Standard directions in section 238 appraisal proceedings confirmed in the Cayman Islands

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Introduction

In a decision that provides additional certainty to dissenting shareholders, the Grand Court of the Cayman Islands has rejected efforts by eHi Car Services Limited (the **Company**) to recast the procedural framework for appraisal proceedings brought under section 238 of the Companies Law (as Revised) (the **Law**).

This decision follows last year's significant ruling of the Chief Justice of the Cayman Islands in JA Solar,[1] which has become the touchstone for directions orders in section 238 proceedings.[2]

Background

Section 238 of the Law gives shareholders a statutory right to dissent from the merger of a Cayman Islands incorporated company, and to be paid a judicially determined fair value for their shares instead of the merger consideration being offered by the merging company.

Upon entering into such a merger, the Company in *eHi Car* presented a petition to have the fair value of the shares held by dissenting shareholders (**Dissenters**) determined by the Grand Court under section 238.

Despite the Grand Court having previously delivered numerous judgments on section 238 directions, the Company sought to dramatically depart from this established jurisprudence by seeking directions that bore little resemblance to what had previously been ordered.

Relevance of previous directions orders

The Honourable Justice Parker emphasised that the relatively "standard" directions that have developed in recent years are the best starting point in section 238 proceedings. These standard directions have been tried and tested by the Court and were confirmed as giving fair and efficient effect to the aims of the Law and the overriding objective of the Grand Court Rules to deal with

cases in a just, economical and expeditious manner.

It is always necessary to decide whether the particular directions sought are fair, economically sensible and necessary to do justice between the parties in each case. The Court found, however, that there was no evidence to suggest that the standard directions - which have been regularly ordered and complied with - have been working any material injustice, or are otherwise unfair. Despite the Company's protestations that these standard directions were unfair and disproportionately costly for companies, Justice Parker was unpersuaded that any significant variations to the standard directions should be ordered unless a compelling reason existed for doing so.

Company disclosure process

In rejecting the Company's assertion that the section 238 disclosure regime had become an information gathering "free for all" and an unnecessary expense for the Company, Justice Parker acknowledged that the discovery process in section 238 cases is different to other types of litigation, but found that this departure is necessary to produce all relevant information for the valuation exercise and is consistent with the Grand Court Rules. Echoing the Chief Justice's comments in *JA Solar* on the "*central importance of discovery*"[3] by companies who hold the majority of relevant information relevant to value, Justice Parker held that the experts needed to have all relevant information to understand the commercial reality in which the company operated both with regard to its existing business and future projections.

Management meetings

Meetings between the valuation experts and the company's management have been a feature of most section 238 proceedings and provide a valuable opportunity for direct dialogue between the experts and the company's management on the core issues of the valuation exercise.

Despite this, the Company argued that the Grand Court had no jurisdiction to order management meetings and, in the alternative, contended that if the Court did have jurisdiction, it should exercise its discretion against ordering any such meetings on the basis that they were unnecessary, inefficient, and contrary to the overriding objective of the Grand Court Rules.

In dismissing the jurisdiction argument, Justice Parker noted that the Grand Court had already rejected the jurisdictional challenge to management meetings on two previous occasions.[4] In deciding how to exercise the discretion to order such meetings, Justice Parker repeated the Chief Justice's findings in *JA Solar* that they are a "*crucial*"[5] part of the information gathering process and have an advantage over written questions and answers of allowing an interactive method by giving information and discussing relevant points. Due to the clear imbalance of information and understanding between the company and dissenting shareholders, the dissenting shareholders and their expert are at some disadvantage and it is necessary to attempt to correct that by members of the company’s management being made available to answer questions.

Addressing the Company's concerns that this procedure may be used oppressively against the Company's management, Justice Parker stressed that it was not a procedure to obtain oral evidence or to "trap" or undermine management. The Court's working assumption is that experts will perform their functions properly and professionally, having regard to their overriding obligations to the Court.

Justice Parker also agreed with the Dissenters that the number of management meetings should not be restricted and that written transcripts of meetings should be taken, as a practical, efficient and fair way of avoiding disputes as to what was said.

Expert information requests

Experts in section 238 proceedings are generally permitted to request information from the company for the purposes of preparing their valuation reports. However, the Company contended that the particular information request process proposed by the Dissenters lacked sufficient safeguards to ensure proportionality and to avoid duplication of effort and costs, particularly given that the Company would already be providing substantial documentary discovery.

Justice Parker disagreed that any change of approach to the usual orders dealing with information requests was either necessary or appropriate. The prescriptive conditions on information requests proposed by the Company were rejected on the basis that they would not help the experts' ability to assist the Court, who must be assumed to act reasonably and proportionately, and be trusted to properly perform their functions.

Dissenter disclosure

The Cayman Islands Court of Appeal had previously confirmed that mutual disclosure was required in section 238 litigation, but had limited the categories of documents that dissenting shareholders needed to disclose, rather than requiring them to provide general disclosure.[6]

Justice Parker rejected the Company's attempts to extend these established categories of dissenter disclosure on the basis that the extensions proposed by the Company were not clearly defined, necessary, proportionate, or sufficiently probative enough so as to make the exercise worthwhile. In doing so, the Court confirmed that the characteristics and motivations of dissenting shareholders are generally irrelevant to fair value, noting that:

"It is not relevant to ascertain whether they are speculative investors engaged in arbitrage or long-term shareholders who are being 'taken out' by the majority against their will, as fair value needs to be determined in one way for all dissenting shareholders irrespective of whether or not they might be said to be more or less 'deserving'."

Forced collaboration

The Company sought unprecedented orders requiring the Dissenters to identify the issues on which they collectively agreed and for them to be restricted to only making one set of written and oral submissions between them on any issues on which they agreed.

Justice Parker found that it was not for the Court to micromanage the conduct of attorneys or counsel. The Court will instead rely upon attorneys' obligations to the Court and the common sense and experience of counsel to coordinate matters sensibly, bearing in mind that section 238 provides that dissenting shareholders may participate "*fully in all proceedings until the determination of fair value*".

In the event that there has been any unreasonable or abusive conduct, the Court has the power to curtail it and to impose punitive orders if necessary, but it will otherwise leave it to the good sense of experienced attorneys to coordinate sensibly.

Conclusion

The Court's rejection of the Company's attempts to deviate from well-established direction orders in section 238 proceedings is a positive development for dissenting shareholders wishing to have the fair value of their shares judicially determined in the Cayman Islands.

Ogier has significant experience in s.238 proceedings. We have advised and acted from the initial objection stage all the way through to full trial. Over the years, Ogier's cross-border team has looked at the issues in different s.238 proceedings from the perspective of the company and that of dissenting shareholders, having acted on mandates for both.

[1] JA Solar Holdings Co Ltd (FSD 153 of 2018, 18 July 2019)

[2] Ogier represented the largest groups of dissenting shareholders at the directions hearings in both eHi Car and JA Solar.

[3] Paragraph [30]

[4] Trina Solar Limited (FSD 92 of 2017, unreported 1 November 2017) and Kongzhong Corporation Limited (FSD 112 of 2017 unreported, 2 February 2018)

[5] Paragraph [97]

[6] Qunar Cayman Islands Limited (CICA 24 of 2017, unreported 10 April 2018)

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