WALKERS

AHAB v SICL & Others: The Cauldron of Fraud

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Written by: Colette Wilkins, Partner, Shelley White, Partner and Sarah Gavin, Associate

Introduction

On 31 May 2018, the Chief Justice of the Grand Court of the Cayman Islands handed down judgment in *Ahmad Hamad Algosaibi & Brothers Company v Saad Investments Company Limited and Others*. At their height, the claims and counterclaims amounted to over US$17 billion.

The Defendants to AHAB's claims were 16 corporate entities, all of which are in official liquidation, and one individual, Maan Al Sanea ("Al Sanea"). Al Sanea did not participate in the proceedings save for an unsuccessful forum challenge. AHAB alleged that its claims gave rise to a proprietary interest in all of the assets held in the estates of the corporate entities, thereby impeding the distribution of the assets of these companies to their creditors by the official liquidators.

After a year-long trial the Chief Justice found that far from being the victim of fraud Ahmad Hamad Algosaibi & Brothers Company ("AHAB") had been actively involved in an enormous and longstanding Ponzi scheme which had defrauded more than one hundred banks. In determining AHAB's claim, the Honourable Chief Justice considered *inter alia* what the AHAB partners knew of the fraud on the banks, the benefits they received as a result of it, AHAB's allegations of forgery and manipulation of documents, tracing, and the defence of illegality. On 14 June 2018, AHAB filed a notice of appeal, appealing the decision of the Grand Court to the Cayman Islands Court of Appeal.

Background to the proceedings

AHAB has its origins in a business began by Hamad Algosaibi in the 1940s. When Hamad died in 1969 he was succeeded by his three sons, Ahmad, Abdulaziz, and Suleiman. Together, they incorporated AHAB as a general partnership and successively chaired AHAB until Suleiman's death in February 2009. AHAB has since been chaired by their respective sons Yousef, Saud, and Dawood who are each AHAB partners. From 1980 onwards, AHAB strategically expanded into financial services and other related businesses. In 1981, the board of directors established the 'Money Exchange' as an unincorporated division of AHAB. Al Sanea, who had married into the family in 1980, was appointed its Managing Director.

The Court found that the Money Exchange was, from inception, a criminal enterprise; together with certain other of AHAB's businesses, it was used by Al Sanea, with AHAB's full knowledge, to perpetrate one of the biggest Ponzi schemes in history. In May 2009, when the global financial crisis impacted AHAB's credit lines, the Ponzi scheme collapsed, with AHAB defaulting on billions of dollars' worth of debt. AHAB commenced proceedings in the Grand Court of the Cayman Islands in July 2009 seeking to recover from Al Sanea and his group of companies (or entities doing business therewith) the amount of borrowing that was unrepaid at the time of the default, which AHAB said represented the proceeds of a fraud Al Sanea had perpetrated against it. AHAB's claims were initially for US$9.2 billion.

Amongst the corporate defendants were entities forming a part of Al Sanea's 'Saad Group', which was headquartered in Al Khobar. The Saad Group included Saudi Arabian entities as well as trusts and companies registered in the Cayman Islands; the latter explaining how the Cayman Islands Court came to hear AHAB's claims. Saad Trading and Contracting Company (STCC) was the Saad Group's head office in Saudi Arabia and was described by the Chief Justice as being the hub of its wheel. It was not, however, a defendant to the proceedings.

Two of the corporate defendants, Saad Investments Company Limited or 'SICL' (the Saad Group's principal international finance and investment arm) and Singularis Holdings Limited or 'Singularis' (incorporated as a special purpose vehicle to facilitate the acquisition of significant shareholdings in financial institutions) brought counterclaims against AHAB for a total of US$5.9 billion.

AHAB's claim

AHAB claimed to be a victim of a fraud perpetrated by Al Sanea. Initially it said that all of the borrowing by the Money Exchange was unauthorised. However, in 2011, late disclosure by AHAB in proceedings brought against it by certain lending banks in London, revealed that until at least mid-2002, AHAB through Saud (and on Saud's account also Suleiman (who died in 2009)) was aware of and had authorised borrowing by the Money Exchange in the order of SAR 7.8 billion (approximately US$2 billion). AHAB's case thereafter became that *some* borrowing was authorised pursuant to a policy termed "*New for Old*", allegedly implemented by Suleiman after Abdulaziz's stroke and intended to restrict borrowing by Al Sanea to only such loans as had been taken before the time of its implementation. AHAB's case was that borrowing in excess of that amount was unauthorised and fraudulent.

AHAB alleged that Al Sanea embarked on forgery on an "industrial scale", applying AHAB partner signatures to facility documents without AHAB's knowledge or authority. Following an amendment belatedly made to its case during the trial, AHAB also argued that some facility documents were manipulated by Al Sanea in order to deceive Suleiman into thinking that the existing and new facility agreements were for the same amount when they were not.

The Chief Justice said that AHAB's claims depended upon three things: (1) unauthorised bank borrowings; (2) forgery; and (3) unauthorised bank borrowing being misappropriated or stolen by Al Sanea. As to which, the Court found that: AHAB knew of and authorised the enormous borrowings from banks which were obtained by fraudulent means; there was no reasonable foundation for a finding that the questioned documents and signatures were deployed by Al Sanea without the knowledge and authority of AHAB partners; and that the transfers out of the Money Exchange were all recorded in the books and records of the Money Exchange, of which AHAB's claim of ignorance and non-authorisation was found to be false. AHAB's claims therefore failed at every level.

AHAB's knowledge and authorisation of the bank borrowings

Whether the AHAB partners knew of and authorised the enormous borrowings from banks which were obtained by fraudulent means through the Money Exchange was said by the Chief Justice to be the "*pivotal issue*". Resolution of this issue was heavily influenced by the Court's findings regarding the extent of the AHAB partners' knowledge of, and involvement with, the means by which the fraud was perpetrated; namely, by the dissemination to the banks of falsified financial statements for the Money Exchange that deliberately and grossly understated the extent of the borrowings and also, therefore, the true extent of the AHAB indebtedness to the banks and its status as a borrower. By their presentation to the banks, the false financial statements became the central instrumentality of the fraud.

The Chief Justice concluded that it was satisfied that the knowledge and authority of the AHAB partners was "*overwhelmingly and conclusively proven*", and that AHAB's attempts in submissions to place a "*misleading gloss upon the evidence*" were "*plainly unacceptable*". The evidence showed that those who were in control of AHAB (over two generations) were aware of the fraudulent practices of the Money Exchange (namely the production of and dissemination to the banks of falsified financial statements); those practices having been institutionalised by Abdulaziz during his chairmanship of AHAB. The Court also found that the policy termed "*New for Old*" was an invention and had never existed, such that there was never any restriction placed upon Al Sanea's authority to borrow.

Forgery

The Chief Justice found that there was no reasonable foundation for a finding that the questioned documents and signatures were deployed by Al Sanea without the knowledge and authority of AHAB partners. Moreover, the 16 sets of bank facility documents on which AHAB's manipulation case rested could not bear the weight of inference that AHAB wished to place upon them. The inevitable conclusion drawn by the Court was that there was no fraud perpetrated upon AHAB. Rather, a fraud on the banks was perpetrated by AHAB and Al Sanea acting in concert against the banks to obtain borrowing which would certainly not have been provided had the banks known the true financial position of the Money Exchange. The fraud on the banks was the Money Exchange's *raison d'être*; defrauding the lending banks was in its DNA.

The fact that AHAB had resiled from its original case that every signature on facility documents was a forgery (without any of AHAB's witnesses explaining to the Court how they could have pursued this dishonest claim for almost two years and without acknowledgement that on their instructions they had pursued dishonest forgery allegations) and the fact that, despite the overwhelming evidence and AHAB's own admissions, AHAB had hedged its bets to the very end as to whether or not Abdulaziz would be found to have been knowingly involved with the fraud on the banks, led the Chief Justice to conclude that "*AHAB's credibility has suffered from its propensity not only for suppression of evidence but for dissemblance as well*".

The Court found that the obvious explanation for AHAB's complicity in the fraud was the pursuit by AHAB of the strategy to use bank borrowings that would not appear on AHAB's books to acquire and hold a portfolio of investments, comprising the strategic equity investments in banks and other institutions. Because of AHAB's failure to inject capital or to pay down the borrowings of the Money Exchange that strategy also required the constant taking of further borrowing to repay earlier borrowing. Such was the Money Exchange's business model.

Al Sanea was allowed by the AHAB partners to deploy a similar strategy for his own purposes as the *quid pro quo* for Al Sanea's willingness also to use the Money Exchange to procure fraudulent borrowing on behalf of AHAB. This resulted in the spiralling vortex of indebtedness which inevitably overwhelmed the Money Exchange.

Misappropriation

Contrary to AHAB's case, Al Sanea's withdrawals from the Money Exchange were not misappropriations but were loans; a debt that Al Sanea was expected to repay. This indebtedness to the Money Exchange was authorised by the AHAB partners and was, over the years, meticulously accounted for. The ledger on which the debt was recorded was concealed from the banks but was audited and reported to the AHAB partners in annual "Audit Packs". As such, the ledger recorded an ongoing facility for Al Sanea to borrow funds; a facility that had been granted to Al Sanea by Abdulaziz and which had never been revoked. What the AHAB partners had not reckoned on and what shocked them in May 2009 when the global financial crisis erupted was that Al Sanea, thought to be one of the wealthiest men in the world, would be unable to repay his debts. The Chief Justice said that the reality was that the AHAB partners made a bad credit decision.

The relevant legal principles and their application to AHAB's claims

Notwithstanding that the Court found that there was no misappropriation, the Chief Justice went on to consider the legal principles applicable to AHAB's claims.

AHAB's claims were primarily proprietary in nature, seeking to recover what AHAB said was its property (or the traceable substitutes) from the Defendants. AHAB therefore had to meet the requirements of the proprietary remedies which it sought. Notwithstanding AHAB's asserted personal claims against the Defendants, AHAB's proprietary claims were crucial to its success because, unless AHAB proved that the assets held by the Defendants were its property, AHAB would be unable to secure priority over the existing contractual claims of third party banks in the respective liquidations of the Defendants. If AHAB had succeeded, it would have established that the assets of the Defendants which represented its property belonged to it and so to that extent would supersede and likely extinguish the contractual (personal) claims of the third party banks.

The Court held that for every proprietary tracing claim, two premises would have to be established: first, the antecedent breach of trust or fiduciary duty; second, the identification of the traced asset or its traceable proceeds in the possession of the defendant. As to the first, having at all times been privy to and having authorised Al Sanea's activities, AHAB had failed to prove that fundamental premise of its case. That finding was sufficient to determine AHAB's claims. In considering the second limb, the Chief Justice gave some informative guidance on how the Cayman Islands Courts should approach tracing exercises.

Tracing

Even if AHAB had been able to establish the antecedent breach of trust by Al Sanea, the Court held that it would still have had to prove the necessary transactional links between its funds, taken from the Money Exchange, and the accounts of the Defendants. In this respect, the Court said that the rules of tracing demand that a plaintiff establish property of his, which has been unlawfully taken from him (a proprietary base), that that property has been used to acquire some other new identifiable property, which may then have been used to acquire another identifiable asset (a series of transactional links) and requires that the chain of substitutes be unbroken. It would be incumbent upon a plaintiff to plead each element of the chain linking the original misappropriation with the property held by the defendant.

The vast majority of transfers out of the Money Exchange went to STCC. STCC itself held very large asset portfolios and incurred large amounts of debt from many banks. This source of wealth and funding was raised independently of any funding obtained by STCC through the Money Exchange. STCC was not joined as a defendant to the Cayman Islands proceedings and there had been no disclosure of its internal financial records and bank accounts. Without such disclosure, it was not possible to identify, by chains of transactions through STCC to the Defendants, funding which had originated from the Money Exchange.

In the absence of transactions linked to the Defendants, AHAB had argued that it was unnecessary to show an unbroken chain of transactions and relied on Relfo Limited (in liquidation) v Varsani [2015] 1 BCLC 14 and Federal Republic of Brazil & Another v Durant International Corp [2015] 3 WLR 599 so as to argue that the Court could infer that transactions were linked. AHAB relied on "patterns" of movement of sums of money leaving the Money Exchange and funding of particular Defendants, from which AHAB said such an inference (that the transactions were linked) could be drawn. Typically what this meant was that money was shown to leave the Money Exchange, primarily to STCC (by means of cheques, letters of credit, or electronic transfers) and certain sums were shown to have been later paid by STCC to Awal Bank and then on to one of the defendants. AHAB said that the patterns observed could be relied upon for the drawing of inferences that they represented money originally transferred from the Money Exchange to STCC. However, the Court found that this "patterns" approach was not a sound basis for the drawing of such inferences, let alone as proof of a proprietary tracing claim. Whilst AHAB cited a number of cases where inference might be allowable as a substitute for direct evidence of a link, or links, in the chain, it would be impermissible to rely upon mere assertion of receipt of monies without linking that to a specific misappropriation, or set of misappropriations to found receipt-based claims. This would be tantamount to reliance on the "swollen assets" theory of tracing that has long been discredited.

No maelstrom

AHAB had also sought to reverse the burden of proof by alleging that the Defendants participated with Al Sanea in the creation of a *maelstrom* or black hole and that they were involved with him in the cross-firing of transactions. The Court held that whilst the rules of tracing do not permit of evasion where transactions are deliberately structured to avoid their operation, the Court said that in every case of a *maelstrom* there would be a minimum requirement of proof of a deliberate attempt to create a coordinated scheme calculated to

hinder any attempt to trace the relevant funds before the burden of proof would be reversed. AHAB had not proven these facts in this case and there was no factual basis for concluding that these transactions had been used merely as an overarching and coordinated campaign to create a *maelstrom* to obfuscate fraudulent activity. While there were myriad and complex transactions going back and forth between the Money Exchange and Al Sanea's Saad Group entities, there were apparent commercial reasons for the transactions (albeit that they appeared to have been designed mainly to facilitate Al Sanea's and his Saad Group companies' business objectives). The transactions appeared to have been invariably and accurately recorded for accounting purposes within the Money Exchange's records and, where available to the Court, in the Saad entities' records as well.

Duty to account

AHAB resorted, impermissibly in the Court's view, to a claim for equitable accounting for reversal of the burden of proof. AHAB's case was that Al Sanea owed a duty to account as an express fiduciary, and the Defendants received the traceable proceeds of AHAB's money with the requisite knowledge of Al Sanea's breach of fiduciary duty, so as to render them liable to account. The Court found that this argument was without merit. Here too, the case law required AHAB to first prove the antecedent breach of trust by Al Sanea, before it might rely on the case law regarding reversal of the burden of proof for which AHAB contended. Moreover, the duty of a constructive trustee to account would not arise where there was no receipt of monies in relation to which a constructive trust could itself arise. AHAB would therefore have had to prove that its money had been received by the Defendants before it would have been entitled to a reversal of the burden of proof. In the absence of transactional links, again AHAB's reliance on patterns was not a sound basis for the drawing of the inferences as proof of a proprietary claim.

Dishonest Assistance, Conspiracy, and Unjust Enrichment

Each of AHAB's dishonest assistance claim, conspiracy claim, and unjust enrichment claim rested upon the allegation that the Defendants received money or assets that represented the proceeds of funds misappropriated from the Money Exchange. As the tracing claim failed, so did these claims. AHAB's claims were further flawed on the facts; the mere receipt of funds, absent more, was insufficient to constitute assistance for the purposes of the tort of dishonest assistance and none of the (relevant) Defendants' acts provided any assistance, let alone dishonest assistance, to Al Sanea in his alleged breaches of fiduciary duty. The tort of conspiracy also required an agreement between co-conspirators whereas AHAB had failed to identify any. And AHAB's claim in unjust enrichment also failed because AHAB had not proved the requisite fraud or receipt of proceeds of that fraud.

AHAB had submitted that, as regards unjust enrichment claims, recovery would be possible against an indirectly enriched recipient provided that there was a sufficient causal connection between the payment in question and the enrichment, and contended that proprietary remedies were available in response to a successful unjust enrichment claim. However, the Court held that AHAB's submissions on the case law were misconceived and could not survive the decision of the United Kingdom Supreme Court in the 2017 case of Commissioners for HM Revenue and Customs v Investment Trust Companies (In Liquidation) [2017] UKSC 29. The Defendants said that it was clear from Lord Reed's careful speech in that case that the "*at the expense of* " limb of unjust enrichment connoted five basic ideas, including the general rule (subject to limited exceptions) that there must be direct dealings between claimant and defendant, and that where the benefit has not been received "directly" from the claimant it will be difficult to demonstrate that one has been enriched by the other. AHAB had been able to establish no such link in the case of any of the Defendants. It had relied solely upon the debunked swollen assets theory and a misguided attempt to reverse the burden of proof in order to show any link at all between the payments from the Money Exchange to the Defendants. As that was insufficient to establish a tracing claim, it was insufficient to establish the equivalent for the purposes of unjust enrichment. AHAB therefore failed to establish a sufficient causal connection between the payments in question and the enrichment of the Defendants and therefore its personal claim in unjust enrichment.

Illegality

In light of AHAB's complicity in the fraud on the banks from beginning to end, the Defendants' defence of illegality was entitled to succeed.

Early in the trial, AHAB admitted (without admission of fraudulent intent) involvement by the AHAB partners in the production and dissemination of falsified financial statements and knowledge, to some extent, of the borrowings up to September 2000 (when Abdulaziz suffered a debilitating stroke). Thereafter, AHAB said, this practice had ceased on Suleiman imposing "*New for Old*". However, and even if "*New for Old*" was real, contrary to the finding of the Chief Justice that it was an invention raised in a desperate attempt to salvage AHAB's falsified case, "*New for Old*" itself involved the continued dissemination to the banks of falsified accounts, in order to induce the banks to continue to lend at least as much as was required to prevent the collapse of the Money Exchange and other Financial Businesses.

The Court considered the case of Patel v Mirza [2016] UKSC 42 and determined that the Money Exchange was indistinguishable from the case of the highwayman or the modern-day example of the drug dealer given by Lord Toulson. AHAB's claim would therefore be barred in any event through the application of the Court's policy that it would not enforce an illegal arrangement or because AHAB lacked clean hands such that it would not be entitled to invoke equitable remedies. In determining this, the Court set down the proper approach when applying the illegality defence and a series of eight questions it will be useful for the Court to ask when considering its application. Concluding, the Chief Justice said it was "*important to remember that, crucially, the highwayman's case (Everet v Williams) remains good law, save that Lord Toulson has updated the example for modern times to include a drug trafficking operation or enterprise… Lord Toulson ought therefore to be read as articulating*

the well-known proposition (repeatedly affirmed following the highwayman's case) that parties to a fraudulent partnership or enterprise will not be entitled to invoke the powers of the court to recover the proceeds of their fraudulent partnership from their fellow criminal so as to profit from it".

Locus Poenitentiae or the opportunity to abstain from committing a crime before it is too late

There was no possibility of AHAB establishing a *locus poenitentiae* in the face of its conduct, even if (which the Court did not accept) "*New for Old*" was real. There could be no suggestion of repentance because AHAB had failed to make any attempt at penitence long after the fraud took place. Even if the AHAB partners had sought to withdraw from their illegality, they would not have been able to do so; the effects of the fraud were entirely irreversible, the loans obtained by the Money Exchange have been paid off many times with the proceeds of other dishonestly borrowed funds. The proceedings before a specifically convened tribunal in Saudi Arabia did nothing to unravel the years of robbing one creditor to pay off another.

Dismissal of the counterclaims

SICL and Singularis counterclaimed against AHAB for a total of US$5.9 billion, instigated in large part by promissory notes presented to them as representing security for debts owed to them by AHAB and signed and delivered to Al Sanea by Suleiman, acting as chairman and on behalf of AHAB. Other of the counterclaims amounting to more than US$1 billion were based primarily upon liabilities recorded in the accounts of SICL and Singularis as due from AHAB.

The counterclaims were dismissed. The evidence relied upon in proof of the counterclaims was unsafe and unreliable and was said by the Court to arise against the background and out of the cauldron of fraud that the Court said characterised the existence and operation, not only of the Money Exchange and other Financial Businesses but also the existence and operation of SICL and Singularis in the manner of their use by Al Sanea to foster the growth of his wealth by defrauding others. So complex and massive had the Ponzi scheme of borrowing through the Financial Businesses and Al Sanea's Saad entities become, that no court could be expected to rely merely upon accounting records from within them as proof of these multi-billion dollar counterclaims, unsupported by the evidence of a single witness who would speak to the correctness of the accounts or provenance of the purported liabilities. These concerns were amply demonstrated by the full and frank (albeit ill-founded) arguments of the joint official liquidators of Grant Thornton and the counter-arguments of AHAB.

Walkers were instructed by the joint official liquidators of nine Saad Group corporate defendants including Saad Investments Company Limited (in Official Liquidation), the Saad Group's principal international finance and investment arm, and Singularis Holdings Limited (in Official Liquidation), a special purpose vehicle to facilitate the acquisition of significant shareholdings in global financial institutions and worked closely with Stephen Akers, Hugh Dickson and Julie Nettleton of Grant Thornton in defending the AHAB proceedings.

Authors

Colette Wilkins, Partner
Insolvency and Dispute Resolution
T: +1 345 914 4215
M: +1 345 525 7199
E: colette.wilkins@walkersglobal.com

Sarah Gavin, Associate
Insolvency and Dispute Resolution
T: +1 345 914 4209
M: +1 345 938 4209
E: sarah.gavin@walkersglobal.com

Shelley White, Partner
Insolvency and Dispute Resolution
T: +1 345 914 4205
M: +1 345 516 3169
E: shelley.white@walkersglobal.com