

Short-form mergers - the appraisal saga continues in Changyou.com

Insights - 01/03/2023

The Cayman Islands Court of Appeal has recently dismissed challenges to its decision that shareholders of companies effecting "short-form" mergers [1] are entitled to be paid fair value for their former shareholdings upon dissenting from the merger. [2]

The judgment confirms that any attempt to reverse engineer new grounds of appeal based on the ultimate findings of the appellate court will be dismissed. It also provides helpful guidance on when a decision on a preliminary issue will be considered final for the purposes of applying for leave to appeal to the Judicial Committee of the Privy Council.

Background to Changyou

Changyou.com Limited (**Changyou**) is a Cayman Islands incorporated company operating in China which merged with its parent company and de-listed from the NASDAQ (thereby effectively forcing out the minority independent shareholders under a short-form merger).

Changyou asserted that dissent rights under section 238 of the Companies Act did not apply in these circumstances. However, certain shareholders still attempted to dissent from the merger. Changyou contended that appraisal rights could only be exercised by shareholders who dissent from a merger in which there is a shareholder vote (a long-form merger) and that since no vote is required for a short-form merger no appraisal rights were available. The dissenters filed a petition seeking payment of the fair value of their former shares.

Decisions

First instance decision granting appraisal rights

The point was determined as a preliminary issue in favour of the dissenters. The Grand Court held

that the provisions of section 238 should be read so as to allow the appraisal process to operate in the absence of any vote authorising the merger to avoid what would otherwise be an absurd result and a violation of the rights guaranteed by the Constitution, namely the right to peaceful enjoyment of property. [3] For a more detailed overview, read our article [Short-form mergers - appraisal rights confirmed in the Cayman Islands in Changyou judgment](#).

Appeal decision confirming appraisal rights

The Court of Appeal preferred Changyou's interpretation of section 238 based on ordinary principles of construction, but agreed with the Grand Court that this produced an absurd result arising from an obvious drafting error. Since shares in a company were plainly "property" for the purposes of the Constitution, the Court of Appeal found that the operative provisions of section 238 needed to be reworded so as not to deprive minority shareholders of the right to peaceful enjoyment of their property without compensation. For a more detailed overview, read our article [Appraisal rights confirmed in Cayman Islands short-form mergers](#).

Challenges to terms of order

Changyou subsequently challenged the terms of the order to be made on the appeal, arguing that the effect of the appeal judgment was actually to allow its appeal.

Firstly, it contended that the dissenters had not validly objected to the merger in accordance with the procedural requirements specified by the Court of Appeal in its construction of section 238. This argument was rejected on the basis that Changyou's appeal had been one of law and not of fact, and this new argument had not been included in Changyou's earlier grounds of appeal or oral submissions at the appeal hearing.

Secondly, Changyou asserted that the different approach taken by the Court of Appeal compared to the Grand Court represented a success for the company. This argument was dismissed on the basis that both Courts were clear that section 238 needed to be judicially amended and were clear as to substance of those amendments. The Court of Appeal's substitution of certain words to achieve compliance with the Constitution did not mean that the Grand Court's approach was impermissible or wrong and did not represent any success for Changyou.

Thirdly, Changyou argued that since the Court of Appeal had agreed with its proffered ordinary construction of section 238, before varying this to comply with the Constitution, it had been successful on an important issue in dispute. This was rejected on the basis that the ordinary construction of 238 was only a precursor to the consideration of the constitutional position, rather than being a separate issue in the appeal.

Leave to appeal to Privy Council

Changyou sought leave to appeal the Court of Appeal's substantive decision to the Privy Council as

of right, on the basis that it was final rather than interlocutory.

The Court of Appeal imported English authority [4] which recognised that a decision is not to be regarded as interlocutory simply because it was not finally determinative of the action whichever way it goes. Rather, it is a "a broad common-sense test...asking whether (if not tried separately) the issue would have formed a substantive part of the final trial". [5] The Court of Appeal considered that the decision on the preliminary point of whether appraisal rights were available in short-form mergers was clearly final as it would have otherwise formed a substantive part of the trial. Furthermore, if it had been determined against the dissenting shareholders, it would have brought the entire proceeding to an end.

Although this meant that Changyou was entitled to appeal to the Privy Council as of right, the Court of Appeal noted it would have also granted leave on the discretionary basis [6] in any event, as the question of appraisal rights in short-form mergers was one of great general or public importance.

Comment

This latest decision in the Changyou appraisal demonstrates that the availability of appraisal rights in short-form mergers remains hotly disputed in the Cayman Islands. Changyou's attempt to frame itself as being the victor in the Court of Appeal may have been overly ambitious, but the fight will continue before the Privy Council and be keenly observed by merging companies and dissenting shareholders alike.

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[1] A parent company merging with a subsidiary in which it holds 90% of the voting power

[2] *In the matter of Changyou.com CICA (Civil)* Appeal No. 6 of 2021, 20 December 2022 - [access judgment here](#)

[3] Cayman Islands Constitution (2009), Bill of Rights, section 15

[4] *White v Brunton* [1984] QB 570 and *Holmes v Bangladesh Biman Corp* [1988] 2 Lloyd's Rep 120

[5] [1988] 2 Lloyd's Rep 120 at p 34C-F

[6] Section 3(2)(a) of the Cayman Islands (Appeals to the Privy Council) Order 1984

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