IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

CAUSE NO: FSD 68 OF 2019 (NSJ)

IN THE MATTER OF SECTIONS 15 & 86 OF THE COMPANIES LAW (2018 REVISION)

AND IN THE MATTER OF THE GRAND COURT RULES 1995 ORDER 102

AND IN THE MATTER OF CHINA AGROTECH HOLDINGS LIMITED (IN LIQUIDATION)

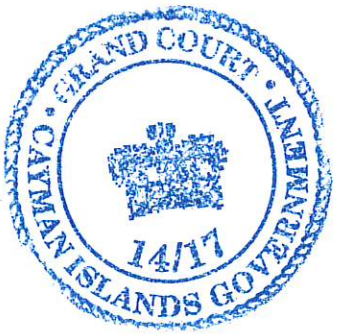
JUDGMENT ON APPLICATIONS TO CONFIRM CAPITAL REDUCTION AND CAYMAN SCHEME

Appearances: **Mr. Jayson Wood of Harney Westwood & Riegels for the Company and the liquidators**

Hearing date: **16 July 2019**

Draft judgment: **18 July 2019**

Judgment delivered: **22 July, 2019**



Introduction

1. On 16 July 2019 I heard two applications (together the ***Applications***) made by China Agrotech Holdings Limited (in liquidation) (now Da Yu Financial Holdings Limited) (the ***Company***) acting by its Hong Kong liquidators. The Company's liquidators are Stephen Liu Yiu Keung and David Yen Ching Wai (***Mr Yen***) of Ernst & Young Transactions Limited. The Company and the liquidators were represented at the hearing by Mr. Jayson Wood of Harney Westwood & Riegels (***Harneys***).

2. The first application was for an order confirming a capital reduction under sections 15 of the

Companies Law (2018 Revision) (the ***Companies Law***). The second application was for an order sanctioning a scheme of arrangement between the Company and its creditors under section 86 of the Companies Law.

3. The Company is incorporated in the Cayman Islands and the liquidators were appointed by the Hong Kong court on 17 August 2015. The Company's shares were listed on the Main Board of the Hong Kong Stock Exchange (but trading in the shares has been suspended since 18 September 2014).

4. The capital reduction and the scheme are part of a post liquidation restructuring of the Company. The liquidators have negotiated a series of agreements and arrangements that, if implemented, will result in the Company being able to continue as a going concern (and retain and realise the value of its Hong Kong listing) and result in the termination of the winding up proceedings. The Company and the liquidators have promoted schemes of arrangement with the Company's creditors in this Court and in Hong Kong and are seeking this Court's confirmation of the reduction of capital.

5. At the end of the hearing I made orders confirming the capital reduction and sanctioning the scheme (but providing, in relation to the latter, that the order only be sealed in circumstances described below). I indicated that I would give my reasons in writing, which I now do.

The background

6. The background to the capital reduction and scheme is set out in my judgment dated 16 July 2019 (the ***Judgment***).

7. The Judgment dealt with a dispute concerning the validity of the resolutions voted on at an extraordinary general meeting of the Company held on 22 May 2019 (the ***EGM***). One of the resolutions was a special resolution approving the capital reduction. The validity of the resolutions had been challenged by a shareholder of the Company, Perfect Gate Holdings Limited (***Perfect Gate***), who voted against the resolutions. The Company and the liquidators applied by summons dated 12 June 2019 (the ***Summons***), for a declaration that the resolutions proposed at the EGM had been validly passed and that the decision of the chairman at the EGM (Mr. Yen) to disallow Perfect Gate's votes and to declare the resolutions as passed was binding and effective. I granted the

Company's application for a declaration and made an order that the resolutions proposed at the EGM were validly passed as declared by the chairman at the meeting.

8. The procedural history of the Applications is also set out in the Judgment. I would note that my order directing that a meeting of creditors be convened to consider and vote on the Cayman scheme was made on 30 April 2019 (the ***Convening Order***).

The proceedings in Hong Kong

9. The Company's (and the liquidators') application to the Hong Kong court to sanction the Hong Kong scheme is listed to be heard on 22 July 2019. That application is opposed by Perfect Gate. At the hearing I asked Mr Wood to explain the basis on which Perfect Gate considered that it had standing to oppose and the grounds on which Perfect Gate opposed the Hong Kong sanction application. He told me that he was unable to provide details to the Court since Perfect Gate's case had yet to be fully particularised. Perfect Gate is not required to file its further skeleton argument until 4.30pm Hong Kong time on 18 July 2019. Although Perfect Gate has clearly already filed a skeleton argument and should have filed further evidence by 12 July, copies of these documents were not provided to the Court or their contents explained. In any event, Mr Wood confirmed that Perfect Gate had not notified the Company and the liquidators that it opposed the application to sanction the Cayman scheme. Nor had it notified the Company and the liquidators that it opposed the application to confirm the capital reduction. Perfect Gate had not given notice of its opposition or made an application to oppose the sanction of the Cayman scheme or the capital reduction.

10. There are three further applications before (or about to be issued in) the Hong Kong court. Details of these proceedings were provided by Mr. Greig of Harneys in his Fourth Affirmation dated 15 July 2019. First, as I explained in the Judgment, on 26 June 2019 Perfect Gate issued an originating summons against the Company and Mr. Yen seeking a declaration that Mr. Yen's decision as chairman at the EGM to exclude its votes was unlawful and that the purported special resolution proposed at the EGM was also unlawful (***Perfect Gate's Application for Declaratory Relief***). Secondly, Mr. Yen intends to file a summons to strike out Perfect Gate's Application for Declaratory Relief (the ***Strike Out Summons***) on the basis that it is bound to fail since Perfect Gate is bound by the Judgment (which deals with the validity of the EGM resolutions) and because it is an abuse of process for Perfect Gate to seek to re-litigate matters which have been conclusively determined by this Court. Thirdly, Perfect Gate has applied for retrospective leave to bring Perfect

Gate's Application for Declaratory Relief against the Company. Directions are to be sought at the 22 July hearing in relation the further conduct of these three applications.

11. Various documents were exhibited to Mr. Greig's Fourth Affirmation. These included the Company's announcement dated 11 July 2019. In that announcement the Company notified shareholders of the Judgment and provided an update on the status of the Hong Kong proceedings together with a revised expected timetable for the proposed restructuring. The announcement also dealt with the possibility and impact of possible further applications by Perfect Gate in relation to the Judgment. The announcement stated that:

> *"In the event that Perfect Gate makes an application for leave to appeal the [Judgment] or order [sic] for suspension of execution of the [Judgment] by 23 July (Cayman Islands time), the Company will announce its withdrawal of the [public offer] by 25 July 2019. Refund cheques in respect of the [public offer] will be despatched to the applicants within five Business days from the announcement. In the[se] circumstances, the entire Proposed Restructuring will lapse and the Liquidators will proceed to conclude the liquidation and the Company will be dissolved."*

12. At the hearing, I sought clarification of the timetable and the Company's expectations regarding the closing of the post liquidation restructuring. Mr. Wood informed the Court that he understood that in order for the restructuring to be completed within the timetable laid down by the Hong Kong Stock Exchange and the Hong Kong Securities and Exchange Commission it was necessary for the sanction of the Cayman scheme, the sanction of the Hong Kong scheme and the confirmation of the capital reduction to be given by 24 July 2019. Mr Wood said that if this was done, and Perfect Gate did not take the steps set out in the 11 July announcement, then the restructuring would be successfully completed. The Company and the liquidators were proceeding on the basis that this would happen. Mr Wood also explained that there had been discussions with the Hong Kong authorities regarding the process and timetable for issuing and listing the new shares in order to expedite the process and ensure that the very tight timetable for completing the necessary steps could be met. It was important that the various preliminary steps that needed to be completed before the new shares could be issued, including the confirmation of the capital reduction, be taken without any delay. For that reason, it was important that the order confirming the capital reduction was made at the end of or as soon as possible following the hearing (and on an unconditional basis).

Confirmation of the capital reduction – the law

13. The statutory provision permitting a reduction of capital is contained in section 14 of the Companies Law which provides that:

> "*Subject to …… confirmation by the Court, a company limited by shares ... and having a share capital may, if so authorised by its articles, by special resolution reduce its share capital in any way...*".

14. Section 16(1) of the Companies Law provides:

> "*The Court, if satisfied with respect to every creditor of the company who under section 15 is entitled to object to the reduction, that either his consent to the reduction has been obtained or his debt or claim has been discharged or has determined, or has been secured, may make an order confirming the reduction on such terms and conditions as it thinks fit.*"

15. The Company and the liquidators relied on the following statement in the judgment of Jones J in *In re Santiago Pipelines Company & New Santiago Pipelines Company* [2012 (2) CILR 343] at [12-14] of the matters that the Court will take into account when exercising its discretion under section 16(1):

> "*12. The statutory purpose of ss. 15 and 16 of the Companies Law (which are based upon ss. 66 and 67 of the English Companies Act 1948) is creditor and shareholder protection. It was well established that an English court should exercise its discretion in favour of confirming a special resolution for a reduction of share capital if the following three criteria were satisfied. First, the shareholders (or different classes of shareholders) must be treated equitably, although equitable treatment does not necessarily mean equal treatment. Secondly, in circumstances where the company must convene an extraordinary general meeting of its shareholders, the purpose and effect of the proposed capital reduction must be properly explained to them in a circular letter or explanatory memorandum delivered with notice of the meeting, such that they are able to make an informed decision about the merits of the proposal. Thirdly, the court must be satisfied that the interests of creditors are unaffected or properly safeguarded. In the circumstances of these cases the question of shareholder and creditor protection does not arise...*
>
> *13. Based upon two judgments of Harman, J. in Re Ratners Group Plc (4) and Re Thorn EMI Plc (5), it is now accepted, both as a matter of English law and Cayman law, that there is a fourth criteria. I have to be satisfied that the capital reduction is being done for a "discernible purpose" but this court has never explained exactly what this means ...*
>
> *14. It is now said, as a matter of general principle, that the court must be satisfied in every case that a special resolution to reduce share capital has been passed for a "discernible purpose" (see In re ING Secs. (Japan) Ltd. [2004-5 CILR 308] and In re China.Com Inc. [2009 CILR 384]). In the Cayman context, this means more than merely satisfying the court that the Petitioner has some actual objective in mind and that the capital reduction is not*

merely an academic exercise which might or might not serve some useful purpose in the future. It means that the court must have a proper understanding of the commercial rationale for the overall transaction of which the capital reduction forms part. Clearly, it is no part of the court's role to second guess the commercial judgment of a company's directors and shareholders but the evidence must demonstrate that they are seeking to achieve some legitimate commercial purpose ..." (emphasis added)

16. During the hearing I referred Mr. Wood to the following helpful and recent summary of the position (under English law) set out in the judgment of Mr. Justice Snowden in *Re Man Group plc* [2019] EWHC 1392 (Ch) at [11] and [12].

> *"11. In relation to a reduction of capital, the Court will require satisfaction of the following matters,*
>
> *a) The resolution reducing capital must be a validly passed special resolution.*
>
> *b) The shareholders must be treated equitably in relation to the reduction. Shareholders do not all have to be treated in the same manner provided that any unequal treatment is either in accordance with the rights attached to any class or the consent of those affected by such treatment has been properly obtained.*
>
> *c) The proposals must have been properly explained to the shareholders so that they can exercise an informed judgment upon them.*
>
> *d) The creditors of the company must be safeguarded so that the proposals do not operate to their detriment, namely that there is a real likelihood that the reduction itself would result in the company being unable to discharge the debts when they fall due.*
>
> *e) The reduction must be proposed for a discernible purpose."*
>
> *12. Proposition (a) above arises from the wording of section 641(1)(b). Propositions (b), (c) and (d) are derived from the judgment of Harman J in Re Ratners Group plc [1988] BCLC 685 at 687b-d, with the judgment of Norris J in Re Liberty International plc [2010] 2 BCLC 665 at para. 11 supplementing proposition (d). Proposition (e) is derived from the judgment of Harman J in Re Thorn EMI Plc [1989] BCLC 612 at 616d."*

Confirmation of the capital reduction – the Company's submissions

17. The Company and the liquidators submitted that all five requirements (that is the four requirements identified by Jones J together with the first requirement identified by Snowden J) were satisfied in the present case:

(a) the first requirement was satisfied because the Judgment had determined the validity of special resolution approving the capital reduction. Mr. Wood submitted that while the time

period within which Perfect Gate could seek permission to or lodge an appeal of the Judgment had not yet expired, no such application had yet been made by Perfect Gate nor had Perfect Gate applied for a stay of execution of the Judgment or for an adjournment of the hearing of the Company's application for a confirmation order. The Court should regard the special resolution as having been validly passed and in the absence of an application by Perfect Gate the Court should not delay making the confirmation order.

(b). the second requirement was also satisfied since the capital reduction related only to ordinary shares and applied to each shareholder equally in proportion to the number of shares they hold. All of the shareholders will suffer an equal pro-rata dilution of their holdings, but at the same time they will equally enjoy any value add that the restructuring will bring to their shares. Shareholders were treated fairly. Further and importantly, the capital reduction itself will not adversely impact shareholders. It did not involve a reduction in the Company's equity, there was no diminution of any liability in respect of unpaid share capital (because there was none) and there was no return of capital to shareholders. The credit in the balance sheet arising from the capital reduction will be applied to eliminate an equivalent amount of the accumulated losses of the Company. The capital reduction left the shareholders with proportionately the same number of shares. That will only change if the scheme is approved and the capital reorganisation is implemented.

(c). the third requirement was satisfied because a proper explanation of the capital reduction and the capital restructuring had been provided to shareholders. The Company had sent a detailed and comprehensive circular to shareholders (of more than 600 pages) containing full information concerning the overall restructuring. It was made clear in the circular that the purpose of the capital reduction was to further the Company's post liquidation restructuring with a view to the Company being able to continue to trade (with a reduced debt burden) and to avoid the liquidators having to continue the liquidation and realise the Company's assets (resulting in no recovery for shareholders). The circular had clearly explained the effect of the capital reduction (and the capital reorganisation) on the Company's existing shareholdings.

(d). the fourth requirement was satisfied since the capital reduction itself had no impact on creditors. The assets of the Company will remain intact (with no return to shareholders). Creditors were dealt with in and by the scheme, which required the separate approval of

the requisite majority of creditors and the Court. Indeed, the capital reduction was part of the post liquidation reorganisation which would benefit creditors by ensuring that they received a higher recovery under the scheme than they would recover if the corporate reorganisation did not proceed.

(e). finally, the fifth requirement was satisfied because the capital reduction was a necessary part of the overall post liquidation reorganisation which was for the benefit of the Company's shareholders and creditors. The Company is currently insolvent and in liquidation. The capital reduction will enable the Company to consummate the conditions of the scheme and allow the Company's debt burden to be reduced, thereby returning it to balance sheet solvency and allowing it to continue trading. As the circular sent to shareholders on 27 April 2019 made clear, the object of the overall corporate restructuring was to "save" the Company through an injection of capital from a new investor and others.

Confirmation of the capital reduction – discussion

18. I considered the five requirements or criteria referred to above. In my view they are satisfied in the present case and it is appropriate to confirm the reduction of capital.

19. I am satisfied that the evidence I have seen demonstrates that:

(a). the special resolution required by section 14 of the Companies Law has been duly passed;

(b). all shareholders have been treated uniformly and equitably in relation to the capital reduction;

(c). the circular sent to shareholders properly explained that part of the post liquidation restructuring and capital reorganisation relating to, and the terms and impact of, the capital reduction;

(d). the discernible purpose of the reduction of capital is clear in that it is a necessary step in the capital reorganisation and required to permit the critical capital raising process to proceed; and

(e). the interests of the Company's creditors are clearly protected and the position of creditors improved by the post liquidation restructuring of which the capital reduction is a part.

20. I have carefully considered (i) the effect on the application to confirm the capital reduction of the evidence filed and arguments made by Perfect Gate in its opposition to the Summons and (ii) whether it is appropriate to confirm the capital reduction at a time when the period within which Perfect Gate may appeal the Judgment has not expired and when the validity of the resolution is in issue in the Hong Kong proceedings:

(a). Perfect Gate has complained that the capital reorganisation is unfair to existing shareholders because it effects too large a dilution of their interest in the equity. This is not an effect of the capital reduction, with which the Court is primarily concerned. Perfect Gate's complaint of unfair treatment arises not from the capital reduction but from the decision to increase the Company's share capital, enter into the subscription agreements and to undertake the capital raising exercise on the terms agreed by the liquidators. It would be necessary for Perfect Gate to show that there was a proper ground to challenge those decisions which it has not done. But even if it is appropriate for the Court to have regard to the treatment of shareholders under transactions closely connected with the capital reduction, I am not satisfied that there is evidence of any relevant unfairness that would justify a refusal to confirm, or prevent the Court from confirming, the capital reduction. The approach to the dilution of existing shareholders appears to be a reasonable one in the all the circumstances. Furthermore, Perfect Gate's failure to oppose the confirmation of the capital reduction means that any issues arising out of its opposition to the Summons are to be given considerably reduced weight.

(b). the validity of the special resolution passed at the EGM is a particularly important factor on the application to confirm the capital reduction as it is a precondition to the Court's jurisdiction to confirm. Therefore the Court should be cautious about confirming the capital reduction while doubts as to the validity of the resolution exist. However, I have concluded that in the present case it is appropriate to confirm the reduction. It was open to Perfect Gate to notify the Court that it intended to appeal the Judgment before the hearing or to seek a stay of the Judgment or an adjournment of the hearing to give it time to decide whether to lodge an appeal. It has taken none of these steps and remained silent. The Judgment is therefore effective and not subject to a stay and determines, in this Court, that

the special resolution is valid. It would in my view be wrong in these circumstances, and in view of the need for the confirmation order to be made urgently to permit the post liquidation restructuring to proceed, to delay making the confirmation order to await further developments and see whether Perfect Gate wishes to appeal the Judgment. Nor, in my view, does the fact that Perfect Gate's Application for Declaratory Relief remains outstanding in the Hong Kong court require or justify such a delay. It will be a matter for the Hong Kong court to decide Perfect Gate's Application for Declaratory Relief (and the Strike Out Summons) in such manner as it considers appropriate. It is to be hoped that inconsistent judgments can be avoided but the issue of the validity of the special resolution for the purpose of this jurisdiction and therefore for the purpose of the application to confirm the capital reduction is disposed of by the Judgment.

(c). I discuss below, when discussing the same issue in relation to the sanction of the scheme, the possible impact of there being other conditions which have to be satisfied before the capital reduction can be implemented.

Sanctioning the scheme of arrangement – the law

21. The Company relied on the summary in the Chief Justice's judgment in *In re The Sphinx Group of Companies* [2014 (2) CILR 152] of the matters to be considered by the Court in determining whether or not to exercise its discretion to sanction a scheme of arrangement. After citing the English position as explained by David Richards J in *Re Telewest Comms. Plc (No. 1)* [2005] 1 BCLC 752, at [20-22] the Chief Justice Smellie stated as follows:

> *"From these dicta, in order to sanction a scheme which has been approved by the requisite majority of creditors at the court-directed meetings, the court must be satisfied that –*
>
> *(a) the meetings of the scheme claimants were summoned and held in accordance with the court's order ("the **compliance issue**");*
>
> *(b) the scheme was approved by the requisite majority of those who voted at the meetings in person or by proxy ("the **voting issue**"); and*
>
> *(c). the scheme is such as an intelligent, honest man acting in respect of his interest might reasonably approve ("the **fairness issue**").*"

22. I would add that, once again, there is a helpful and recent summary of the position (under English law) set out in Mr. Justice Snowden's judgment in *Re Man Group plc* [2019] EWHC 1392 (Ch) at [10]:

> *"The function of the Court at a sanction hearing for a scheme is summarised in the following extract from Buckley on the Companies Acts on section 899 of the [UK Companies] Act which has frequently been cited with approval and applied by this Court:*
>
> > *"Sanction of the court*
> >
> > *Once the meetings have approved the scheme, the sanction of the court must be sought. The sanction of the court is not a mere formality. Although the court has an unfettered discretion as to whether or not to sanction the scheme, it is likely to do so, as long as: (1) the provisions of the statute have been complied with; (2) the class was fairly represented by those who attended the meeting and that the statutory majority are acting bona fide and are not coercing the minority in order to promote interests adverse to those of the class whom they purport to represent; and (3) the arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest might reasonably approve...*
> >
> > *The court does not sit merely to see that the majority are acting bona fide and thereupon to register the decision of the meeting. The court will decline to sanction the scheme if the class has not been properly convened and properly consulted, or the meeting has not considered the matter with a view to the interests of the class which it is empowered to bind, or some blot is found in the scheme which had been unobserved when it had been approved by members or creditors, but will otherwise be slow to differ from the meeting."*

Sanctioning the scheme of arrangement – the Company's submissions

23. At the scheme meeting, held in Hong Kong on 5 July 2019, the scheme was approved by the requisite majority of the single class of creditors. The resolution approving the scheme was passed by 90.9% in number of the scheme creditors present in person or by proxy or authorised representative and voting, holding 93.62% of the aggregate principal amount of the scheme claims represented by those scheme creditors present and voting. In total, twenty two scheme creditors attended the scheme meeting by proxy or in person holding in aggregate HK$768,270,172.01 by value of scheme claims. The parallel scheme in Hong Kong was approved by the same majorities. Not every scheme creditor attended the scheme meeting. In total, the liquidators are aware of forty three claims totaling HK$1.68 billion. Therefore, approximately half of all known scheme creditors attended the scheme meeting. There was no obligation on scheme creditors to attend the scheme meeting, and the proportion of attendees having regard to total scheme claims was significant. The liquidators submit that it was significant that of those scheme creditors who showed sufficient interest to attend and vote on the scheme, the overwhelming majority approved the scheme.

24. At the scheme meeting there were two votes against the scheme admitted for voting purposes. One was disputed and admitted in the sum of HK$1.00 even though the notice of claim lodged by that scheme creditor was for HK$202,000,000. This claim was adjudicated by Mr. Yen as chairman as being a contingent claim and subject to a counter-claim by the Company. This was the same approach to this particular scheme creditor as had been taken by the Official Receiver of Hong Kong at the first meeting of the Company's creditors held on 16 July 2015. The Company and the liquidators pointed out that even if the claim had been allowed in full for voting purposes, it would not have changed the outcome of the meeting and the resolution approving the scheme would have still been passed by 83.42% of the value of claims (and a majority in number) of scheme creditors present and voting.

25. Based on the proofs of debt that have been submitted to the liquidators, the Company's indebtedness is in the approximate amount of HK$1,677.9 million and comprises:

(a). wages, salaries and other employee benefits of approximately HK$2.2 million;
(b). directors' fees of approximately HK$2.7 million;
(c). professional fees of approximately HK$2.4 million;
(d). rent of approximately HK$0.9 million;
(e). guaranteed bank loan of approximately HK$61.9 million;
(f). convertible bonds of approximately HK$540 million;
(g). corporate bonds of approximately HK$57.3 million;
(h). liabilities arising from a financial guarantee provided to the Company's PRC subsidiaries of approximately HK$198.2 million; and
(i). liabilities arising from a financial guarantee provided to a guarantor of the Company's PRC subsidiaries of approximately HK$812.3 million.

26. As I have explained in the Judgment, the liquidators consider that in the absence of a restructuring of the Company's indebtedness as part of and to facilitate the capital reorganisation, the only viable alternative is a realisation of the assets within the liquidation of the Company and of its subsidiaries. In that event, the likely return to the scheme creditors is zero.

27. In light of this, the liquidators engaged in discussions with the Company's major creditors to assess their appetite for a compromise of their indebtedness. The responses from creditors were positive

and the liquidators then undertook investigations with a view to identifying potential new (white knight) investors. Those investigations were successful and the proposed scheme was promulgated in conjunction with support and input from the scheme creditors.

28. At the time of the convening hearing before this Court on 30 April 2019, approximately 82% of scheme creditors by value had indicated their commitment to vote in favour of the scheme.

29. The ultimate objective of the scheme, as part of the broader post-liquidation restructuring, is to realise the value of the Company's listing status on the Hong Kong Stock Exchange for the benefit of the Company's creditors. Under the scheme, the Company's creditors compromise their claims against the Company in consideration for (subject to adjudication of their claims) distributions from (i) HK$80 million, being part of the proceeds from the new share subscriptions made by the new investor and by others under a public share offer, and (ii) dividends and recoveries from the Company's subsidiaries (however, the liquidators' liquidation analysis indicates that there are not expected to be any dividends or recoveries from the Company's subsidiaries). The result for scheme creditors under the scheme is a dividend of approximately 4.3 cents in the dollar whereas, if a restructuring is not effected, scheme creditors will likely receive nothing following the realisation of assets by the liquidators.

30. The Company and the liquidators prepared and distributed to scheme creditors a detailed explanatory statement which:

(a) summarised the court process for the scheme to be sanctioned and provided advice for scheme creditors as to how to participate in that process; provided a concise overview of the benefits for scheme creditors if the scheme is implemented, and a timeline of key events.

(b). explained the compromise to be effected by the scheme; the background to and the effect of the transactions proposed in the scheme and why scheme creditors should consider voting in favour of it.

(c). set out the mechanics of the restructuring whereby funds will be raised from new share subscriptions and those funds will be used primarily to purchase 100% of the shares in Yu

Ming Investment Management Limited (***Yu Ming***) for HK$400 million and pay HK$80 million to satisfy the claims of scheme creditors under the scheme.

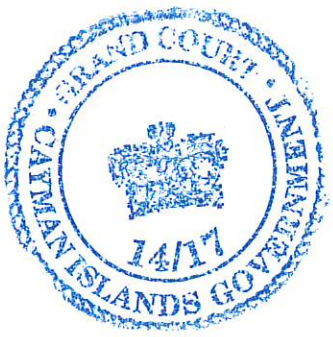
(d). contained the liquidators' assessment of the recoveries and outcome for creditors in the event that the scheme was not approved and the post liquidation restructuring did not proceed (in the liquidation analysis).

(e). confirmed that scheme creditors will be paid out rateably and that scheme creditors will have no further claims against the Company.

(f). confirmed the liquidators' opinion that scheme creditors were likely to receive a better return through the scheme than through the sale of the Company's assets in the liquidation.

(g). set out the conditions precedent to the scheme (the ***Conditions Precedent***) which needed to be satisfied before the scheme would becoming binding and effective. Section 3 of the explanatory statement stated that:

> *"The Schemes will become binding and effective on the Company and Scheme Creditors under Cayman Islands law and Hong Kong law if the following conditions are satisfied:*
>
> *(a). [the requisite majority of creditors vote in favour of the schemes];*
>
> *(b). [this Court sanctions the Cayman scheme] and an office copy of the [sanction order] is delivered to the [Cayman Registrar of Companies];*
>
> *(c). [the Hong Kong court sanctions the Hong Kong scheme] and an office copy of the [sanction order] is delivered to the [Hong Kong Registrar of Companies].*
>
> ……
>
> *As the Schemes are part of the [post liquidation restructuring and capital reorganisation] the Closing of the Schemes is conditional upon:*
>
> *(a). the completion of the [capital reorganisation, including the acquisition of the shares in Yu Ming, the subscriptions for new shares, the private placing and the public offer.]*
>
> *(b). the Company receiving the [HK$80,000,000, being part of the subscription proceeds of proceeds of the subscription and private placing];*
>
> *(c). the Executive Director of the Corporate Finance Division of the Securities and Futures Commission granting the [consent required because some scheme creditors are also shareholders]; and*



(d). the fulfilment of the conditions for the resumption of [the listing and trading of the Company's shares] imposed by the [Hong Kong] Stock Exchange.

All of these conditions cannot be waived"

(h). contained information concerning the person from whom the Company will acquire shares in the target company, Yu Ming and the new investor.

(i). set out the interests of the Company's directors in the scheme.

31. Certain amendments to the scheme and the explanatory statement were made after the Convening Order. Paragraph 3 of the Convening Order required that the scheme and explanatory statement to be sent to creditors be substantially in the form of Schedule B to the Convening Order. As is normal in large schemes of this kind, it was understood that prior to being sent out it would be necessary for some further amendments to be made to these documents. Following the making of the Convening Order, the Company amended the scheme and the explanatory statement in certain respects so as to improve the explanation of the restructuring proposal to scheme creditors. Those amendments comprised:

(a) amendments required by me;

(b). the correction of typographical, grammatical, and other minor errors;

(c). the insertion of basic details not known at the time of Convening Order (such as the date and time for the meeting of the scheme creditors); and

(d). the insertion/deletion of information to reflect changes in circumstances which occurred following the Convening Order. These changes were, in summary, as follows:

(i). amendments were made to include further details of the timing and amount of payments of sums to be advanced to the Company by the vendor of the shares in Yu Ming;

(ii). amendments were made to expand and update the explanation on the progress of the restructuring since the appointment of liquidators, including, inter alia: (i) the

uncooperativeness of the management of the Company; (ii) the fact that the liquidators had undertaken a quantitative analysis of the expected return to scheme creditors which estimated a zero return in the event that it became necessary to realise the Company's assets within the liquidation if the post liquidation restructuring failed; (iii) details of the alternative restructuring and resumption proposals considered by the liquidators; and (iv) that the post liquidation restructuring proposal – put forward by the seller of the shares in Yu Ming and the new investor – presented the best outcome for scheme creditors in the circumstances and was comparable to other successful restructuring proposals that the liquidators had previously handled;

(iii). amendments were made to inform the scheme creditors of the engagement of Lego Corporate Finance Limited as a financial adviser and that based on its advice the liquidators were satisfied that there was unlikely to be a better proposal in the short term than the current post liquidation restructuring proposal;

(iv). amendments were made to include details of the cash consideration provided for participating creditors in comparable schemes of arrangements involving listed companies under (in those cases) provisional liquidation and similar stages of delisting;

(v). amendments were made to include details of the scheme costs, including a breakdown of the costs of the schemes to be paid out of the cash consideration of HK$80 million.

32. The Company and the liquidators submitted that these amendments were insubstantial so that paragraph 3 of the Convening Order had been complied with.

33. The Company submitted that in these circumstances all the requirements for the sanction of the Cayman scheme had been satisfied:

(a). as regards the compliance issue, all the requirements of the Convening Order and the applicable Grand Court Rules had been complied with;

(b). as regards the voting issue, the scheme was approved by the requisite majorities required by section 86 of the Companies Law and the scheme had obtained substantial support;

(c). as regards the fairness issue, the evidence demonstrated that the scheme was one which an intelligent, honest man acting in respect of his interest might reasonably approve. The impact of the scheme on scheme creditors was simply to provide for an extinguishment of their debts in exchange for receiving a part-payment of the amount owing to them in excess of what they would (or were expected to) receive under the alternative to the current post liquidation restructuring. The proper comparator for these purposes was the outcome of the realisation of the Company's assets by the liquidators, which would occur if the post liquidation restructuring was not approved and implemented. All scheme creditors will receive the same pro-rata payment of their outstanding debt and the rights of priority creditors (secured creditors, of whom there appear to be none; preferential creditors totaling approximately HK$215,000 and creditors whose claims rank as liquidation expenses) are protected and preserved;

(d). as regards other issues relevant to the exercise by the Court of its discretion:

(i). the Court customarily considers whether the scheme will be effective in relevant foreign jurisdictions and will not sanction the scheme if the evidence demonstrates that it will not be. As to this, the main purpose of there being a scheme in Cayman was to ensure that scheme creditors cannot disrupt the smooth operation of the scheme by taking hostile action against the Company in its place of incorporation. The scheme will be effective in the other relevant jurisdiction, which is Hong Kong, where the Company and its subsidiaries carry on business and where the preponderance of the Company's debts are located (most of the Company's liabilities are governed by Hong Kong law). The parallel and inter-conditional scheme proposed in Hong Kong will ensure that such liabilities are effectively dealt with and compromised by the scheme.

(ii) the fact that the scheme was conditional on the Hong Kong scheme being sanctioned by the Hong Kong court and subject to the other conditions precedent did not prevent the Court from making an order sanctioning the scheme and the Court could and should make such an order now without waiting for the Hong

Kong court's decision or the satisfaction of the other Conditions Precedent. Alternatively, the Court can and should sanction the Cayman scheme subject to and conditional upon the Hong Kong court sanctioning the Hong Kong scheme. As regards the question of whether the Court had jurisdiction to make a sanction order conditional on the satisfaction of certain conditions and when the Court should do so, the Company and the liquidators submitted as follows:

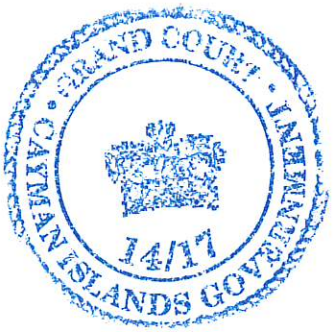
(A). section 86(2) of the Companies Law provides that, if the statutory voting majorities are achieved, a compromise or arrangement will be binding "*if sanctioned by the Court*". The issue was whether, on its proper interpretation, the discretion afforded by section 86(2) permits the Court to make a conditional sanction order.

(B). there was no Cayman Islands authority on the point and so regard should be had to the English position since section 899 of the English Companies Act 2006 contains a similar provision.

(C). the leading English authority was *Re Lombard Medical Technologies plc* [2015] 1 BCLC 656. In this decision, Henderson J undertook a detailed analysis of the position in both England and Australia as regards conditional sanction orders.

(D). in that case the scheme of arrangement in question was subject to conditions which needed to be satisfied before the scheme could become effective. The question was whether the court could sanction the scheme in those circumstances. Henderson J held that conditions could be attached to sanction, and in this case, the court could direct that the sanction order not be sealed or not be delivered to the Registrar of Companies until the conditions were satisfied. Henderson J stated at [24]:

> "*I can see no reason in principle, however, why the court may not, in an appropriate case, sanction a scheme when there is an outstanding condition which still needs to be satisfied, and direct that the order should not be sealed (or, as in the present case, that the order should not be delivered to the registrar) until the condition has been satisfied.*"



(E). after reviewing relevant case law, Henderson J stated at [30]:

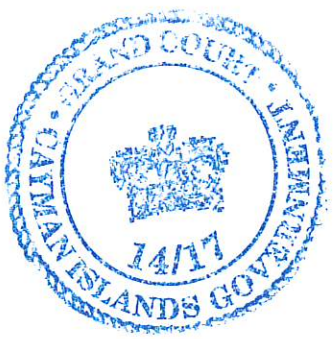
> "*In the light of the principles which I have discussed, I agree with Mr Shaw (to return to the present case) that there is no objection in principle either to the limited conditionality of the scheme (in the sense that its operation was made conditional on the successful completion of the fundraising) or to the solution devised to the problem (whereby the order sanctioning the scheme would not be delivered to the registrar until the condition had been satisfied). There were good commercial reasons for proceeding in this way ...*"

(F). Henderson J then proceeded to review the decision of Hildyard J in *Fiberweb plc v PGI Acquisitions Limited* [2013] EWHC 4653 (Ch) to determine whether that decision might cause him to take a different view. He concluded it did not.

(G). Henderson J sanctioned the scheme but directed that the sealed order not be delivered to the Registrar of Companies until the conditions precedent in the scheme were satisfied. He noted at [42]:

> "*.....the solution adopted in the present case finds some indirect support in previous authority and practice, and seems to me to fall well within the proper scope of the unfettered discretion conferred on the court by s 899(1).*"

(H). the Company and the liquidators submitted that if the Court was concerned about the result of the hearing of the Hong Kong petition on 22 July 2019 and its impact on the Cayman Islands scheme, the unfettered discretion afforded by section 86(2) of the Companies Law permitted the making of a sanction order with an accompanying direction that the order not be delivered to the Registrar of Companies unless and until the Hong Kong scheme of arrangement was sanctioned. If that sanction was not given at the hearing in Hong Kong on 22 July 2019, the post liquidation restructuring will collapse in any event.

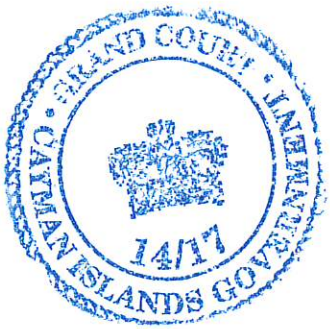


(I). but they further submitted that, although the Court had the power to make a conditional sanction order, it need and should not do so in the present case. The restructuring of the Company involved parallel schemes of

arrangement in the Cayman Islands and Hong Kong. If the Hong Kong scheme was not sanctioned on 22 July 2019, then the restructuring will fail. They noted the following comments made by Henderson J in *Lombard Medical* at [7]:

> "*My own understanding is that the court has in the past, as a matter of practice, proceeded on the basis and, when alerted to the point, insisted on the bidder confirming to it that the conditions to which the offer was subject have been satisfied or waived, except in circumstances usually arising out of a cross-border context where, for example, the approval of some other court or regulator is required, in which case that conditionality having been explained will ordinarily be accepted.*"

(J). the Company and the liquidators submitted that the same issue of conditionality did not arise in the context of the confirmation of the Company's capital reduction. If the capital reduction was confirmed and the order lodged with the Registrar of Companies immediately, its only effect will be to reduce the par value of the Company's shares already in issue. The proportionate interests of the shareholders in the Company will not be changed. Even if the Hong Kong scheme of arrangement was not sanctioned at the hearing on 22 July 2019 and the post liquidation restructuring failed, shareholder interests would not be affected. Shareholders did not need the protection of a conditional confirmation order because the capital reduction did not adversely affect their rights and even if the post liquidation restructuring failed, the shares would be worthless. Furthermore, it was important, in view of the very tight timetable set by the Hong Kong authorities and the process for issuing and listing the new shares pursuant to the capital reorganisation that there be no conditionality to the Court's order confirming that capital reduction.



Sanction of the scheme of arrangement – discussion

34. I accept the submissions made by the Company and the liquidators in relation to the compliance issue, the voting issue and the fairness issue:

(a). I am satisfied that the terms of the Convening Order (including paragraph 3) and the applicable statutory provisions have been complied with;

(b). I am also satisfied that matters relating to the voting issue have been complied with. The scheme comfortably obtained the necessary statutory majorities in favour and a significant number of creditors attended the scheme meeting. The scheme creditors attending the meeting appear to have been fairly representative of the class and I have no reason to believe that the majority were acting in bad faith or that they were seeking to promote interests adverse to those of the class.

(c). I am also satisfied that an intelligent and honest creditor of the Company could reasonably consider the scheme to be in his best interests. I am not required to be satisfied that the scheme is the only fair scheme or even the best scheme available. The scheme offers creditors a better return – albeit a modest return - than would probably be available if the liquidators were required to realise the Company's assets and continue the liquidation.

(d). I would add that I am also not aware of any blot on the scheme.

35. I also accept the submissions of the Company and the liquidators on the question of whether the Court has the power to sanction schemes subject to the satisfaction of conditions to implementation which are unsatisfied at the hearing date and the question of whether the Court can in effect make its order subject to the satisfaction of certain conditions. I find the analysis and approach of Henderson J in *Lombard Medical* to be completely convincing and consider that it should be followed in this jurisdiction. However, contrary to the primary case of the Company and liquidators, I consider that the sanction order should not become effective unless and until the Hong Kong court has sanctioned the Hong Kong scheme. It seems to me to be important that this Court retains control over the scheme process, in particular the time at which its scheme becomes effective. It would not be acceptable, and in the interests of scheme creditors, if this Court were to sanction unconditionally the Cayman scheme and then there was a delay in the Hong Kong court's decision on the application to sanction the Hong Kong scheme (or if the Hong Kong scheme was modified in a manner that was arguably insignificant at a time when this Court had already and finally determined the application to sanction of the Cayman scheme). I appreciate that there is no risk of the Cayman scheme being implemented if the Hong Kong scheme is not sanctioned (or the capital reorganisation is not completed) but there are other risks to be managed. I note Henderson J's

comments (at [26] of his judgment) when explaining that the court can sanction a scheme even when there is an outstanding condition at the hearing date or when the court's order is to be sealed:

> *"Nor is it always indispensable, in my view, that an outstanding condition should be satisfied before the order is sealed. I can see no objection in principle to the court sanctioning a scheme which is conditional in one or more respects, provided always that the court considers it appropriate to do so in the exercise of its discretion. Examples of the kind of condition which the court may be willing to sanction, even if they are unsatisfied at the date of the hearing, are outstanding requirements for foreign regulatory approval which there is no reason to suppose will not be granted."*
>
> [underlining added]

Of course, the Hong Kong court is not a foreign regulatory body but the point made by Henderson J nonetheless applies. The sanction of the Hong Kong scheme is a condition to implementation of the Cayman scheme and the application for sanction is subject to opposition, the precise grounds of which are unclear. There is in my view a sufficient degree of uncertainty both as to the outcome and the timing of the Hong Kong court's decision to require caution (the uncertainty is increased in the present case because it appears, as I have explained in paragraph 11 above, that Perfect Gate has the unilateral ability to cause the post liquidation restructuring to fail). Therefore I decided that the sanction order should not be sealed until the Hong Kong court had decided to sanction the Hong Kong scheme and that this Court should retain the ability to make further orders if that did not happen within the near future. I directed that the following wording be included in the sanction order:

> *"This Order shall not be sealed until the Court receives written confirmation from the Company's attorneys [Harneys] that the High Court of the Hong Kong Special Administrative Region has sanctioned the Hong Kong scheme without modification. If confirmation has not been received by 16 August 2019, this Order may not be sealed without further order of the Court and the Company's application for sanction of the scheme shall be restored to be heard at a time to be fixed."*

36. I accept the Company's and the liquidators' submission that a similar condition should not, on this occasion, be included in the order confirming the capital reduction. I was minded to include such a condition, as it seemed to me to be inappropriate to confirm the capital reduction unconditionally when there was a material risk that the capital reorganisation of which it was a part might not proceed. However, in view of the importance of the capital reduction becoming unconditional without delay in order to allow the practical steps needed to have the new shares issued and listed in time, and the fact that shareholders would suffer no prejudice if the reduction was confirmed but the post liquidation restructuring failed, I decided that it was appropriate to make the confirmation order on an unconditional basis.

37. I would add one further point. Throughout this case I have reminded the liquidators (and Perfect Gate) of the need to consider the coordination of the applications being made in this Court and the Hong Kong court (and the possible benefit of and need for common directions regarding the filing of evidence and submissions in both courts and even of court to court communication and simultaneous hearings). For reasons of which I am not aware this has not proved to be possible in this case. I do not intend to be critical. There may be good reasons why these steps were considered to be inappropriate or unavailable in this case (and I would note with gratitude that Mr. Justice Harris in the Hong Kong court very helpfully sent me a copy of his Decision of 9 July). But I would remind parties for the future to keep the need for such coordination firmly in mind.

Mr. Justice Segal
Justice of the Grand Court, Cayman Island

22 July 2019