

## Fictitious Profits - Recovering Money from Ponzi Scheme Investors

On 22 June 2015, the High Court released a decision in respect of an investor in the Ross Asset Management Limited ("RAM") Ponzi scheme. *Fisk v McIntosh* [2015] NZHC 1403 has implications for all investors in RAM and similar Ponzi schemes. The decision will be of particular interest to investors in BlackfortFX, as the Receivers of that scheme have reportedly issued letters to some of the 1100 investors, demanding that they return payments made to them by BlackfortFX.

### Background

Mr McIntosh invested \$500,000 with David Ross, through his company, RAM. If RAM had operated as a bona fide investment company, Mr McIntosh would have retained ownership of his funds, which would have been held on trust by RAM. A separate management agreement would have provided RAM with a contractual authority to invest Mr McIntosh's funds in order to generate profits, which would also be held on trust for Mr McIntosh.

Instead of operating a legitimate investment business, RAM took Mr McIntosh's funds (as well as funds from other investors) and used them for its own purposes and the purposes of Mr Ross' group of companies (the "Ross Group"). Rather than generating profits through legitimate investments, investors' funds were used to meet any Ross Group expenditure or withdrawals sought by other investors.

Mr McIntosh remained unaware that RAM was operating a Ponzi scheme. Between July and September 2011, he sought to withdraw his funds from RAM. RAM eventually paid Mr McIntosh \$954,047.62 in several tranches in November 2011. That sum was made up of his original \$500,000 investment, plus a 'profit' of \$454,047.62. However, the 'profit' was entirely fictional and was in fact paid out of funds contributed by other investors.

RAM was subsequently placed into receivership and liquidation, at which point the existence of the Ponzi scheme was widely publicised. The Liquidators sought to recover the \$954,047.62 paid to Mr McIntosh under sections 345 to 348 of the Property Law Act 2007 ("the PLA") and sections 292, 294 and 297 of the Companies Act 1993 ("the CA").

### The High Court Decision

The liquidators argued the payments to Mr McIntosh ought to be set aside as:

- creditors of RAM had been prejudiced by the payments as:
  - RAM was insolvent at the time the payments were made;
  - the payments were made with intent to hinder, delay or defeat creditors of RAM in the exercise of the creditors' rights of recourse to recover money owed to them; and
  - RAM did not receive reasonably equivalent value in exchange for making the payments; and / or
- the payments amounted to an insolvent transaction as:
  - they were made when RAM was unable to pay its due debts; and
  - they enabled Mr McIntosh to receive more towards the satisfaction of a debt owed to him by RAM than he would receive or likely receive in RAM's liquidation.

Justice MacKenzie was satisfied that the liquidators' case to set aside the payments to Mr McIntosh were, prima facie at least, established.

However, his Honour was also required to consider the defences raised by Mr McIntosh under section 349 of the PLA and section 296(3) of the CA.

In order to retain the payments made by RAM, Mr McIntosh was required to show that:

- he received the payments in good faith and without knowledge or suspicion that RAM was insolvent at the time of payment; and
- he gave value, or provided valuable consideration in exchange for receiving the payments; or

- if he had not given value or provided valuable consideration:
  - his circumstances had so changed since the receipt of the property that it is unjust to order that the payments be repaid; or
  - he altered his position in the reasonably held belief that the payments to him were valid and would not be set aside.

It was accepted by all parties that Mr McIntosh had no idea RAM was a Ponzi scheme and had acted in good faith in investing in RAM and receiving the payments in November 2011.

Justice MacKenzie considered that Mr McIntosh had given value, or provided valuable consideration in respect of amounts repaid to him, up to the value of his original investment. By appropriating Mr McIntosh's investment for its own purposes rather than hold it on trust, RAM had received value, or valuable consideration from Mr McIntosh. The repayment of that \$500,000 to Mr McIntosh in November 2011 amounted to an exchange of consideration.

However, his Honour determined that Mr McIntosh had not given value, or provided valuable consideration in respect of the fictitious profit. Mr McIntosh had not provided RAM with anything of additional value which would justify RAM paying him funds belonging to other investors. Allowing Mr McIntosh to retain the fictitious profit also failed to achieve a fair balance between the rights of the general body of RAM's creditors to recover insolvent transactions and Mr McIntosh's rights to keep funds paid to him.

Having established a valid defence to the payment of \$500,000, Justice MacKenzie turned to consider whether Mr McIntosh's circumstances had so changed, or he had altered his position to such an extent that the \$454,047.62 in fictitious profit ought not to be repaid.

Ultimately, Justice MacKenzie was not satisfied that the payments had caused Mr McIntyre to change his circumstances to such an extent that it would be unjust to order the fictitious payments to be repaid. Nor was he satisfied that Mr McIntyre altered his position in the reasonably held belief that the payments were valid and would not be set aside.

Mr McIntyre was ordered to repay the fictitious profits of \$454,047.62 to the liquidators.

### **Significance of the decision for investors in Ponzi schemes**

Mr McIntyre has appealed the decision to the Court of Appeal but a hearing of that Appeal will still be some time away.

In the meantime, investors in Ponzi schemes should note the following principles arising out of *Fisk v McIntosh*:

- investors seeking to retain any amounts paid to them by a Ponzi scheme must be able to show they acted in good faith and without knowledge or suspicion that the 'investment' entity was in fact a Ponzi scheme;
- liquidators will likely be able to establish prima facie grounds to set aside payments made by the Ponzi scheme to investors in order to claw them back to be shared amongst all investors and creditors;
- an investor will likely be able to keep amounts paid by the Ponzi scheme up to the amount of their investment in the scheme on the basis that the sum of their investment represented value given or valuable consideration provided to the scheme;
- an investor will only be able to keep fictitious profits paid by the Ponzi scheme if he or she can show:
  - the investor provided some kind of value or valuable consideration to the Ponzi scheme in addition to his or her original investment; or
  - the investor's circumstances have so changed since the receipt of the fictitious profits that it would be unjust to order those profits to be repaid; or
  - the investor altered his or her position following receipt of the fictitious profits in the reasonably held belief that the fictitious profits were valid and would not be set aside.

As each individual investor's circumstances are likely to be different, it is worth taking legal advice before acceding to a demand to repay funds received from a Ponzi scheme.

If you would like to know more about *Fisk v McIntosh*, or if you invested in a Ponzi scheme and wish to understand your legal rights, please contact either [Simon Munro](#) or [Jonathan Nicolle](#)