

Primeo v HSBC - Landmark Judgment Handed Down in Grand Court

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In a landmark judgment in the Cayman Islands Grand Court in August, Justice Jones QC dismissed a claim for approximately US\$2 billion in damages for negligence made by Primeo Fund ("Primeo") against its administrator and custodian. Even though the defendants were determined to be liable for their acts and omissions, the Judge held that Primeo failed to establish the causal link between such acts or omissions and the loss that was allegedly suffered.

This judgment illustrates the risks which can arise when providing services to funds, and directs administrators and custodians on the scope of their obligations.

Primeo was a Cayman investment fund which directly invested in Bernard L Madoff Investment Securities LLC ("BLMIS") for 14 years from 1993-2007. In 2007 Primeo began indirectly investing in BLMIS through another Madoff feeder fund, Herald Fund SPC ("Herald").

Following Madoff's arrest and the exposure of his infamous Ponzi Scheme in 2008, the liquidators of Primeo launched proceedings against HSBC, who had acted as the custodian and administrator for both Primeo and Herald, alleging that they had been grossly negligent in the performance of their duties as both custodian and administrator, thereby causing Primeo's investors to suffer substantial losses.

BLMIS acted as investment manager, broker and sub-custodian for its clients, including Primeo, which led to a high risk investment structure. It was alleged that putting in place the most effective safeguards to protect Primeo's assets, monitoring the suitability of BLMIS to act as sub-custodian and adopting appropriate valuation

procedures were among the duties the Defendants were obligated to carry out.

On 23 August 2017, Justice Jones QC ruled that the Defendants owed a continuing contractual duty to assure themselves of the suitability of BLMIS acting as the sub-custodian and failed to provide Primeo with readily available safeguards which would have protected Primeo's assets. It was also held that the Defendants were grossly negligent in the procedures applied to the calculation of Net Asset Value.

However, Justice Jones, QC did not accept that the Defendants' breach of duty caused Primeo to suffer any loss, or that the Directors of Primeo would have withdrawn the investments placed with BLMIS or ceased to invest further with BLMIS had the Defendants acted in the way that Primeo suggested they should have.

Justice Jones, QC also rejected Primeo's claim for lost value of its shareholding in Herald, under the principles of reflective loss since the proper claimant for any such loss should be Herald itself. Justice Jones, QC held that, had the Claimants been successful, he would in any event have reduced the damages awarded by 75% due to Primeo's contributory negligence.

This decision highlights the duties of custodians and administrators of funds, and what may be considered "gross negligence" in the performance of such duties. It is very likely that the Claimants will appeal. The Court of Appeal's decision in this regard, would be of great interest.

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