



## The Privy Council Exercises its Leverage to Dismiss the Appeal in: *Al Sadik -v- Investcorp Bank BSC and Others*

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On 18 June 2018, the long running case of *Al Sadik -v- Investcorp Bank BSC and others*<sup>1</sup> reached its conclusion in the Privy Council. Investment Managers will welcome the Privy Council's dismissal of the appeal by Mr. Al Sadik. The Privy Council found that the Cayman Islands Court of Appeal and Grand Court both correctly decided that the Share Purchase Agreement ("SPA") authorised Investcorp Bank BSC ("Investcorp") (and its related entities) to leverage Mr. Al Sadik's investments and take administrative steps in furtherance of that goal, including transferring Mr. Al Sadik's funds to a special purpose vehicle ("SPV"), Blossom IAM Ltd ("Blossom").

### Leveraging of investments

Leveraging an investment is a common way to increase an investor's potential returns. Instead of solely relying on the investor's own funds, borrowed funds are also used to increase the size of investment and thereby increase the size of the potential return. However, any losses on the underlying investment will also be increased.

There are a number of ways to leverage an investment through an investment fund. For example:

- An investor may simply choose to invest in a hedge fund with its own internal element of leveraging.
- An investor may invest in one or more feeder funds which are used as leveraging vehicles for multiple investors so as to increase the amount invested in the underlying hedge funds.
- An investor, or the investment manager, may set up an SPV for the specific purpose of that investor's leveraging, with the SPV holding the investment assets and being liable to repay any borrowing.

### *Al Sadik -v- Investcorp Bank BSC and others*

Mr. Al Sadik invested c. US\$130 million with Investcorp in March 2008 pursuant to the terms of the SPA. Those funds were leveraged through the use of the Blossom SPV. Ultimately, the leveraging increased the losses Mr. Al Sadik incurred on his investment in 2008/2009, one of the worst periods for hedge fund investors in history as the global financial crisis developed. When Mr. Sadik ultimately redeemed his investment in December 2009, he had lost over 40% of the initial amount invested.

Mr. Al Sadik made a number of claims against Investcorp (and related entities) in respect of the losses he incurred. On appeal, the two main issues considered by the Privy Council were as follows:

- Was the transfer of Mr. Al Sadik's funds to Blossom permitted under the SPA?
- Was the leveraging of Mr. Al Sadik's funds a breach of the SPA?

<sup>1</sup> [2018] UKPC 15.

The terms of the SPA were general in nature and dealt with the substance of the proposed transaction at a relatively high level. The authorised powers were described broadly by reference to purpose rather than by spelling out in minute detail every power exercisable: “*The Company’s board of directors will authorise or otherwise cause the Company to take any actions that the board believes are necessary or desirable in order to effectuate the purposes of this investment.*”.

The Privy Council noted that Court of Appeal had properly considered the factual background. Particularly, that the relevant Investment Proposal had suggested leveraged investments in hedge funds to Mr. Al Sadik. Accordingly, the Court found that the SPA needed to be construed so as to permit this type of investing.

Counsel for Mr. Al Sadik asserted that a distinction should have been made between the different methods the investment could be leveraged (and that the transfer of funds to the Blossom SPV was a not a permitted method of leveraging under the SPA). However, the Privy Council was not attracted to this submission. Given the general nature of powers granted under the SPA, the way in which the investment was leveraged was not material.

The Privy Council found that the Court of Appeal and Grand Court were both correct in concluding that, upon its true construction, the SPA authorised the leverage and payment to (or purchase of shares in) Blossom, which was an authorised administrative step, rather than an investment, for the achievement of that leveraging purpose.

## Conclusion

Given the common use of generally drafted clauses in commercial investment agreements, the Privy Council decision will be welcomed by the investment community. Nevertheless, the decision is a reminder to managers to ensure that the terms of investment agreements are fit for purpose in order to mitigate the risk of future misunderstandings/disputes between manager and investor.

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