142.5472		187,142.5472
Net Asset Value per share Class A: * **184002** Claris **13-016169**	-0.27%	$ **29.4856**	-1.86%	$ **29.5663**
*Estimate				
Number of shares outstanding Class B:		5,478.7870		5,478.7870
Net Asset Value per share Class B:* **184102** Claris **13-016168**	-0.36%	$ **24.9563**	-1.95%	$ **25.0455**
*Estimate				

BELMONT CUSTOMIZED DYNAMIC GROWTH SPC

ESTIMATED NET ASSET VALUE STATEMENTS

PERIOD JANUARY 1 THRU JULY 31, 2012

(In USD)

STATEMENT OF OPERATIONS	January 1 thru July 31, 2012 Unaudited		January 1 thru June 30, 2012 Unaudited	
Investment Income				
Income:				
Interest: · Bonds	-		-	
· Discount papers	-		-	
· Repurchase agreements	-		-	
· Loans	-		-	
· Bank and broker balances	2,655		2,655	
		2,655		2,655
Dividends (gross income)	-		-	
less: Withholding tax	-		-	
		-		-
Other income		-		-
Total income		2,655		2,655
Expenses:				
Interest: · Bonds	-		-	
· Discount papers	-		-	
· Reverse repurchase agreements	-		-	
· Loans	-		-	
· Bank and broker balances	-		-	
Dividends on short sales	-		-	
Management fees	20,565		17,736	
Performance fees	-		-	
Administrative services	8,876		7,626	
Audit fees	46,341		45,872	
Director fees	193		167	
Legal fees	133,926		133,926	
Custody fees	549		492	
Bank and broker expenses	1,594		1,488	
Amortized organizational expenses	168		144	
General and other expenses	832		718	
Total expenses		213,044		208,169
Net investment income (loss)		(210,389)		(205,514)
Realized and unrealized gains (losses) on investments				
Realized gains (losses) on investments in:				
Securities		(254,437)		(254,437)
Options		-		-
Contracts for differences		-		-
Futures contracts		-		-
Forward contracts		-		-
Foreign currency exchange		315		629
		(254,122)		(253,808)
Unrealized appreciation (depreciation) on investments in:	Beginning of year	End of period	Beginning of year	End of period
Securities	(5,923,220)	(6,286,590)	(5,923,220)	(6,275,971)
Options	-	-	-	-
Contracts for differences	-	-	-	-
Futures contracts	-	-	-	-
Forward contracts	-	-	-	-
	(5,923,220)	(6,286,590)	(5,923,220)	(6,275,971)
Increase (decrease) unrealized appreciation on investments		(363,370)		(352,751)
Unrealized gains (losses) on foreign currency exchange:				
Beginning of year (1-1-2012)	1,023		1,023	
End of period	365		147	
		(658)		(876)
Net realized and unrealized gains (losses) on investments		(618,150)		(607,435)
Net increase (decrease) in net assets resulting from operations		**-828,539**		**-812,949**

BELMONT CUSTOMIZED DYNAMIC GROWTH SPC

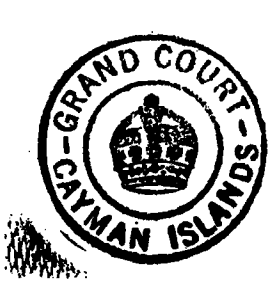
ESTIMATED NET ASSET VALUE STATEMENTS

PERIOD JANUARY 1 THRU JULY 31, 2012

(In USD)

STATEMENT OF CHANGES IN NET ASSETS	January 1 thru July 31, 2012 Unaudited		January 1 thru June 30, 2012 Unaudited	
Increase (decrease) in net assets from operations:				
Net investment income (loss)		(210,389)		(205,514)
Net realized gains (losses) on investments		(254,122)		(253,808)
Increase (decrease) unrealized appreciation on investments		(363,370)		(352,751)
Net unrealized gains (losses) on foreign currency exchange		(658)		(876)
Net increase (decrease) in net assets resulting from operations		(828,539)		(812,949)
Distribution to Stockholders		-		-
From capital stock transactions:				
Proceeds from sales of shares	-		-	
Cost of repurchases of shares	-		-	
Increase (decrease) in net assets resulting from capital stock transactions		-		-
Net increase (decrease) in net assets		(828,539)		(812,949)
Net Assets:				
Beginning of year (1-1-2012)		6,483,277		6,483,277
End of period		**5,654,738**		5,670,328

APPENDIX H



IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

Cause No. FSD 15 of 2009 (AJJ)

In Open Court
11 July 2012
Before the Honourable Justice Andrew J Jones QC

IN THE MATTER OF SECTION 92 OF THE COMPANIES LAW (2011 REVISION)

AND IN THE MATTER OF BELMONT ASSET BASED LENDING LTD (IN OFFICIAL LIQUIDATION)

BETWEEN:

J.P. MORGAN MARKETS LIMITED
(formerly known as Bear, Sterns International Limited)
Applicant

and

FINTER BANK ZURICH LTD
Representative Respondent

ORDER FOR DIRECTIONS

UPON HEARING leading counsel for the Applicant and counsel for the Representative Respondent upon the Joint Official Liquidators' summons dated 5 August 2011 (as amended by the order made on 11 July 2012) by which they sought a direction that the Applicant's Proof of Debt dated 7 March 2012 should be admitted to proof

AND UPON READING the agreed statement of facts and the Third Affidavit of Stuart Sybersma sworn on 14 October 2011 on behalf of the Joint Official Liquidators

IT IS ORDERED AND DIRECTED that the Applicant's Proof of Debt shall be rejected.

AND IT IS FURTHER DIRECTED that the question whether the Joint Official Liquidators' costs of attending and being represented at the hearing of summons shall be paid out of the assets of the company as an expense of the liquidation shall be adjourned to be heard on 7 August 2012.

DATED the 13th day of July 2012

FILED the 16th day of July 2012

The Honourable Mr Justice Andrew J. Jones QC
JUDGE OF THE GRAND COURT

GRAND COURT - CAYMAN ISLANDS

IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

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BETWEEN:

J.P. MORGAN MARKETS LIMITED
(formerly known as Bear, Stearns International Limited)
Applicant

and

FINTER BANK ZURICH LTD
Representative Respondent

Appearances:

Mr. Richard Handyside QC instructed by Mr. Andrew Bolton of Appleby (Cayman) Ltd on behalf of J.P Morgan Markets Limited

Mr. Fraser Hughes of Conyers Dill & Pearman on behalf of Finter Bank Zurich Ltd as representative respondent on behalf of the participating shareholders of the Fund

Mr. Simon Dickson of Mourant Ozannes on behalf of the Joint Official Liquidators of the Fund

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REASONS

FOR ORDER FOR DIRECTIONS

Introduction

1 On 5 August 2011, the Joint Official Liquidators ("the JOLs") of Belmont Asset Based Lending Limited ("the Fund") issued a summons seeking directions that they may admit to proof a claim of Bear Steams Alternative Assets International Limited

("BSAAIL") in the amount of US$59,947,747.00 plus interest in respect of the Strike under an option agreement entered into between J.P. Morgan Markets Limited (formerly known as Bear, Stearns International Limited) ("BSIL") and the Fund dated 27 April 2007 ("the Option Agreement"). On 24 November 2011 I directed that the summons be treated as an application by BSAAIL, as applicant, against Finter Bank Zurich Ltd ("Finter"), as representative respondent to determine whether, upon the true construction of the Option Agreement, BSAAIL is a creditor for that amount. [1]

2. At the time the JOLs' summons was issued, neither BSIL nor its affiliate BSAAIL had actually submitted any proof of debt. However, the JOLs had taken legal advice from specialist London counsel, Mr. Iain Milligan QC, as to the interpretation of the Option Agreement. In his written opinion, which has since been disclosed to the parties,[2] Mr. Milligan advised, on the assumption that Cayman Islands law is the same as English law in the relevant respects, that the Fund was obliged to treat Bear Stearns as a creditor.

3. BSIL has now submitted a proof of debt dated 7 March 2012 by which it claims the sum of US$61,208,180.21, being the amount of the Strike allegedly due and owing under the terms of the Option Agreement as at that date. It was agreed that I should make an order for substitution to reflect that the claimant is BSIL (rather than BSAAIL) and that the claim is for US$61,208,180.21 (rather than USD$59,947,747.00), thus bringing the application into line with the proof of debt. It follows that the issue to be decided is whether, upon a true construction of the Option Agreement, BSIL is a creditor for the amount of its proof of debt. Having determined this issue, I shall direct the JOLs to admit or reject the proof of debt as the case may be. These amendments have no bearing upon the substance of the matter in issue which is a pure point of law to be determined upon the basis of an Agreed Statement of Facts filed with the Court on 16 January 2012 (and agreed on 13 February 2012).

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[1] Written reasons for making this order and dismissing the JOLs application for leave to appeal were delivered on 19 December 2011.

[2] Mr. Milligan's opinion was originally disclosed by the JOLs in redacted form on 23 November 2011. An un-redacted, updated version of the opinion was disclosed by them on 1 March 2012.

The Fund

4. The Fund was incorporated and registered under the Companies Law as an exempted company on 24 October 2003. It carried on business as an open ended investment fund and was registered with the Cayman Islands Monetary Authority pursuant to section 4(3)(c) of the Mutual Funds Law. Upon its incorporation the Fund's authorised share capital was the aggregate of US$29,000 and €20,000 comprising 100 Voting Shares of US$100 each (held by the Fund's management) and four classes of Redeemable Non-Voting Participating Shares. The Class A and Class B shares are denominated in US dollars and the Class C and Class D shares are denominated in Euros. At this stage the only other distinction between the classes is that no management and performance fees were charged to the Class A shares which could only be issued to funds of hedge funds under the same management as the Fund.[3]

5. The Fund was established as a fund of hedge funds. The investment objective described in the Confidential Information Memorandum dated 10 July 2006[4] (at page 13) was as follows –

> "The investment objective of the [Fund] in each of its Classes is to maximise long-term returns to shareholders by investing in a diversified portfolio of fixed income related hedge fund strategies. The [Fund] will allocate its assets to various Fund Managers employing various fixed income strategies, including relative value hedge fund strategies such as fixed income arbitrage, mortgage-backed securities arbitrage and capital structure arbitrage, as well as directional hedge fund strategies such as distressed securities, long/short high yield, and emerging markets debt."

The use of leverage, both for liquidity purposes and investment purposes, was described in the following way

> "The [Fund] may use leverage in each of its Classes to meet redemptions or to enhance investments, but such leverage shall be subject to a maximum of one hundred and fifty per cent (150%) of the aggregate net asset value of the [Fund]."

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[3] The Fund was promoted by Harcourt Investment Consulting AG which is part of the Vontobel Banking Group, headquartered in Zurich, Switzerland. Harcourt group companies acted as investment manager and investment adviser to the Fund.

[4] The original version of the Confidential Offering Document which must have been filed with the Cayman Islands Monetary Authority when the Fund was launched in 2003 has not been put in evidence.

It went on to say that the Fund might establish a credit facility for any of its Classes of Participating Shares, the maximum of which would depend upon the liquidity of the investments of each Class. I was told that the Fund's assets (which comprised shares in other hedge funds) were in fact treated as a single portfolio and not allocated in any way to particular share classes. The risk factor associated with the use of leverage was described (at pages 19- 20) as follows –

> "The [Fund] may, in the sole discretion of the Investment Manager, leverage its investment positions by borrowing funds, which will typically be secured by the [Fund's] securities and other assets, from securities broker-dealers, banks or others. Such leverage will be subject to a maximum of one hundred and fifty per cent (150%) of the aggregate net asset value of the Fund."
>
> "Borrowing money to purchase securities may provide the Investment Manager with the opportunity for greater capital appreciation but, at the same time, will increase the [Fund's] exposure to capital risk and higher current expenses. Moreover, if assets under management are not sufficient to pay the principal of, and interest on, the debt when due, the [Fund] could sustain a total loss of its investment."

Finally (at page 23), it stated that –

> "If losses or liabilities are sustained by a Class of Shares in excess of the assets attributable to such class, such excess may be apportioned to the other Class of Shares. It is not possible to isolate or protect the assets attributable to one Class of Shares from the liabilities attributable to the other Class of Shares are insufficient to satisfy the liabilities attributable to such Class of Shares. While efforts will be made to contract with parties on a "limited recourse" basis, there is no guarantee that the Company will be able to attain such result."

Whether or not the Fund actually employed leverage at this point in its trading history is not addressed in the evidence.

Introduction of leveraged share classes and the execution of the Option Agreement

6. In April 2007 the Fund's memorandum and articles of association were amended to provide for the issue of leveraged and non-leveraged classes of Participating Shares (or leveraged classes with different levels of leverage).[5] Four additional classes of Participating shares were created and described as Class A+, Class B+, Class C+ and Class D+. Thus, an investor wishing to make a Euro denominated investment could

[5] I use the expression "leveraged shares" or "leveraged share classes" to mean those having a leveraged exposure to the Fund's investment performance and "unleveraged shares" or "unleveraged share classes" to me those which did not. The leveraged share classes are identified by the suffix "+".

choose between an unleveraged exposure to the Fund's investment performance by subscribing for Class B shares or a leveraged exposure by subscribing for the Class B+ shares. In addition, the amendment provided for the creation of a new class of participating shares, the Class F Shares, which could be issued only to a credit provider. For reasons which will become apparent when I describe the terms of the Option Agreement, it is reasonable to infer that the creation of the Class F shares must have been done with the Option Agreement specifically in mind. Thereafter, this structure remained unchanged. Nothing turns on the fact that the aggregate amount of the authorised share capital and the number of classes of participating shares was increased on two subsequent occasions. Henceforth, I use the expression "Memorandum and Articles of Association" to mean the Fund's memorandum and articles of association as amended and re-stated on 19 April 2007. It is this version of the document which forms part of the factual matrix relevant to the construction of the Option Agreement.

7. At the same time as amending the Memorandum and Articles of Association, the Fund's directors re-wrote its offering document. Henceforth, I use the expression "Confidential Information Memorandum" to mean the version dated April 2007. Three subsequent versions were issued but it is the April 2007 version which is relevant for present purposes. The description of the way in which the Fund will employ leverage and provide some, but not all, of its investors with a leveraged exposure to its performance was changed and re-stated in Section 3 of the Confidential Information Memorandum as follows :-

> "The Fund may use leverage in each of its Share Classes to meet redemptions, to bridge-finance new investments for FX margin purposes, or to enhance investments. Such leverage shall be subject to a maximum of 50% of the aggregate Net Asset Value of the relevant Share Classes (or 1.5 times leverage) in the case of Classes A, B, BB, C, CC, D, DD and F and 150% of the aggregate Net Asset Value of the relevant Share Classes (or 2.5 times leverage) in the case of Classes A+, B+, C+, D+. Notwithstanding the foregoing, the Investment Manager anticipates that leverage for Classes A+, B+, C+, D+ will, on average, be around 100% of the aggregate Net Asset Value of those Share Classes (or 2 times leverage). The Fund may establish a credit facility or a derivative structure to provide leverage for any of its Classes of Participating Shares. The maximum leverage depends on the liquidity of the investments of each Class of Participating Shares. The Fund will be able to borrow, repay and re-borrow amounts under the leverage facility. Such leverage facility may be utilised to enable the Fund to establish the desired investment exposure and/or to cover the margin requirements for a currency hedge."

8. This statement means that the Fund will employ leverage for both liquidity purposes (financing redemptions, bridge-financing new investments and financing foreign exchange transactions) and investment purposes (which is what is meant by the expression "to enhance investments"). For the purposes of this application, I am concerned only with the way in which it employed leverage for investment purposes. This statement reflects that the directors intended to issue two categories of shares, one with a maximum of 1.5x leverage and one with a maximum of 2.5x leverage. I was told that in fact the Class A, B, BB, C, CC, D, DD shares were unleveraged and the Class A+, B+, C+, D+ shares were leveraged 2x.[6] For present purposes, the relevant point is that the Fund intended to issue two categories of shares having the benefit/burden of differential levels of leverage. Whether it was "unleveraged and leveraged 2x" or "leveraged 1.5x and leveraged 2.5x" makes no difference to the relevant factual background.

9. Section 14 of the Confidential Information Memorandum further describes the risks associated with employing leverage for investment purposes as follows :-

> **"14.3 Risk of Leverage**
> The Risk of leverage needs to be considered at the portfolio level, the class level and within the investment vehicles that the Fund invests into.
>
> Portfolio Level
> The Fund may, at the sole discretion of the Investment Manager, leverage its investment positions by borrowing funds, which will typically be secured by the Fund's securities and other assets, from securities broker-dealers, banks or others. Borrowing money to purchase securities may provide the Investment Manager with the opportunity for greater capital appreciation but, at the same time, will increase the Fund's exposure to capital risk and higher current expenses. Moreover, if the assets under management are not sufficient to pay the principal of, and interest on, the debt when due, the Fund could sustain a total loss of its investment. As such, the Fund's exposure to capital risk is enhanced.
>
> Class Level
> Each Share Class may employ different levels of leverage as described under "Investment Objective" above. The Directors will attempt to ensure that a Shareholder's interest will be

[6] For the sake of completeness, I point out that additional leveraged share classes were created later, after the execution of the Option Agreement, but this fact has no bearing upon the issue to be decided in this application. By the commencement of the liquidation there were 19 classes of participating shares open to investors, namely unleveraged Classes A, B, BB, C, CC, D, and DD and leveraged Classes A+, B+, C+, D+, B2+, C2+, D2+, BB+, CC+, D3+ and B2+ Dividend. The only other share classes were the voting shares registered in the name of the Investment Manager and the Class F shares registered in the name of BSAAIL, presumably as custodian for BSIL.

> limited to the assets and liabilities represented by the Share Class in which he invests. Investors should, however, be aware that in an event a claim is made against the Fund, if the assets attributable to a Share Class in respect of which the claim is made are insufficient to cover such claim, then the creditor may have recourse to the assets attributable to other Share Classes. As at the date of this Information Memorandum, the Directors are not aware of any such existing or contingent liabilities. Your attention is drawn to "Cross Class Liability" below.

10. The distinction between "portfolio level leverage" and "class level leverage" was not made in the previous version of the offering document and clearly reflects the decision made in April 2007 to issue classes of shares which will have the benefit/risk of leverage (or higher leverage) and classes which will not. With effect from the 1 May 2007 Subscription Day new investors could choose between investing in shares offering an unleveraged exposure or shares offering a leveraged exposure to the Fund's performance. The latter share classes are identified by the suffix " + ". The Offering Document contemplates a maximum leverage target level of 2.5x, but the actual target level was 2x because that was the target provided for under the terms of Appendix B of the Option Agreement. Existing shareholders were given the option of "switching" their investments into one of the new share classes offering a leveraged exposure, as described in Section 8 of the Confidential Information Memorandum.

11. It is implicit in this arrangement that *only* those who subscribe for the leveraged share classes should have the advantage of potentially enhanced returns and bear the corresponding risk of potentially greater losses. I agree with counsel for Finter that this arrangement would not make commercial sense if those opting for the unleveraged shares are exposed to the risk of leverage, but have none of the benefit. This point is addressed in those parts Confidential Information Memorandum (quoted above) which discuss the distinction between portfolio level leverage and class level leverage. It states that "The Directors will attempt to ensure that a Shareholder's interest will be limited to the assets and liabilities represented by the Share Class in which he invests". However, the Fund was not incorporated as a segregated portfolio company under the provisions of Part XIV of the Companies Law and so this result could be achieved only by contracting with its credit provider on terms that its recourse would be limited to the assets attributable to the Share Class for whose benefit the credit has been obtained. The risk of not achieving this result is described in Section 14.5 of the Confidential Information Memorandum in the following way:

> "Cross Class Liability
> The Fund has twelve Share Classes and further classes of shares may be created in the future. However, the Fund is a single legal entity and all of the assets of the Fund may be available to meet the Fund's liabilities, regardless of the separate portfolio to which such assets or liabilities are attributable. In practice, cross class liability will usually only arise where the Class becomes insolvent or exhausts its assets and is unable to meet all of its liabilities. In this case, all of the assets of the Fund attributable to the other Classes may be applied to cover the liabilities of the insolvent Class. As at the date of this Information Memorandum, the Directors are not aware of any such existing or contingent liability."

Clearly, the Fund's directors would not have contracted with a credit provider with the intention of preferring the leveraged shareholders at the (potential) expense of the unleveraged shareholders, but as counsel for BSIL rightly pointed out, the subjective intention of the directors is irrelevant to the issue I have to decide.

The Option Agreement

12. It is against this factual background that the Option Agreement was executed on 27 April 2007. Commercially, this whole arrangement took effect as of 1 May 2007, being the next Subscription Day upon which new investors could subscribe for leveraged shares and existing investors could switch into leveraged shares. Before turning to the actual terms of the Option agreement, it will be helpful to illustrate, by reference to a simple hypothetical example, how the provision and application of leverage worked. Assume that, at inception, two investors decide to invest $1m each. Investor #1 subscribes $1m in consideration for the issue of 10,000 unleveraged Class B shares at a price/NAV of $100 per share. Investor #2 subscribes $1m for 10,000 leveraged Class B+ shares at $100 per share. In consequence of Investor #2's subscription, the Fund then pays $1m to BSIL which in turn subscribes $2m for the issue of 20,000 Class F shares. At that point the Fund has gross assets of $3m; the Fund's NAV is $3m, $1m of which is attributable to the NAV of the unleveraged Class B shares, $2m of which is attributable to the Class F shares, from which the NAV of the Class B+ shares is derived after deducting the value of the Strike ($1m). Assume that, as at the end of the first year, the market value of the Fund's assets has increased by 20% and the value of the Strike has increased by 5% (by reference to US$ LIBOR + 70 basis points), the intended result is as follows. The Fund's NA

deemed to be $3.6m. The calculation is $3m (subscribed capital) + $0.6m (capital appreciation) = $3.6m. Investor #1, who is exposed to the Fund's unleveraged performance, is treated as having an NAV of $120 per share, reflecting a positive return of 20%. The calculation is ($1m + $0.2m) = $1.2m ÷ 10,000 shares = $120 per share. Investor #2, who has the benefit/risk of the Fund's leveraged performance, is treated as having an NAV of $135 per share. The calculation is $2m + $0.4m - $1.05m = $1.35m ÷ 10,000 shares = $135 per share, reflecting a positive return of 35%. In this way the amount of the Strike ($1.05m) is treated as if it was a liability attributable to the Class B+ shares only. Assume that Investor #2 decides to redeem his shareholding at this point. BSIL will redeem its Class F shares which are treated as having an NAV of $2.4m (being $2m subscribed capital plus 20% appreciation). The Fund pays the redemption proceeds of $2.4m to BSIL. Having reduced the value of the Strike to zero (from $1.05m), BSIL then pays the Cash Settlement Amount ($1.35m) to the Fund, which is the amount of the redemption proceeds payable to Investor #2 in respect of 10,000 Class B+ shares at $135 per share. Conversely, if the market value of the underlying assets of the Fund falls by 20% over the period, the result is as follows. The NAV of Investor #1's unleveraged Class B shares is treated as having fallen to $80 per share reflecting a negative return of 20%. The NAV of Investor #2's leveraged Class B+ shares is treated as having fallen to $55 per share, reflecting a negative return of 45%. In this scenario, the redemption proceeds of the Class F shares is $1.6m ($2m capital invested less depreciation of $0.4m). After reducing the value of the Strike to zero, the Cash Settlement Amount is $0.55m. In either scenario, BSIL is able to reduce the value of the Strike to zero by deducting the whole amount from the redemption proceeds of the Class F Shares, thereby earning a return of 5% by reference to LIBOR + 70 basis points. The issue I have to decide is what happens, upon a true construction of the Option Agreement, if the Fund's underlying assets depreciate to such an extent that the redemption proceeds of the Class F Shares is less than the amount of the Strike Finter's case is that nothing should happen. BSIL argues that I should imply a payment obligation which would have the legal effect of turning the Option Agreement into a loan agreement.

13. As counsel for BSIL says, it is apparent from this illustration that BSIL's subscription for Class F shares pursuant to the Option Agreement was the *economic equivalent* of

making a loan to the Fund under a credit facility with an initial loan to value ratio of 50%. However, it seems to me that when an investment bank and a hedge fund enter into a derivate transaction intended to create an economic result equivalent to a loan agreement, it is not open to the Court to re-write the transaction by turning it into an actual loan agreement. Taking this point one step further, Finter's case is that on its true construction the Option Agreement was intended to produce a result which is the economic equivalent of a limited recourse loan facility agreement.

The express terms of the Option Agreement

14. The Option Agreement is contained in a confirmation letter dated 27 April 2007 ("the Confirmation") which is subject to and incorporates the 2000 ISDA Definitions and the 1992 ISDA Master Agreement. The Trade Date of the Option Transaction was 27 April 2007 and BSIL is the Seller and the Fund is the Buyer. It is expressed to be governed by English law and the parties have agreed that the applicable English law is the same as Cayman Islands law. I am indebted to BSIL's counsel for his careful summary of the express terms which I have largely adopted in the following paragraphs.

15. The Option Terms are stated in the Confirmation as follows:-

> "This Transaction is an Option Transaction under Section 10.1(c) of the Definitions; and this means, inter alia, that [BSIL] has granted the [Fund] the right to cause [BSIL] to either (i) pay the Cash Settlement Amount(s), if any, on the Cash Settlement Payment Date(s) or (ii) transfer to the [Fund] the Reference Fund Shares on the Physical Settlement Date against payment of the Strike, in the case of an election of Physical Settlement."

In essence therefore, the Fund was granted an option to bring about the transfer to it of the Reference Fund Shares (meaning the Class F shares), either through redemption of those shares or physical delivery of them. Upon exercise of the Option, the Fund was entitled to receive either a cash payment in the amount (if any) by which the redemption proceeds of the Reference Fund Shares exceeded the Strike, or physical delivery of the Shares.

16. On the Premium Payment Date, namely 27 April 2007, a Premium[7] of US$10,700,000 (the "Initial Premium") was to be paid to BSIL by the Company in the form of US$1,700,000 in cash and Class F Shares to the value of US$9,000,000.

17. The Option Agreement provided that the Premium might be increased from time to time in accordance with an Option Premium Increase through Transfer of Shares. Under this mechanism, the Fund could, on no less than two Business Days' prior written notice, increase the then current Premium by transferring, or procuring the transfer of, Shares of the Reference Fund to BSIL or any of its affiliates prior to such Business Day. The result of such a transfer would be to reduce the Leverage Factor, but not the Strike, under the Option. The Premium could similarly be decreased from time to time under an Option Premium Decrease through Transfer of Shares, by which the Fund could, again on no less than two Business Days' prior written notice, decrease the then Current Premium by having the Seller or any of its affiliates transfer Reference Fund Shares to the Buyer. An Option Premium Increase and an Option Premium Decrease were both subject to BSIL's approval, such approval being subject to (among other things) the composition of the Reference Fund Basket being compliant with the Investment Guidelines set out in Appendix D and, in the case of an Option Premium Decrease, the Leverage Factor following such decrease not being higher than the Maximum Leverage Factor.

18. As of the Commencement Date (27 April 2007), the Strike was a US$ amount equal to US$10,700,000. For any Business Day after the Commencement Date, the Strike was a US$ amount calculated in accordance with Appendix A to the Confirmation. In essence, the Strike on a given Business Day was to be calculated by applying a formula to the Strike on the previous Business Day (called "$Strike_{t-1}$"). The commercial effect of the formula is equivalent to BSIL charging interest on the Strike for the previous Business Day at US$ daily LIBOR plus a margin of 70 basis points. On 30 November 2007, the definition of the Strike was amended so that where the

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[7] "Premium" is defined in Section 11.3(a) of the 2000 ISDA Definitions as meaning, "in respect of an Option Transaction and in respect of a Premium Payment Date, the amount, if any, that is specified as such in the related Confirmation (or determined pursuant to a method specified for such purpose) and, subject to any applicable condition precedent, is payable by Buyer to Seller on the Premium Payment Date or on each Premium Payment Date if more than one is specified."

Strike for the previous Business Day exceeded the Maximum Strike, it would be increased by the application of an additional 65 basis points.

19. The Confirmation provided that the Strike might be adjusted following an Option Deleveraging, a Strike Increase by Payment of Cash to Buyer, a Strike Decrease by Payment of Cash to Seller, or Additions to / Removals from the Reference Fund Basket. In summary, these operated as follows. A Strike Increase by Payment of Cash to Buyer could be effected by serving a Notice on BSIL to increase the Strike, provided that the increase was approved by BSIL. Such approval was subject to (among other things) the resulting Strike not being in excess of the Maximum Strike,[8] and the Leverage Factor[9] following such Strike Increase not being higher than the Maximum Leverage Factor.[10] The definition of Strike Increase by Payment of Cash to Buyer expressly provided that as a consequence of such a Strike Increase, the value of the Option (to the Fund/Buyer) would decrease by the Strike Amount Increase. A Strike Decrease by Payment of Cash to Seller would occur where the Fund/Buyer requested a decrease of the Strike by transferring a specified US$ amount (of not less than US$100,000) to BSIL. The definition of Strike Decrease by Payment of Cash to Seller expressly provided that as a consequence of such Strike Decrease, the value of the Option (to the Fund/Buyer) would increase by the Strike Amount Decrease.

20. Additions to or Removals from the Reference Fund Basket could be effected by BSIL following a written request from the Fund/Buyer specifying the number of shares of the Reference Fund that it wished to add to or remove from the Reference Fund Basket together with the most recent NAV of such Shares. BSIL was then required to confirm to the Fund/Buyer whether such Addition(s) or Removal(s) were approved,

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8 The Maximum Strike was initially US$20m, subject to any increase agreed by the parties. The Maximum Strike was subsequently increased under Amendment Agreements dated as of 30 May 2007, 28 June 2007 and 30 July 2007 to US$30m, US$50m and US$80m respectively. The provision in the definition of Strike Increase by Payment of Cash to Buyer whereby the resulting Strike could not exceed the Maximum Strike was amended by an Amendment Agreement dated as of 30 November 2007 so that the resulting Strike could with BSIL's consent exceed the Maximum Strike.

9 The Leverage Factor was to be calculated in accordance with a formula set out in Appendix B of the Confirmation. It was to be calculated on a given Business Day by taking the value of the Reference Fund Shares and dividing it by the amount by which that value exceeded the Strike on that day. Effectively, it was the commercial equivalent of a loan to value ratio stipulated under a secured credit facility agreement.

10 The Maximum Leverage Factor was 2.2x leverage.

such approval being subject to (a) the composition of the Reference Fund Basket being compliant with the Investment Guidelines set out in Appendix D to the Confirmation, and (b) in the case of Additions only, the resulting Leverage Factor (having taken into consideration any pending adjustment to the Strike[11]) not being higher than the Maximum Leverage Factor and the resulting Strike not being in excess of the Maximum Strike.[12] Removal(s) from the Reference Fund Basket could also be effected where BSIL determined in good faith and in a commercially reasonable manner that such Removal(s) were necessary to comply with the Option Deleveraging provisions set out in Appendix B to the Confirmation and/or to cure any of the Structural Events set out in Appendix C to the Confirmation.[13]

21. Under the Option Deleveraging Provisions, if on any Business Day the Maximum Leverage Factor (2.2x) was exceeded, a Reallocation Event would occur and within 10 Business Days of such occurrence, the Fund/Buyer was required to take one of four identified steps to reduce the Leverage Factor to the Target Leverage Factor (2x). If the Fund/Buyer did not take one of those steps within the 10 day time period, BSIL was entitled to submit redemption notices for Shares in the Reference Fund for an amount equal to the Redemption Amount as of the next possible redemption date, and the Strike would be adjusted effective on the date of receipt of the redemption proceeds in accordance with the definition and formula of $Strike_{t-1}$ contained in Appendix A.

22. The Option was exercisable by the Fund/Buyer during the period commencing on (and including) the Commencement Date (27 April 2007) and ending on (and including) the Expiration Date. The Expiration Date was defined to mean the earlier of (a) the first Exercise Business Day of May 2012 ("the Scheduled Expiration

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[11] Where BSIL or any of its affiliates subscribed for or purchased Reference Fund Shares in connection with an Addition of Reference Fund Shares, the Strike was to be increased by any cash amount paid by BSIL or any of its affiliates for those shares. Conversely, where BSIL or any of its affiliates redeemed or sold any Reference Fund Shares in connection with a Removal from the Reference Fund Basket of Reference Fund Shares, the Strike would be decreased by any cash amount received by BSIL or any of its affiliates on connection with the redemption or sale of such Shares.

[12] This provision was amended by an Amendment Agreement dated as of 30 November 2007 so that the resulting Strike could with BSIL's consent exceed the Maximum Strike.

[13] The Structural Events are defined to include such things as the commencement of a regulatory investigation against the Fund's investment manager; a dissolution or liquidation of the Fund; replacement of the Fund's management without BSIL's consent; and suspending redemptions.

Date"), meaning that the Option Agreement would expire at the end of a 5 year term on 1 May 2012; (b) the Early Expiration Date (if any) designated by BSIL in accordance with Appendix C to the Confirmation; and (c) any anniversary date of the Commencement Date (27 April 2007) notified by BSIL to the Fund/Buyer with no less than 6 calendar months' prior written notice.

23. The occurrence of a Designation Event, as defined in Appendix C to the Confirmation, entitled BSIL to designate an Early Expiration Date. The Designation Events, as determined by BSIL acting in good faith and in a commercially reasonable manner, included (1) the Reference Fund's NAV declining by more than 10% in any given calendar month, and (2) the Reference Fund failing to report its NAV on a monthly basis or delayed its reporting by more than 10 Business Days, both of which actually happened in September 2008.

24. The Option Agreement provided for Cash Settlement unless the Company elected for physical settlement. The Cash Settlement Amount was defined as follows:

> "In respect of a Cash Settlement Payment Date, an amount calculated in respect of the immediately preceding Receipt Date, equal to:
> (i) USD 0, if $Strike_t$ as of such Receipt Date is higher that USD 0; or
> (ii) if $Strike_t$ is equal to 0 as of such Receipt Date, the redemption proceeds received by Seller or any of its affiliates on such Receipt Date.
> For the avoidance of doubt, upon Option Exercise (and subject to "Election for Physical Settlement" below), the full amount of Reference Fund Shares shall be redeemed and corresponding proceeds will go first towards reducing the Strike, before being paid to Seller only when the value of the Strike is equal to zero."

25. "Cash Settlement Payment Dates" were defined as the second Business Day following each of the Receipt Dates, provided that no Cash Settlement Payment Date would occur after the second anniversary date of the Expiration Date "Receipt Dates" were in turn defined as:

> "Each day (or, if such day is not a Business Day, the next following Business Day) on which Seller or any of its affiliates receives redemption proceeds with respect to Reference Fund Shares redeemed in conjunction with the exercise of the Option."

In other words, the Cash Settlement Amount (if any) is payable by BSIL to the [illegible] two business days after receipt of the redemption proceeds of the Class F shar[illegible]

26. The Election for Physical Settlement term in the Confirmation provided that upon exercise or deemed exercise of the Option (other than following the occurrence of a Designation Event as defined in Appendix C), the Fund/Buyer had the right to elect physical settlement by giving irrevocable notice to BSIL. It further provided:

> "If Buyer elects for physical settlement pursuant to the provisions of the preceding paragraph, Seller will, to the extent practicable, transfer to Buyer or to the Buyer's designee the Reference Fund Shares comprising the Reference Fund Basket against payment by Buyer to Seller of the Strike Price on the Physical Settlement Date.
> If, following an election by Buyer for physical settlement, Seller determines (acting in good faith and in a commercially reasonable manner) that it is not practicable to effect physical settlement, then Seller shall notify Buyer as soon as practicable and the Option shall be settled in Cash, notwithstanding the election by Buyer for physical settlement."

I agree with counsel for the parties that the words "against payment by Buyer of the Strike Price" imply a payment obligation. A payment obligation creates a liability on the part of the Fund. These words are to be contrasted with the concept of "reducing the value of the Strike to zero" which is employed in the definition of the Cash Settlement Amount. This concept is employed to produce the same economic result without creating a liability on the part of the Fund.

The termination of the Option Agreement

27. By a notice dated 3 September 2008 BSIL notified the Fund of the Expiration Date in accordance with sub-paragraph (c) of the definition of the Expiration Date, thereby terminating the Option Agreement on its next anniversary date which was 27 April 2009. In fact the notice mistakenly specified 30 April rather than 27 April 2009 as the anniversary date, but nothing turns on this point.

28. On 15 September 2008 Lehman Brothers filed for bankruptcy, thus precipitating a market collapse. On 19 September 2008, BSAAIL submitted a request for redemption of Class F Shares to the value of US$8,800,000 on 30 September 2008 in respect of which the Fund subsequently paid proceeds by three instalments totalling US$3,308,868, particulars of which are set out in the schedule to BSIL's proof of debt.

29. The NAV of the Reference Fund fell by 17.64% in the month of September 2008. This constituted a Designation Event as defined in Appendix C, thereby entitling BSIL to serve a further notice on 22 October 2008 (expressed to supersede the 3 September notice) designating a new Expiration Date of 31 December 2008, thereby terminating the Option Agreement on that date. Under the term of the Confirmation, the Option was deemed to have been exercised on that date and the Cash Settlement provision became applicable. At the same time BSAAIL, as the registered holder of the Class F shares, gave notice of its intention to redeem them on 31 December 2008.

30. Shortly thereafter, on 27 October 2008, the Fund's board of directors resolved (1) to recommend to the sole voting shareholder that the Fund be wound up voluntarily and (2) to declare an immediate suspension of the calculation of the NAV of all classes of Participating Shares and accordingly of all subscriptions and redemptions of such shares. The Fund's investment manager did not accept this advice and more than a year later, on 26 November 2009, BSAAIL issued a winding up petition on the just and equitable ground in its capacity as the registered holder of the Class F Shares.

The law relating to construction of commercial contracts

31. The applicable English and Cayman Islands law relating to the interpretation of contracts is well settled and requires the court to determine what the parties meant by the language used. This involves ascertaining what a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract would have understood the parties to have meant. The applicable principles have been discussed in many cases, most notably by Lord Hoffmann in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896, in which he said (at pages 912-913) –

> "The principles may be summarised as follows.
> (1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

> (2) The background was famously referred to by Lord Wilberforce as the 'matrix of fact', but this phrase is, if anything, an understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.
>
> (3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification. The law makes this distinction for reasons of practical policy and, in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this exception are in some respects unclear. But this is not the occasion on which to explore them.
>
> (4) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax: see *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749.
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> (5) The 'rule' that words should be given their 'natural and ordinary meaning' reflects the commonsense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had. Lord Diplock made this point more vigorously when he said in *Antaios Compania Naviera SA v. Salen Rederierna AB,* [1985] AC 191, 201: 'if detailed semantic and syntactical analysis of words in a commercial contract is going to be lead to a conclusion that flouts business common sense, it must be made to yield to business common sense.' "

32. Where the language used by the parties has more than one potential meaning, so that there are two possible constructions, it will generally be appropriate for the Court to prefer the construction which is most consistent with business common sense. *Rainy Sky SA v. Kookmin Bank* [2011] 1 WLR 2900, per Lord Clarke at paragraph 30; *Reilly v. National Insurance and Guarantee Corporation Ltd* [2008] EWCA Civ 1460 per Moore-Bick LJ at paragraph 10; and *Schuler AG v. Wickman Machine Tool Sales Ltd* [1974] AC 235, in which Lord Reid said (at page 251E) –

> "The fact that a particular construction leads to a very reasonable result must be a relevant consideration. The more unreasonable the result the more unlikely it is that the parties can have intended it, and if they did intend it the more necessary it is that they shall make their intention abundantly clear."

33. The question of implying a term arises when the contract does not expressly provide for what is to happen when some event occurs. Where the reasonable addressee would understand, reading the other provisions of the contract against the relevant background, that the parties must have intended that something is to happen, and that

this is what the contract must mean even though it does not expressly say so, the Court will imply a term as to what will happen if the event in question occurs: see *Attorney General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988 at paragraphs 17 and 18 in which Lord Hoffmann said –

> "[16] Before discussing in greater detail the reasoning of the Court of Appeal, the Board will make some general observations about the process of implication. The Court has no power to improve upon the instrument which it is called upon to construe, whether it be a contract, a statute or articles of association. It cannot introduce terms to make it fairer or more reasonable. It is concerned only to discover what the instrument means. However, that meaning is not necessarily or always what the authors or parties to the document would have intended. It is the meaning which the instrument would convey to a reasonable person having all the background knowledge which would reasonably be available to the audience to whom the instrument is addressed: see *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896, 912-913. It is this objective meaning which is conventionally called the intention of the parties, or the intention of Parliament, or the intention of whatever person or body was or is deemed to have been the author of the instrument.
>
> [17] The question of implication arises when the instrument does not expressly provide for what is to happen when some event occurs. The most usual inference in such a case is that nothing is to happen. If the parties had intended something to happen, the instrument would have said so. Otherwise, the express provisions of the instrument are to continue to operate undisturbed. If the event has caused loss to one or other of the parties, the loss lies where it falls.
>
> [18] In some cases, however, the reasonable addressee would understand the instrument to mean something else. He would consider that the only meaning consistent with the other provisions of the instrument, read against the relevant background, is that something is to happen. The event in question is to affect the rights of the parties. The instrument may not have expressly said so, but this is what it must mean. In such a case, it is said that the Court implies a terms as to what will happen if the event in question occurs. But the implication of the term is not an addition to the instrument. It only spells out what the instrument means."

Construction of the Option Agreement

34. The Election for Physical Settlement contains an express provision for the *payment* of the Strike and counsel are agreed that it creates a payment obligation which arises only if and when the Fund makes this election. In contrast, neither the definition of Cash Settlement Amount (quoted in paragraph 24 above) nor any other provision of the Option Agreement contains any express provision for *payment* of the Strike upon exercise of the Option. In my judgment, the reason why no payment obligation is expressed is that the parties intended to achieve an economically equivalent result by a different mechanism, namely the redemption of the Class F shares and payment by

BSIL/Seller of the Cash Settlement Amount to the Fund/Buyer. The mechanism for determining what, if anything, is payable by BSIL involves reducing the value of the Strike to zero. This is the mechanism whereby BSIL receives value for the Strike without imposing a payment obligation upon the Fund. This begs the question, what is to happen if the value of the Strike is greater than the redemption proceeds so that it cannot be reduced to zero in this way. In my judgment nothing is to happen. The loss rests with BSIL, because the transaction is intended, in this event, to have a result which is economically equivalent to a limited recourse loan. Implying into the Option Agreement a payment obligation – whether it be an independent obligation to pay the Strike in full or an obligation to pay the balance, arising only in the event that the value of the Strike cannot be reduced to zero by application of the redemption proceeds - is to re-write the parties' contract, which I am not entitled to do.

35. Any investment bank must understand perfectly well the risks associated with providing credit on a limited recourse basis. It cannot be said that it is inherently unlikely that BSIL would undertake any such risk having regard to the factual background in this case. I find it impossible to avoid the conclusion that an essential part of the Option Agreement was to provide the Fund with credit for the purpose of providing some investors with a leveraged exposure to its performance, whilst at the same time providing others with an unleveraged exposure or an exposure at a different level of leverage. In order to achieve this result, the Fund must be able to treat the amount of the Strike as a "liability" of the leveraged share classes only. The purpose of the Option Agreement was to achieve this result, which is not contrary to business common sense or unreasonable in any way. Except in respect of the Election for Physical Settlement, the draftsman has carefully avoided using language which might tend to suggest the creation of a payment obligation.

36. Any lender whose recourse is limited to the proceeds of the sale of a particular asset, in this case the Class F shares, is exposed to market risk. By the express terms of the Option Agreement, BSIL hedged its market risk in various ways. The Investment Guidelines contained in Appendix D enabled BSIL to monitor and limit the way in which the Fund invested and managed its assets. If the market value of the Fund's assets fell with the result that the Maximum Leverage Factor (which is the equivalent

of a loan to value ratio stipulated in a secured credit facility) exceeds the maximum of 2.2x leverage, a Reallocation Event occurs, thus requiring the Fund to take any one or more of four identified steps to cure the position. The provisions of Appendix C are also designed to hedge BSIL's risk by enabling it to terminate the Option Agreement by designating an Early Terminate Date in the event that various types of event occur, such as a fall of more than 10% in the NAV of the Reference Fund.

37. There is no basis for thinking that the use of limited recourse is inherently unlikely in the context of this case and I do not accept Mr. Handyside's suggestion that the parties are unlikely to have viewed the Option Agreement as the economic equivalent of a limited recourse loan, because it does not provide for BSIL to have any "upside" participation in any increase in the NAV of the Class F shares over its term.

38. Mr. Handyside also points to the definition "Strike Increase by Payment of Cash to Buyer" which expressly states that the value of the Option (to the Fund) decreases by the Strike Amount Increase. It goes without saying that when BSIL pays cash to the Fund, the value of the Strike is increased dollar for dollar which means, all other things being equal, that the Cash Settlement Amount decreases dollar for dollar. This scenario does not shed any light upon the manner in which BSIL receive value for the Strike is to be discharged. The parties could have stipulated for its discharge to be achieved by the performance of a payment obligation. Instead, they stipulated for its value to be reduced to zero through the mechanism for establishing the Cash Settlement Amount, effectively by setting it off against the redemption proceeds of the Class F shares.

39. The parties are agreed that if the Fund elects for physical settlement (which is the economic equivalent of electing to repay a loan prior to the term date), then the Election for Physical Settlement provision imposes upon the Fund a payment obligation. This makes perfectly good commercial sense. Taking the analogy of the secured credit facility, the borrower cannot expect to terminate the facility and recover his security without first repaying the lender in full. However, the fact that the borrower has the right to terminate the facility by repaying the loan prior to the term date is in no way inconsistent with it being a limited recourse transaction as Mr.

Handyside seeks to suggest. He also relies on the provision which states that if BSIL determines (in good faith and acting commercially reasonably) that it is not practicable to effect physical settlement, the Option will be cash settled instead. Provisions of this kind are typically included in contracts of this sort as a protection for the obligor whose ability to effect a timely physical delivery of an asset may be limited in some way by matters outside of his control. No such consideration arises in the circumstances of this case, because the asset in question is the Class F shares issued by the Fund itself. In these circumstances, "physical delivery" is likely to be a formality. BSIL could achieve "physical delivery" by the simple mechanism of instructing or authorising the Fund to cancel the shares. Furthermore, in the ordinary course of business the Fund will only ever elect for Physical Settlement if and when it is in a position to discharge the payment obligation which will then arise. Mr. Handyside's argument that BSIL's entitlement to receive the Strike in full could in some circumstances depend upon whether or not it is practical to effect physical settlement seemed rather artificial to me.

40. Mr. Handyside placed a good deal of emphasis upon the final paragraph of the definition of "Cash Settlement Amount" (set out in full in paragraph 24 above) which states that :–

> " For the avoidance of doubt, upon option Exercise (and subject to "Election for Physical Settlement" below), the full amount of Reference Fund Shares shall be redeemed and corresponding proceeds will go first towards reducing the Strike, before being paid to *Seller* (emphasis added) only when the value of the Strike is equal to zero."

Read literally, this provision makes no sense whatsoever. According to Mr. Handyside the provision means that the Fund must first reduce the value of the Strike to zero by paying money to BSIL. When this has been done, and only then, he says that the Fund has an obligation to pay the redemption proceeds to BSIL, which then has an obligation to repay exactly the same sum back to Fund by way of the Cash Settlement Amount. To my mind this construction produces a wholly unreasonable, even nonsensical, result which cannot possibly have been intended by the parties. The use of the word *Seller* must be a typographical error. If one substitutes the word *Buyer*, the whole clause makes perfectly good commercial sense. What it means is that the amount of the redemption proceeds received by BSIL will go first to reducing the Strike and only when the value of the Strike is equal to zero (meaning only when

it has been "paid" in full) will any part of it be paid back to the Fund by way of the Cash Settlement Amount. I found Mr. Handyside's argument on this point to be highly artificial. In my judgment this clause does not point to the conclusion that the Option Agreement should be construed as imposing an obligation upon the Fund to pay the Strike, independently of the obligation to pay redemption proceeds which will be applied to reduce the value of the Strike to zero.

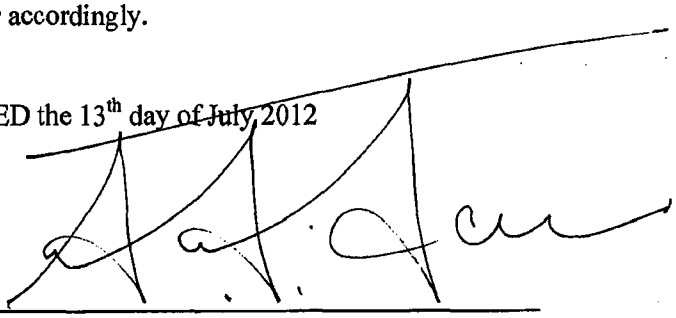
Conclusion

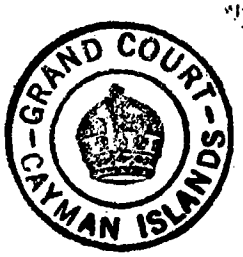
41. In my judgment, on a true construction of the Option Agreement, BSIL's right is limited to reducing the amount of the Strike from the redemption proceeds of the Class F Shares. It follows that BSIL is not a creditor of the Fund and the JOLs are directed to reject its proof of debt.

42. As regards costs, I have already ordered that both parties' costs of this application shall be paid out of the assets of the Fund, such costs to be taxed on the indemnity basis if not agreed with the JOLs. The question whether the JOLs' costs of attending the hearing should be allowed will be adjourned for consideration on 7th August 2012 (at the same time as their summons for approval of their remuneration).

Order accordingly.

DATED the 13th day of July 2012





The Honourable Mr Justice Andrew J. Jones QC
JUDGE OF THE GRAND COURT