12-Feb-10
(AJJ.GC)

IN THE GRAND COURT OF THE CAYMAN ISLANDS

FINANCIAL SERVICES DIVISION

The Hon. Mr Justice Andrew J. Jones QC in Open Court

26th and 27th January and 12th February 2010

FSD NOS: 0041, 0042, 0043 & 0044 OF 2009 (AJJ)

IN THE MATTER OF SECTION 94 OF THE COMPANIES LAW (2009 REVISION)

AND IN THE MATTER OF HSH CAYMAN I GP LTD

AND IN THE MATTER OF HSH CAYMAN II GP LTD

AND IN THEMATTER OF HSH CAYMAN V GP LTD

AND IN THE MATTER OF HSH COINVEST (CAYMAN) GP LTD

Appearances: Mr Terence Mowschenson QC, instructed by Messrs Graeme Halkerston and Jayson Wood of Appleby on behalf of the Petitioners

Mr Charles Béar QC, instructed by Mr Vahid Chittleborough of Walkers on behalf of the Companies

JUDGEMENT

1 On 9th September 2009 ABN AMRO Bank NV ("the Petitioner") presented winding up petitions against HSH Cayman I GP Ltd, HSH Cayman II GP Ltd, HSH Cayman V GP Ltd and HSH Coinvest (Cayman) GP Ltd, which I shall refer to collectively as the "the Companies", on the ground of insolvency. On 13th November 2009 Foster J. made winding up orders and appointed

two qualified insolvency practitioners, namely Messrs Walker and Stokoe who are respectively a partner and director of the Cayman Islands firm of PricewaterhouseCoopers, as joint official liquidators of each Company. On 9th December 2009 the Court of Appeal set aside these winding up orders on the grounds that the Petitioner had failed to comply with the requirements of the Companies Winding Up Rules, but did not strike out the petitions. Instead, it ordered a stay of all further proceedings for 7 days during which period the Petitioners applied for leave to amend their petitions and the Companies made a cross application for them to be struck out as an abuse of the process. On 17th December 2009 I dismissed the strike out applications; granted leave to amend the Petitions; and gave directions for trial. This is the trial of the amended petitions.

2 The Companies now accept that there has been full compliance with the procedural and evidential requirements of the Companies Winding Up Rules and that the facts pleaded in the amended petitions have been proved. In particular, it is now admitted that the Petitioners are creditors with standing to present the winding up petitions and that each of the Companies is insolvent by reference to the cash flow test prescribed by Section 92(d) of the Companies Law (2009 Revision).

3 A winding up order is a discretionary remedy, but it is well established as a matter of Cayman Islands law that an unpaid petitioning creditor in respect of an undisputed debt is entitled to expect the Court to exercise its discretion in his favour by making a winding up order in the absence of some exceptional circumstances or special reasons. Recognising that the burden of argument lies upon the Companies to establish that there is some exceptional circumstance or special reason which justifies the Court departing from the usual course, I agreed that Counsel for the Companies should be allowed to open the case and have the last word in reply.

4 It was also agreed that the evidence and arguments relevant to the way in which the Court should exercise its discretion is the same in each case, with the result that it was convenient to hear the four petitions together. The amounts owing by each Company are different and only three of the four Companies claim to be solvent on a balance sheet test, but it appeared to be common ground that these differences did not affect the parties' arguments.

FACTUAL BACKGROUND

5 The relevant factual background can be summarised quite simply as follows. The Companies were incorporated in the Cayman Islands on 15th September 2006 for the sole purpose of acting as the general partners of four limited partnerships established pursuant to the law of Alberta, Canada ("the Limited Partnerships"). The Limited Partnerships were established on 19th

September 2006 as the vehicles through which the underlying investors would acquire and hold substantial minority interests in HSH Nordbank.

6 HSH Nordbank is a large German regional bank created in 2003 from the merger of two state-owned banks and the City of Hamburg and the State of Schleswig-Holstein became the largest shareholders in the merged entity. In 2006 seven investment vehicles advised by J.C. Flowers & Co, a well known private equity investment adviser based in New York, collectively acquired 26.58% of the shares in HSH Nordbank from Westseutsche Landesbank for an aggregate price of €1.25 billion. The seven investor vehicles (which are referred to in Counsel's skeleton argument as the "Shareholder Entities") comprise the four Alberta Limited Partnerships, two Luxembourg companies and a Delaware limited partnership. The Shareholder Entities financed their acquisition in part by borrowing a total of €350 million from the Petitioner.

7 On 19th October 2006 each of the Companies, in its capacity as a general partner, entered into a Loan Facility Agreement with the Petitioner, as arranger and facility agent and as original lender. Apart from the fact that the amounts borrowed vary, I am told by Counsel that the terms of the Facility Agreements are the same, at least in so far as they are material to this matter. Shortly thereafter, in December 2006 and January 2007 the Petitioner syndicated the loans amongst itself and six other British and European banks which are now the lenders for the purposes of the Loan Facility Agreements (whom I shall refer to collectively as "the Lenders"). As one would expect, this syndicate of banks are acting in concert through their Facility Agent, which is now the Global Restructuring Group of the Royal Bank of Scotland Plc (the parent company of the Petitioner). Its Director of Financial Institutions in the Global Restructuring Group, Mr Paul Fillmore, has sworn five affidavits in connection with this matter.

8 The Loan Facility Agreements comprise two elements, namely (a) a term loan which could only be used for the purpose of acquiring the shares in HSH Nordbank and (b) a revolving credit facility which can only be used in or towards financing interest, certain expenses incurred in connection with the share acquisition and re-financing revolving loans. Counsel for the Companies has made the point that it would have been obvious to the Lenders that the only external source of funds available to the Companies with which to service the loans was the dividends received from HSH Nordbank. This may be so, but it is irrelevant to the matter in issue. The Loan Facility Agreements are not limited recourse agreements.

9 In 2008, as a result of the global financial crisis, HSH Nordbank reported substantial losses. The key financial statistics, extracted from the bank's published accounts, are tabulated in paragraph 31 of Mr. J.C. Flowers' affidavit. It suffered a net loss of about €2.7 billion in 2008 and a further

loss of about €800 million in the first three quarters of 2009. Tangible book value per share fell from €57.4 as at the 2007 year end, to €28.7 as at the 2008 year end, and fell again to €19.4 as at the end of the third quarter of 2009. HSH Norbank's financial crisis had an immediate impact upon its shareholders because it ceased to pay dividends and was forced to seek an injection of new capital. Three of the four Limited Partnerships participated in the first recapitalisation in August 2008 by subscribing a total of about €400 million for new shares. A second recapitalisation took place in June 2009 in which the City of Hamburg and the State of Schleswig-Holstein subscribed a further €3 billion and provided an asset guarantee up to €10 billion. None of the seven Shareholder Entities participated in the second recapitalisation with the result that their combined equity stake was diluted to 9.19%. The combined equity stake of the four Limited Partnerships is now 7.31%. This second recapitalisation is the subject of an investigation by the European Commission as to whether or not it constituted "state aid" which would be illegal under the applicable European Union competition law.

10 The Companies failed to pay sums due on 30th January 2009 and on various payment dates thereafter. It is not necessary for me to analyse or recite the details of the defaults because it is common ground that there was a default and, as a result of acceleration of the amounts due under each of the term loans, the four Companies owed a combined sum of approximately €264 million as at 8th September 2009. On 12th November 2009, the day before the hearing before Foster J., the Companies and the Shareholder Entities had issued a proceeding against the Lenders in the English High Court, by which they sought a declaration that the Lenders "were/are estopped from seeking to recover or enforce payment under the Facility Agreements or to accelerate as they purported to do by way of notices dated 8 September 2009". However, no claim form and particulars of claim was ever served and on 20th January 2010 the Companies' London solicitors informed the Petitioner that it would not be served. This estoppel argument has now been abandoned. It is now accepted that the Lenders were entitled to accelerate the loans; that the sums of approximately €124.8m, €58.2m, €14.1m and €66.7m (being about €264m in total) were owed by the Companies respectively, as at 8th September 2009; that they are unable to pay their debts; and that they are insolvent within the meaning of section 92(d) of the Companies Law (2009 Revision).

LEGAL PRINCIPLES APPLICABLE TO THE EXERCISE OF THE COURT'S DISCRETION

11 The applicable legal principles are well established and not in dispute between the parties. On the basis of the admitted facts, the Petitioners have a prima facie right to expect the Court to make winding up orders. The Court's power is a discretionary one, but the Petitioners can expect the

Court to exercise its discretion in favour of making an immediate winding up order unless it is satisfied that there is some exceptional circumstance or special reason which justifies the adoption of a different course. Part V of the Companies Law (2009 Revision) is derived from the English Companies Act 1862 and this Court has consistently followed the decisions of the English Courts on this subject. In *Re Camburn Products Ltd* [1980] 1 WLR 86 at page 93F -94A Slade J (as he then was) said :

"I do not, however, feel much doubt in principle as to what that attitude should be. In the case of a creditor's petition not opposed by other creditors, the general approach of the court was expressed by Lord Cranworth in *Bowes v. Hope Life Insurance and Guarantee Co.* (1865) 11 H.L.Cas. 389, 402: "*...I agree with what has been said, that it is not a discretionary matter with the court when a debt is established, and not satisfied, to say whether the company shall be wound up or not; that is to say, if there be a valid debt established, valid both a law and in equity. One does not like to say positively that no case could occur in which it would be right to refuse it; but, ordinarily speaking, it is the duty of the court to direct the winding up.*"

In other words a creditor in the circumstances mentioned is prima facie entitled to his order and is prima facie not bound to give time to enable the debtor to pay. In my judgment, subject to the discretion given to it by section 25 and 346 of the Companies Act 1948, to which I have already referred, the attitude of the court should be, and is, essentially unchanged today. While I recognise that it would have the right under these two actions to pay regard to the wishes of contributories, in deciding whether or not to make a winding up order on a creditor's petition, or to adjourn the hearing, in my judgment it can, and should, ordinarily attach little weight to the wishes of contributories, in comparison with the weight it attaches to the wishes of any creditor, who proves both that he is unpaid and that the company is "unable to pay its debts."

12 In *Re Lummus Agricultural Services Ltd* [1999] BCC 953, at page 955 Park J said :

"I begin with the basic proposition that although [the equivalent sections in the English Act] give the court a discretion whether to make a winding up order, it is well settled that, if a creditor with standing to make the application wants to have the company wound up, and if the court is satisfied that the company is unable to pay its debts, a winding up order will follow unless there is some special reason why it should not. It is sometimes said that, in such a case, a petitioning creditor is entitled to a winding up order *ex debito justitiae*. I therefore start with the assumption that such an order should be made in this case, and the burden of argument rests upon [counsel for the company] to show me why it should not."

For this reason is was agreed the burden of argument fell upon Mr Béar as counsel for the Companies, with the result that he was allowed to open the argument and have the last word in reply.

THE CASE FOR THE COMPANIES

Summary

13 The Companies' case is that the Court should exercise its discretion by adjourning the petitions or staying all further proceedings in favour of proceedings which were commenced on 21st January 2010 by the Limited Partnerships under Chapter 11 of the US Bankruptcy Code in the Bankruptcy Court for the District of Delaware. Counsel put the argument under two basic heads. First, he contends that putting the Companies under the control of official liquidators is not a commercially sensible course of action, by which he means that it would not be in the commercial interests of either the Companies or Lenders. The Petitioner, which is representing the collective view of all the Lenders, disagrees with this proposition and I am being asked, in effect, to substitute the Court's own view of what ought to be in their interests. Second, counsel contends that, in substance the liquidation process would be a liquidation of the Limited Partnerships rather than the Companies. Liquidating the general partner is said to be a form of "backdoor process" for liquidating the Limited Partnerships and should therefore lead me to the conclusion that this Court should defer to Chapter 11 proceedings commenced by the Limited Partnerships. I now turn to analyse the reasons why it is said that there are exceptional circumstances or special reasons which should lead the Court to adjourn or stay these petitions.

The Companies are said to be "balance sheet solvent"

14 The concept of "balance sheet solvency" is not referred to or defined in the Companies Law (2009 Revision). In this jurisdiction a company is said to be "balance sheet solvent" if the realisable value of its assets is greater than the amount of its liabilities, taking into account a due allowance for its prospective and contingent liabilities. The performance of a "balance sheet test" is relevant for certain purposes in the course of a liquidation, but it is not relevant for the purpose of determining whether the Court has jurisdiction to make a winding up order on the ground of insolvency. Sections 92 and 93 import only a "cash flow test". By section 93, a company is deemed to be unable to pay its debts if (a) having received a statutory demand, it neglects to pay the sum due or secure or compound for it to the satisfaction of the creditor within three weeks; or (b) execution of process on a judgement is returned unsatisfied; or (c) it is otherwise proved to the satisfaction of the Court that the company is unable to pay its debts. If a company fails to pay what is presently due and owing to the petitioning creditor, the Court has jurisdiction to make a winding up order and it is no defence for the company to prove that the realisable value of its assets is now greater than the amount of its liabilities or will become so at some future date. The only relevance of balance sheet solvency is that it may influence the expressed views of creditors

and it may justify the Court having some regard to the views of the shareholders, but the weight to be attributed to their views must still be slight.

15 The amount of the Companies' liabilities under the Loan Facility Agreement is readily ascertainable and is not in dispute. The Companies have no other liabilities except for some fees payable to their professional service providers, the amount of which must be de minimis in comparison to the sums owing to the Lenders. It is admitted that HSH Coinvest (Cayman) GP Ltd must be regarded as "balance sheet insolvent", but is said that the other three Companies should be regarded as "balance sheet solvent". Looked at collectively, the Lenders can expect to be repaid in full only if the realisable value of the shares exceeds €12.32 per share. The Court has the benefit of valuation evidence from Mr J.C. Flowers, the Companies' own investment adviser who advised in connection with the original acquisition. Whilst I accept that he possesses relevant knowledge and expertise, he is not put forward as an independent expert witness. I also have the evidence of Mr Thoralf Erb of Susat & Partner OHG who has been retained to give an independent expert opinion on behalf of the Companies.

16 Mr Erb's report constitutes a series of bullet point summaries of the kind which would be prepared for an audio visual presentation. Unfortunately, I found myself in the position of having to read the bullet points without having the benefit of the oral presentation and the opportunity to ask questions. His opinion is that (a) the "current indicative fair value" of the shares is €19.03 per share, adopting a discounted cash flow valuation approach; (b) the value which could be expected to be realised in a sale on short notice under current capital markets' conditions is between €5.00 and €8.50 per share (subject possible discounts); and (c) the prospective value which could be expected to be achieved in an IPO in 2013 or 2014 is €30.00 – €31.50 per share. I make a number of observations about this evidence.

17 First, I found it unhelpful that Mr Erb did not define what he meant by "fair value" for the purposes of his report. For financial reporting purposes, the "fair value" of an asset is the amount for which that asset could be exchanged between knowledgeable, willing parties in an arm's length transaction. Mr D.J. Katsikas explains (in paragraph 23 of his 1st Affidavit) that this is the basis upon which the shares are valued for the purposes of the financial statements of the Limited Partnerships. Subject to the qualification discussed in paragraph 18 below, I believe that Mr Erb is using the expression "fair value" in this sense, in which case I should not draw any distinction between "fair value" and "market value". The fair value put on the shares by the Companies for the purposes of the Limited Partnerships' unaudited financial statements for the quarter ended 30th September 2009 is €17.00 per share.

18 Second, Mr Erb adopts a discounted cash flow methodology for the purposes of determining his "current indicative fair value" of the shares. Using this methodology, the value of a business is the equivalent of the net present value of future cash flows generated by the business. The Petitioner has engaged Mr. S.C. Taylor, the head of Ernst & Young's Valuation and Business Modelling team, to advise and comment upon Mr Erb's opinion. He agrees (in paragraph 15 of his Affidavit) that a discounted cash flow approach is an appropriate valuation methodology, albeit not the only one. He makes the obvious point that this methodology is typically used to value a business as a whole. Clearly, the market will require a discount for the fact that the Companies' asset is a small minority interest. Collectively, their shareholding is only 7.31% of the equity, or 9.12% if it is marketed with that of the other Shareholder Entities. Mr Erb cannot have overlooked this point. When he says that €19.03 is the fair value "based on a DCF valuation approach indicating the share's intrinsic value", I think he means that it is the fair value, disregarding the minority interest discount or, to put it another way, assuming that the shares will be sold as part of an IPO, which is not going to happen until 2013 at the earliest. In addition to a minority interest discount, the Duff & Phelps Report (exhibited to the Affidavit of Mr R.A. Bartell) says that there should be an illiquidity discount. In my judgment it is not appropriate to look at the "intrinsic value" of the shares for the purposes of ascertaining whether these Companies are balance sheet solvent or insolvent for present purposes. I would regard them as balance sheet solvent only if the realisable value (which is the current market value) is more than the amount of their liabilities. For this reason, it is more useful to have regard to Mr Erb's "price estimation for short-term sale" of €5.00 - €8.50 per share which obviously does take account of a minority interest discount and may also take account of an additional illiquidity discount, rather than his indicative fair value of €19 per share. On this basis all four Companies are balance sheet insolvent.

19 Third, Mr Erb was given only four days in which to perform his work. Not surprisingly, he says that it was insufficient time within which to provide his client with a "full scope valuation report". It also meant that he had to rely upon the cash flow projections contained in HSH Nordbank's business plan dated as of 1st September 2009 without doing any work to satisfy himself about the reasonableness of these projections. Given that he has adopted a discounted cash flow valuation methodology, this is an important qualification. Nor has Mr Taylor been able to consider the reasonableness of these cash flow projections because the business plan has not been disclosed to the Lenders on the ground that it is a confidential document.

20 Having given careful consideration to the valuation evidence, I have reached the following conclusions. First, it seems to me that all four of the Companies are probably balance sheet

insolvent, in that the realisable value of their assets is *currently* less than the amount of their liabilities. Second, I think that I am bound to recognise that there is at least a possibility that the Companies will become balance sheet solvent at some point in the future, if and when HSH Nordbank returns to profitability. I must then ask myself what is the relevance of these conclusions ? I am bound to have regard to the wishes of the creditors and, in my judgment, what matters is the Lenders' view of this evidence, rather than mine. I am supported in this conclusion by *Re Falcon R.J. Developments Ltd (1987) 3 BCC 146.* This was a case in which the English High Court was called upon to decide whether, if a voluntary winding up had commenced before the hearing of a petition, a compulsory order should be made if supported by independent creditors with the largest stake in the outcome, and if so, what weight should be given to the opposing views of directors and others associated with the company. Vinelott J. said (at page 155):

"I can see no reason why the views of the majority as to what is in their best interest should not prevail. There is no reason why the court should impose on them its own view as to what is in their best interests. That is a commercial decision."

I endorse this statement of principle. It is not for me to tell the Lenders what is or is not in their commercial interest. I am entitled to assume that they have given consideration to the Companies' valuation evidence. Their collective view of the matter is expressed by Mr Fillmore as follows :-

"The confidence with which Mr Flowers asserts that an IPO of HSH will take place in 2013 and that the HSH share price will improve dramatically cannot be relied upon. There is not, as Mr Flowers seems to imply, any certainty that the HSH share price will increase in the near to mid-term. This view is supported by the statements made by Mr Belsham in his second affidavit dated 14 December 2009, in which he states that if the European Commission's investigation results in the unwinding of the recapitalisation of HSH that took place in June 2009 (which cannot be ruled out) a new recapitalisation would need to take place at a lower subscription price and this could result in HSH not being able to continue as a going concern (Belsham Two paragraph 16(d)). This would not just decrease the value of the HSH share price, arguably it may put it into liquidation. HSH is also a well known lender in the shipping and commercial real estate sectors and the possibility that additional losses may occur in these sectors directly impacting the equity value of HSH cannot be discounted. Given the uncertainty in the financial markets, the Lenders are seeking to wind up the Companies as soon as possible while the HSH shares have any value at all."

Even if I thought that the Companies were balance sheet solvent, that would not be an exceptional circumstance or special reason for refusing to make an immediate winding up order.

A sale by an official liquidator will be destructive of intrinsic value

21 Counsel emphasised the argument that a sale of the Companies' shares by an official liquidator will be immensely "destructive of value". What Counsel means by this submission is that the intrinsic value of the Companies' shares which could be realised in an IPO, assuming that HSH Nordbank is restored to profitability and its recapitalisation is not unwound by order of the European Commission, is potentially far greater than the amount which could be realised from the sale of the shares in today's market. This submission is self evidently true. It seems to me that the sale of an illiquid minority interest is always bound to realise less than the intrinsic value which would be realised through the mechanism of an IPO or a takeover bid. A sale of the minority interest will always be destructive of *potential* value in this sense. However, the proposition that a winding up order made in respect of these Companies will be destructive of potential intrinsic value in 3 or 4 years' time is quite different from the proposition that it will be destructive of actual market value today.

22 The *Duff & Phelps Report* addresses the difficulties associated with marketing the shares in HSH Nordbank today. It seems to me that some of these difficulties are inherent in this particular investment. Others are associated with the very difficult market conditions currently prevailing. Mr Bartell's conclusion (at page 15 of the Report) is that "we estimate that the discount associated with such a forced sale in the current market would be within the range of 60 to 80 per cent of the long term going concern value of the Bank ...". If one take's Mr Erb's valuation of €30 per share as the long term going concern value of HSH Nordbank, a discount of 60% to 80% points to a current market value in the region of €6 - €12 per share. From the Lenders' perspective, €12 per share comes close to a full recovery and €6 per share equates to a 50% recovery.

23 There is no authority for the proposition that the Court can properly exercise its discretion by refusing to make a winding up order in respect of an admittedly insolvent company, on a petition supported by *all* of its creditors, at the request of its shareholders merely because they believe that the value of its assets may increase sufficiently at some point in the future, such that they will recover at least part of their investment. The authorities point to exactly the opposite conclusion. The possibility that a company's sole or main asset may increase in value of the next 3 or 4 years as a result of extraneous factors (in this case an improved financial performance on the part of HSH Nordbank and improved market conditions) is not an exceptional circumstance or special reason which justifies refusing a winding up order or staying proceedings on a petition against the wishes of a majority or, as in this case, all of its creditors.

24 *Re Demaglass Holdings Ltd* [2001] 2 BCLC 633 is authority for the proposition that the Court might properly exercise its discretion by adjourning a petition for a short period if it can be demonstrated that the order itself would be destructive of current market value in respect of an asset which is materially important to the financial outcome of a liquidation. It is helpful to summarise the facts of that case in order to illustrate the point. The company carried on the business of manufacturing and distributing commercial glassware to hotels and restaurants. The company's bank, which was its single largest creditor, appointed administrative receivers pursuant to a debenture. Shortly thereafter, a trade creditor presented a winding up petition. The petitioner's argument was that the court should make a winding up order and appoint official liquidators in place of the administrative receivers. The concern was that the receivers, in carrying out their primary function of protecting the bank's interests, had or might under-estimate the value of the company's stock or sell it for less than its proper value. The evidence established that the making of an immediate winding up order would have the opposite effect. The receiver was carrying on the company's business, albeit for the limited purpose of selling the stock using its own sales force, which comprised 30 employees. He anticipated that he needed a further 10 weeks in which to complete the stock sales operation. The Court accepted the receiver's evidence that a substantially lower price would be likely to be realised if the company were put into liquidation immediately, with the consequence that it would cease to trade and the contracts of employment of its sales force would be automatically terminated. The receiver said that the stock was too large for the market to absorb all at once, so that a severely discounted price would likely result, especially if an official liquidator did not have the assistance of the existing sales force. The 10 week adjournment sought by the receiver was granted because (a) it was supported by a majority of the creditors and (b) the court accepted that it was definitely more likely than not that the sale of the remaining stock would achieve a significantly higher price if the receiver were allowed to continue to sell it over a 10 week period with the assistance of an experienced sales force, rather than putting it all on the market at once. The court observed that it was almost certain to make a winding up order at the end of the 10 week adjournment. This case is not authority for the proposition that a petition can properly be adjourned on the basis that there are grounds for believing that, for whatever reason, the potential realisable value of an important asset might increase over time.

25 A series of other points are made in support of the argument that a sale by of the shares by official liquidators will be difficult and "destructive of value" First, the Companies rely upon the fact that under HSH Nordbank's articles of association a transfer of shares requires consent from the other shareholders and Mr J.C. Flowers expresses the view that such consent is unlikely to

be forthcoming for most potential purchasers. In particular, he says that the bank is unlikely to welcome a purchase by a competitor or a "vulture fund". He may be right, but the Lenders must have been well aware of this restriction when they entered into the Credit Facility Agreement and they are aware of it now. It is not unusual for official liquidators to deal with the realisation of shares or other assets which are subject to various kinds of restrictions. By itself, this fact cannot possibly constitute an exceptional circumstance which would justify the refusal of an immediate winding up order.

26 Second, the shareholders of HSH Nordbank are parties to a shareholder agreement (described as "the Principle Agreement") executed in March 2003. As a condition of consenting to a transfer, any new shareholder will be required to become a party to the Principle Agreement, as the Shareholder Entities did in October 2006. It gives them the right to representation on the bank's supervisory board of directors. Mr S.K. Gauke, the Shareholder Entities' German lawyer, expresses the opinion that the consequence of making a winding up order is that "the opening of insolvency proceedings with respect to the assets of a shareholder being party to the Principle Agreement could result in an automatic dissolution of the entire Principle Agreement". He proceeds on the assumption that the Companies are not themselves the shareholders and assumes that a winding up order in respect of them would trigger an automatic dissolution of the Limited Partnerships under Alberta Law. The Petitioners do not agree with this analysis. However, assuming Mr Grauke is right, what is the relevance of the point for present purposes ? At worst, the Companies will cease to be represented on the supervisory board. Given that I have no evidence from HSH Nordbank or any of its other shareholders, it is impossible to know how they will respond to an automatic termination of the Principle Agreement, except that they can be expected to do whatever is in their best commercial interest. I am not prepared to assume that the bank, its management and other shareholders will adopt an adversarial approach towards the official liquidators.

27 Third, there is the point about the European Commission's investigation to which I referred in paragraph 9 above. The nature and possible outcome of this investigation is explained in the affidavit of Mr. S.K. Grauke, who was first retained by J.C. Flowers & Co in connection with the share acquisition in 2006. At the time of swearing his affidavit, Mr Grauke envisaged that a final decision would be made by the European Commission at the end of January or beginning February 2010, although he could not exclude the possibility that the Commission might ask for more information in which case the process could continue for several more months. I infer that no decision had been made by the time of the hearing, otherwise I would have been told about it.

If the Commission concludes that the second recapitalisation did involve the provision of unlawful "state aid", the beneficiaries of it (which necessarily includes, but is not limited to, HSH Nordbank itself) could be required to repay it, in which case they will have rights of appeal which might take 3-4 years to conclude. What relevant conclusion can be drawn ? At best, the European Commission might have ruled in favour of HSH Nordbank by the time I publish my judgment. At worst, it will rule that the second recapitalisation has to be unwound in some way, which may in turn lead to appeals lasting for several years. The worst case scenario probably will have an adverse impact upon the marketability of the shares. However, the mere fact that the marketability and value of a company's sole or principal asset is or may be adversely affected by events outside the control of its official liquidator, is not a reason for refusing to make a winding up order.

The current management is best placed to retain value in the shares

28 The Companies argue that an official liquidator would be "considerably less well placed to maintain the value of the shares" than if the Companies were to remain under the control of their existing management, meaning the current team of professional service providers. The Companies do not have any employees. Whether or not the current value of the shares improves, declines or is maintained depends upon the performance of HSH Nordbank. It is said that J.C. Flowers & Co will bring to bear expertise and influence which will somehow have a positive effect and that it is implausible to think that official liquidators will have the ear of the bank's management. Even if this is true, it cannot possibly constitute an exceptional circumstance which would justify refusing to make a winding up order. The proposed official liquidators are experienced insolvency practitioners and they will be expected to engage the services of appropriately qualified and experienced professionals to advise in connection with the marketing and sale of the shares. As Vinelott J. said in *Re Falcon R.J. Developments Ltd* , "the majority of outside creditors, ... are entitled to say, faced with a choice between a compulsory winding up and a voluntary winding up conducted by a man chosen and put into office by [its directors] they prefer a compulsory winding up." The point applies with even greater force in the present case. Without in any way questioning the expertise and experience of J.C. Flowers & Co, the creditors are entitled to say that they prefer to rely upon official liquidators, who can be expected to engage the services of a new and independent team of professional advisers.

Compromise is the best and inevitable result

29 Given all the various difficulties and obstacles identified by the Companies' counsel, the Court is asked to conclude that "compromise is the best and inevitable result" and that it can and should

be achieved through a Chapter 11 proceeding commenced in the US Bankruptcy Court for the District of Delaware. This Court recognises that the supervised reorganisation of an entity under Chapter 11 can, and often does, produce for creditors a result which is commercially preferable to that which might be produced by a liquidation. It was open to the Companies to seek similar relief by presenting a petition and applying under section 104(3) of the Companies Law (2009 Revision) and CWR Order 4, Part II. This type of procedure is best suited to the situation in which there are multiple creditors and/or shareholders. However, in the circumstances of this case I consider this proposal to be wholly unrealistic and impractical.

30 There are essentially only "two parties in interest". On the one hand there is the syndicate of seven banks acting in concert through their facility agent. For all practical purposes, they constitute the entire body of creditors. On the other hand, there are the four Companies, also acting in concert through their common investment adviser, J.C. Flowers & Co. The fact that the Companies are articulating the interests of the limited partners and their ultimate beneficial owners reflects the commercial realities of the matter and I do not regard it as a point of criticism. Thus, I approach the "Chapter 11 argument" on the basis there are just two groups of parties, each acting in concert. (I use the expression "the parties" as a convenient shorthand in this context). The evidence is that these two parties have been engaged in discussions since mid 2008 when HSH Nordbank's financial difficulties first became apparent. They have been actively negotiating a restructuring agreement from January 2009 onwards. Offers and counter-offers have been put forward and rejected. The parties failed to reach agreement and the Petitioners were perfectly entitled to present their petitions when they did in September of last year. In these circumstances I fail to see how it would now serve any useful purpose for me to force the parties into a Chapter 11 proceeding in Delaware or to impose a similar process upon them in this Court, through the mechanism of appointing provisional liquidators and giving directions under CWR Order 4, Part II. The fact that the relationship between the parties has deteriorated during this period to the point at which allegations of bad faith are being asserted, reinforces the futility of a Chapter 11 proceeding.

31 On 27th January 2009 the Companies' representative (Mr Sinha of J.C.Flowerrs & Co) informed Mr Fillmore that they had "20 million" in cash available for debt service. He assumed (rightly as it turned out) that this meant US$20m rather than €20m. However, at a meeting in London on 30th January Mr Sinha said that no part of this cash would be used to pay what had admittedly fallen due that day under the Loan Facility Agreements. Not only did the Companies continue to refuse to use their available cash to pay debts which were properly due and owing, the evidence

available to the Lenders was that most of it had been disbursed because it is no longer reflected in the financial statements of the Limited Partnerships for the period ended 30th September 2009. Given that the Companies are special purpose vehicles which have no business other than owning the shares and servicing their debt, it is not surprising that the Petitioners drew the inference that this money had been improperly diverted and that the Companies' directors are in breach of their fiduciary duties. A full explanation of the source and application of this cash is contained in Mr Belsham's 5th Affidavit (at paragraphs 13-29) which was sworn on the first day of the trial. This evidence reflects that sums of approximately US$11.8m, US$5.1m, US$672,000 and US$5.3m stood to the credit of the respective limited partners in their personal bank accounts maintained with JP MorganChase Bank as at 22nd January 2010. It is not necessary for me to express any view on whether or not this evidence leads to the conclusion those who ultimately control the Companies and the Limited Partnerships were improperly attempting to put partnership assets outside the reach of the general partners and their creditors. Suffice it to say that the relevant information was not disclosed until the day before the trial of the petitions and then only in response to an allegation of impropriety. On any view, conduct of this sort is hardly conducive to achieving a consensual resolution of the matter.

32 As I have already noted in paragraph 10 above, the Companies commenced proceedings in the English High Court on the day before the petitions came on for hearing before Foster J. If the Companies and their advisers genuinely believed that the debts were not due and payable because of some estoppel argument, that could have been raised as a defence to the petitions. The Petitioners' suspicion that the English proceeding was merely a spoiling tactic tends to be confirmed by the fact that it was never served and the argument has now been dropped. This appears to be an example of commercially illegitimate behaviour on the part of the Companies and the investors who stand behind them. I also tend to view the amendment of the partnership agreements and the appointment of new general partners in the same light.

33 On 29th May 2009 Mr Sinha telephoned Mr Fillmore and offered to buy the outstanding indebtedness for 10% of its face value. Mr Fillmore says (in paragraphs 21-26 of his 5th Affidavit) that this offer was made in full and final settlement, with no offer of upside participation in the event that the Companies' optimistic view of HSH Nordbank's forecast performance turns out to be justified by future events. The Lenders rejected this offer as derisory. Its significance for present purposes is that it is reflective of the Companies' attitude towards their bankers. Ten percent of face value of the indebtedness translates to about €1.23 per share. Even on the most pessimistic view expressed by Mr Erb of Susat & partner OHG, this was perhaps as little as a

quarter of what they probably thought the shares were worth. On the most optimistic view expressed by Mr Bartell of Duff & Phelps, it might have been as little as a tenth of the current market value. It is difficult to see why the Companies would seriously expect the Lenders to accept 10 cents on the Euro. Again, it is another incident which tends to suggest that the time for negotiation is past.

34 The Companies' case is that the current indicative fair value of the shares is about €19, albeit without any minority discount, and Mr J.C. Flowers confidently predicts that €30+ will be realised in an IPO in 3 or 4 years time. In the light of this submission I asked Counsel why his clients had "chosen not to re-finance their debts". He rightly pointed out that there is no evidence that they had "chosen" not to re-finance. There is in fact no evidence about this subject at all, which is a little odd. If the Companies and their advisers' confidently expressed belief about the likely future realisable value of these shares is realistic, one might have expected them to have at least investigated the possibility of re-financing the debt, in which case I would expect to read something about the outcome in one or other of the many affidavits. The absence of any evidence on this subject does tend to support the view expressed by the Petitioners' counsel that they are simply attempting to place a "one way bet" if they can get away with it.

35 The procedures and benefits of a Chapter 11 proceeding are explained in the 1st Affidavit of Mr Mark D. Collins, a Delaware bankruptcy lawyer whose firm has been retained by the Limited Partnerships. The Limited Partnerships are said to be "debtors" within the meaning of section 109 of the Bankruptcy Code, and therefore eligible to file proceedings under Chapter 11, because they each have "property in the United States", namely credit balances on bank accounts with JP MorganChase. Bank. No bank statements are exhibited either to Mr. M.D. Collin's 1st or 2nd Affidavits. The bank accounts discussed in paragraph 25 of Mr D.K. Belsham's 5th Affidavit (and the copy statements comprised in Exhibit DKB-4) clearly relate to accounts in the names of the limited partners, not the Limited Partnerships. These statements reflect the amounts distributed to them by the Limited Partnerships. Presumably some other, as yet undisclosed, accounts have been established in the names of the Limited Partnerships and/or the Companies with JP MorganChase Bank in order to satisfy the requirement to have property in the United States, without which they will not be "debtors" within the meaning of section 109.

36 In my judgment, the fact that the Limited Partnerships and/or the Companies are entitled to treat themselves as "debtors" eligible to invoke the Chapter 11 jurisdiction by the simple mechanism of establishing bank accounts with JP MorganChase Bank in New York cannot, by itself, possibly constitute an extraordinary circumstance or special reason why this Court should adjourn or stay

winding up proceedings. It is, after all, open to any and every Cayman Islands company to open a bank account in New York. There must be something more. As I minimum, I would want to see this course of action supported by a substantial majority of independent creditors before I would exercise the Court's discretion in this way. In this case, it is opposed by *all* the independent creditors and the amounts owing to the related party creditors who can be expected to support their clients' case is de minimis.

37 I would also expect to see some evidence from which to infer that a Chapter 11 proceeding (or some similar procedure in this or some other jurisdiction) would be likely to produce a positive result which is capable of becoming binding upon all the creditors. There is no such evidence in this case. No reorganisation plan was filed by the Limited Partnerships. No draft plan has been submitted to this Court. I appreciate that the applicable rules allow a debtor 120 days within which to formulate and file a reorganisation plan, but if these Companies (and the investors who stand behind them) were serious about putting forward another restructuring proposal rather than simply "buying more time", I would have expected them to formulate a new proposal which goes some way towards meeting the Lenders' concerns expressed during the course of negotiations which have been going on at least since January 2009. There is no basis upon which I can sensibly infer that the procedures of a Chapter 11 proceeding will lead a majority of the Lenders to change their minds. The evidence of Mr Mark D. Collins is that the US Bankruptcy Court cannot impose a reorganisation plan unless it is approved by a majority of the independent creditors, holding at least two-thirds of the debts. (1st Affidavit, paragraph12(e)(iv).) Currently, the restructuring proposals put forward by the Shareholder Entities have been unanimously rejected.

CONCLUSION

38 I have read and given careful consideration to a large volume of written evidence, much of which is directed at difficult valuation issues and points of foreign law. However, in the final analysis, this is not a complicated case. The Companies are admittedly insolvent. Having engaged in restructuring negotiations over a period of many months, the Petitioners now seek an immediate winding up order and are supported by the whole body of independent creditors. The underlying investors (whose views are being articulated through the Companies) are "under water" and seek to delay a winding up for as long as possible in the hope that HSH Nordbank's financial condition will be restored to such an extent that there will be an IPO in 3 or 4 years' time, in which case they should recover part of their investment. From the investors' perspective, this is the obvious strategy. It preserves the potential for upside benefit, but without any further downside risk. As a matter of law, I am bound to give greater weight to the views of the creditors. The Lenders are

unanimously of the view that it will be in their commercial interest to put the Companies into liquidation now. The evidence suggests that the Lenders can expect a recovery, albeit probably not a full recovery. In these circumstances, I am satisfied that the Petitioners are entitled to winding up orders in respect of each of the Companies.

39 The nominated liquidators are Messrs Walker and Stokoe who respective a partner and director of the Cayman Islands firm of PricewaterhouseCoopers ("PWC, Cayman"). The procedural and evidential failings identified in the Court of Appeal's judgment have been cured and their credentials have been properly established. However, the Companies now complain for the first time that Messrs Walker and Stokoe do not meet the independence requirement because the German firm of PricewaterhouseCoopers ("PWC, Germany") were engaged by the management board of HSH Nordbank some time in 2009 to determine the indicative business value for HSH Nordbank as at 31st March 2009. This was done for the purposes of the second capitalisation which took place in June 2009. PWC Germany's role was first raised in correspondence at the beginning of January 2010 and is discussed by Mr D.K. Belsham, J.C.Flowers & Co's European legal counsel, in paragraph 44 of his 5th Affidavit. I infer that he must have known about PWC Germany's role long before these petitions were presented in September 2009, but the point was not taken when the matter came before Foster J. Nor was it raised before the Court of Appeal. PWC Cayman's response, set out in paragraphs 6-23 of Mr Stokoe's 7th Affidavit is highly instructive and worth summarising in some detail.

40 In August 2009 Mr Fillmore formally approached Mr Schwarzmann, who is the leader of the Business Recovery Services practice of the United Kingdom firm of PricewaterhouseCoopers ("PWC UK"), to find out whether PWC UK and/or PWC Cayman would be able to act as official liquidators of the Companies. PWC UK, PWC Cayman and PWC Germany are all member firms of PricewaterhouseCoopers International Limited ("PWC International") which is colloquially referred to as the "PWC network". Mr Stokoe's evidence is that its member firms employ some 150,000 people in 150 countries. In response to Mr Fillmore's enquiry, PWC UK carried out an independence and conflicts check in accordance with the firm's risk management protocol. At that stage the intention was that Mr Schwarzmann of PWC UK would be nominated for appointment as official liquidator jointly with Mr Walker of PWC Cayman. PWC Cayman relied upon PWC UK to perform the client pre-acceptance procedures. These procedures are conducted internationally with the co-operation of all the network firms. Every potential new engagement is referred to PWC UK's Risk Management Team for investigation. It then refers the matter to the Project Acceptance Committee which is headed by a partner and meets every day. The Project Acceptance

Committee applies the Code of Ethics issued by the United Kingdom Joint Insolvency Committee. Whilst insolvency practitioners qualified to practice in the Cayman Islands may not be bound by this Code of Ethics, it is regarded by this Court as appropriate guidance to which they should have regard.

41 As one would expect, this procedure revealed to PWC UK and PWC Cayman that PWC Germany had performed valuation work for HSH Nordbank earlier in the year. Neither PWC UK or PWC Cayman participated in this work. Nor do their partners and staff have access to PWC Germany's working papers. The report itself is a confidential document. Mr Stokoe's evidence is that on 21st August 2009 the Project Acceptance Committee determined that PWC UK and/or PWC Cayman could accept the potential engagement and that their partners could accept appointment as official liquidators. Given the lapse of time and the complaint raised by the Companies, Mr Stokoe rightly decided that the original decision should be reviewed and updated. He sent the relevant documents to PWC UK's Risk Management Team. The original decision that PWC Germany's role will not present any real threat to the objectivity of Messrs Walker and Stokoe of PWC Cayman was confirmed. In the light of this evidence, I accept that Messrs Walker and Stokoe are independent as regards the Companies for the purposes of Regulation 6.

42 The Companies also complain that Messrs Walker and Stokoe lack relevant experience. This point is made opportunistically and arises out of the fact that the Petitioners originally intended to nominate Mr Walker (of PWC Cayman) for appointment jointly with Mr Schwarzmann (of PW UK). For reasons which are explained in my previous ruling, this turned out not to be possible. In response to this complaint, Messrs Walker and Stokoe have submitted their curriculum vitae which reflect lengthy experience of dealing with a variety of insolvency and restructuring matters. Quite apart from this evidence, the Judges of the Financial Services Division of this Court necessarily have first hand knowledge of the capabilities and experience of individual insolvency practitioners and the firms of which they are partners. Whilst Mr Stokoe has worked in this jurisdiction for a relatively short time and his experience has been gained in the United Kingdom outside the financial services sector, Mr Walker and his firm have been appointed by this Court in similar matters on many previous occasions. It is also relevant to note that they will be entitled to engage independent expert consultants to assist with the marketing and sale of the Companies' shares in HSH Nordbank and they could of course engage Mr Schwarzmann as a consultant if they thought it appropriate to do so.

43 I am satisfied that I can properly appoint Messrs Walker and Stokoe of PWC Cayman as joint official liquidators of each of the Companies and I make orders accordingly.

44 I will hear Counsel on the question of costs and any other consequential matters which they may wish to raise.

Dated 12th February 2010

The Honourable Mr Justice Andrew J. Jones QC

GRAND COURT CAYMAN ISLANDS