4-09-12

IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

Cause No. FSD 18 of 2012 (AJJ)

The Honourable Mr. Justice Andrew J. Jones QC
In Chambers, 22nd and 23rd August 2012

IN THE MATTER OF THE COMPANIES LAW (2011 REVISION)

AND IN THE MATTER OF TRIKONA ADVISORS LIMITED

BETWEEN:

(1) ARC CAPITAL LLC

(2) HAIDA INVESTMENTS LTD — **Petitioners**

-And-

ASIA PACIFIC LIMITED — **Respondent**

Appearances:

Ms Sara Dobbyn of Stuarts Walker Hersant on behalf of the Respondent (and on behalf of the Company in respect of the Summons dated 3rd April 2012)

Mr. Ross McDonough and Mr. Guy Cowan of Campbells of behalf of the Petitioners

REASONS

1. On 22 and 23rd August 2012 the Court heard argument on four Summonses. By its Summons dated 23rd March 2012 the Respondent sought a stay of the Winding Up Petition on case management grounds pending the resolution of actions pending in both the Federal and State courts of Connecticut ("the Connecticut Proceedings"). The Petitioners response was to issue a Summons dated 28th March 2012 by which they seek an order for the appointment of provisional liquidators. By a Summons dated 13th April 2012 (as amended on 17th July 2012), the Respondent sought an order that the Petition be struck out as an abuse of the process on the grounds that the Petitioners have been offered and refused an adequate alternative remedy and/or because the Petition was presented and is being pursued for an improper purpose. Finally, there is a fourth Summons dated 2nd April 2012 by which the Company

applies for an order validating both actual and prospective dispositions of the Company's property made after the presentation of the Winding Up Petition.

2. At the outset of the hearing counsel agreed that these Summonses should be heard and determined sequentially. Having dismissed the Respondent's strike out Summons, I went on to hear the Summons for a stay. In the event Mr. McDonough's argument in opposition to the stay included points made in support of the appointment of provisional liquidators with the result that argument on these two Summonses was merged. I dismissed the Respondent's Summons for a stay and made no order on the Petitioners' Summons for appointment of provisional liquidators. Instead, I made an injunction (and related disclosure order) restraining the Company's directors from using its assets for the purpose of financing the various legal proceedings specified in the schedule to the Order, including the Connecticut Proceedings and the new proceeding commenced in the New York State Court by one of the Petitioners against Mr. Kalra and his companies. The Order leaves open the possibility that the Petitioners could renew their application for the appointment of provisional liquidators in the event of non-compliance with the injunction. As regards the Company's validation Summons, it will be dismissed in so far as it seeks an order validating expenditure on the legal proceedings specified in the schedule to the Order. In so far as it seeks an order to validate expenditure on litigation and arbitration proceedings against third parties unrelated to the Company's shareholders and directors, Ms Dobbyn decided that she was not in a position to pursue the application without filing additional evidence. In the absence of opposition from Mr. McDonough, I made an order that this Summons be adjourned to a date to be fixed. I now give my reasons for making these orders.

STRIKE OUT APPLICATION – ADEQUATE ALTERNATIVE REMEDY

3. It is well established as a matter of Cayman Islands law that when considering a contributory's petition for a winding up order presented on the just and equitable ground, the Court is required to address the questions whether there is an adequate alternative remedy available to the petitioner and whether he is acting unreasonably in not pursuing or accepting that alternative remedy. In *Camulos Partners Offshore Limited v. Kathrein and Company* [2010] 1 CILR 303 Sir John Chadwick P. said –

> *If a court is satisfied that both of those questions should be answered in the affirmative, then it can be expected to take the view that the presentation of the petition is an abuse of its process or, alternatively, that the petition is bound to fail because it would not, in those circumstances, be "just and equitable" that the Company should be wound up.*

In cases where the petitioner is a minority shareholder who complains about oppression on the part of the majority, it is well established that an offer to purchase his shares at fair value will be regarded as an adequate alternative remedy, the rejection of which will lead the Court to strike out the petition. See *CVC/Opportunity*

Equity Partners Ltd v. Demarco Almeida [2002] CILR 77. The same analysis is capable of being applied to cases such as the present in which the Company is characterised as a quasi-partnership between two shareholders (or two groups of shareholders) who each own 50% of the shares.

4. The Petitioners' case is that the Company should be characterized as a quasi partnership between the two Petitioners (which each own 25% of the shares) and the Respondent (which owns 50% of the shares) and that there was a legitimate expectation that the Petitioners and Respondent would each have equal representation on the board of directors, thus giving each of them an effective veto. The Petitioners' representative is Mr. Rakshitt Chugh ("Mr. Chugh") who owns and controls Arc Capital LLC. [1] Their case is that the Respondent, which is wholly owned and controlled by Mr. Aashish Kalra ("Mr. Kalra"), has wrongly seized control of the Company by purporting to remove Mr. Chugh from its board of directors and excluding him from participating in any managerial decisions. It is not in dispute that Mr. Chugh was given no notice of the board meeting at which it was resolved to remove him from office. *Prima facie*, this resolution must be invalid. The Respondent's case will be that Mr. Chugh's *de facto* exclusion is justifiable because he has behaved towards the Company in a manner which constitutes a flagrant breach of his fiduciary duty. The Petitioners make similar allegations against Mr. Kalra. At an earlier hearing Quin J. decided that the Company should be treated as the subject-matter of the Petition which is in reality a shareholder dispute between the Petitioners and Mr. Chugh on one side and the Respondent and Mr. Kalra on the other side.

5. On 1st August 2012 the Respondent/Mr. Kalra made a written offer to the effect that the Company itself would buy back (or redeem) the Petitioners' shares at a "fair value" price to be determined by an expert assessor (referred to by counsel as the "buy out offer"). The proposed mechanism for determining the "fair value" is not derived from any provisions in the Company's articles of association. It is simply reproduced from that which was approved by the House of Lords in *O'Neill v. Phillips* [1999] 1 WLR 1092, the factual circumstances of which were wholly different from the present case. In that case the company in question carried on a profitable business. Mr. O'Neill owned 25% of the shares and served as the company's managing director for which he was paid a salary. The House of Lords reversed the decision of the Court of Appeal and held that Mr. Phillips' decision to dismiss Mr. O'Neill from his employment and limit him to receiving 25% of any dividends was not unfairly prejudicial within section 459 of the English Companies Acts. However, the House of Lords held that even if Mr. Phillips' conduct had been unfairly prejudicial to Mr. O'Neill, his petition should still have been dismissed because Mr. Phillips had made an offer to buy his shares at a fair price and this constituted the whole of the relief to which he would have entitled. Lord Hoffman's judgment (at page 1107-8) describes in general terms the valuation principles which

[1] It is asserted in the Connecticut Proceedings that Mr. Chugh also owns and controls Haida Investments Ltd, with the result that the two Petitioners should be regarded as the *alter ego* of Mr. Chugh. It is not disputed that he was appointed to the Company's board of directors as representative of both the petitioning shareholders and that they are acting in concert, but there is no evidence from which to infer that he is the beneficial owner of Haida Investments Ltd.

should be used to value a minority interest in a business which is a going concern and also the mechanism for determination of the purchase price.

6. The Respondent's offer embodies the same kind of mechanism for determining the purchase price as that approved by the House of Lords. It involves the appointment of an independent assessor whose function will be to determine the "fair value" of the Petitioners' shares. It is proposed that the assessor will be chosen by the Petitioners from a panel of four qualified chartered accountants nominated by the Respondent; his fees and expenses will be shared equally; he will set a timetable for receiving written submissions from the parties who must also provide him with all the supporting documentation; and the assessor will act as an expert (rather than an arbitrator) and will have full and final authority to determine the price. In my view a valuation mechanism of this sort is both unnecessary and inappropriate in the circumstances of this case. The evidence reflects that Company ceased to carry on its business in 2009. Apart from the proceedings listed in the schedule to the Order, which I characterize as litigation between the shareholders in which the Company has no independent interest, its only activity is the defence of some adverse claims asserted by independent third parties and the pursuit of an insurance claim in respect of legal fees incurred in litigation which has been settled. Messrs Kalra and Chugh are accusing each other of having diverted to themselves (or companies controlled by them) business opportunities which should have belonged to their Company. In these circumstances it is plainly obvious that no new business will ever be put through the Company, or at least not unless and until it is under the sole undisputed ownership of Mr. Kalra. It follows that there is no business or goodwill which needs to be valued by an independent assessor. During the course of the argument I was told by Ms Dobbyn (on instructions from Mr. Kalra) that the Company's assets currently comprise (i) cash of US$1.4m, (ii) cash of $5m held in the Company's Indian subsidiary which is said to be "locked up", meaning that it is subject to exchange control restrictions, (iii) a receivable of about US$2m, (iv) marketable securities worth US$1.2m and (v) an unsettled insurance claim of US$8m. I was told that the Company's liabilities and contingent liabilities are about US$0.5m. It follows, according to the Respondent, that the Company's current net asset value is about US$9m plus whatever is paid by its insurers which will be US$8m if the claim is paid in full. Having regard to the nature of these assets and the fact that there is no business capable of being valued on a going concern basis, it would serve no useful purpose to engage in a valuation exercise of the kind considered and approved by the House of Lords in *O'Neill v. Phillips*. If Counsel's description of the Company's assets is complete and accurate, it does not require the certificate of an independent expert assessor to work out that 50% of the NAV is $4.5m plus half of whatever is paid by the insurers. The proposed valuation mechanism invalidates the reasonableness of the offer because it would result in significant delay and shared expense for no useful purpose.

7. Furthermore, quite apart from the inappropriate valuation mechanism, the terms of the Respondent's purchase offer do not provide the Petitioners with an adequate alternative remedy for the following reasons. First, the proposal is that the Company,

not the Respondent, will buy back (or redeem) the Petitioners' shares in accordance with the provisions of section 37 of the Companies Law at a price equivalent to 50% of the NAV, excluding any value attaching to its claim against Mr. Chugh in the US Proceedings and any provision for the actual and prospective cost of conducting the proceedings. In other words, it is proposed that the Company will buy back the Petitioners' shares for up to US$8.5m or US$4.5m plus half of whatever is received in respect of the insurance claim. However, it is proposed that payment will be deferred until after conclusion of the Connecticut Proceedings which may not happen for some considerable time. As a matter of law, the Petitioners will be subordinated creditors and their ability to enforce a buy-back/redemption agreement concluded now will depend upon the future solvency of the Company and in the meantime they will have no control over the expenditure of its assets if the Winding Up Petition is consequentially dismissed. During the course of argument, Ms Dobbyn suggested that this point could be met by a guarantee from the Respondent but, in the absence of evidence to the contrary, the reasonable inference must be that it was incorporated as a special purpose vehicle for holding its shares in the Company in which case its guarantee would be worthless. In summary, the "buy back offer" is an offer by the Company to agree that it will buy back or redeem the Petitioners' shares at a price equivalent to 50% of the current NAV, on the basis that payment of the redemption proceeds will be deferred to an uncertain future date and will be contingent on the Company still being solvent. In this respect the "buy back offer" is not an adequate alternative remedy because there is no guarantee that the Company's assets will not have been dissipated by Mr. Kalra in the meantime.

8. Second, it is a term of the proposal that if the Company obtains a money judgment in the Connecticut Proceedings against Mr. Chugh and/or the Peak companies which are alleged to be the beneficiaries of his breaches of fiduciary duty, the amount will be set off against the sum owed to the Petitioners. This is not necessarily what would happen if a winding up order is made. The effect of section 140 of the Companies Law is that the official liquidator will not be able to set off the debt owed by the Company to the Respondent against the judgment debt owed to the Company by Mr. Chugh (or the Peak companies) unless he can establish mutuality to the satisfaction of this Court. Mr. Chugh denies that the Petitioners are his *alter ego*. If a winding up order is made, the burden will be on the official liquidator to prove mutuality, whereas the Respondent's "buy out offer" comprises an express tripartite set-off agreement which would be binding as between the Respondent and the Company in any event. In this respect, it is not an adequate alternative remedy because it deprives the Respondent of the right to require the official liquidator to prove that the statutory right of set-off applies.

9. Third, the Respondent's "buy out offer" is conditional upon the Company failing on its claim for an order for the forfeiture of the Petitioners' shares in the Connecticut Proceedings. Ms Dobbyn submits that "The Petitioners' status as Shareholders is sub-judice in the USA". Even if this is right as a matter of Connecticut law (which is disputed by the Petitioners' US attorney), the Respondent would still have to commence an action in this Court for an order for rectification of the register of

shareholders and it is by no means clear that this Court would be bound to recognize and give effect to an order for forfeiture. Ms Dobbyn points out that under the articles of association the Company is given lien over a member's shares in respect of unpaid debts, but the lien can only arise if the debt is owed by the Petitioners, as opposed to Mr. Chugh or the Peak companies, and the debt remains unpaid. In effect, it seems to me that the Petitioners are being asked to agree that any order for forfeiture will be given automatic effect, whether or not it would be recognized and given effect by this Court, about which there must be some scope for argument. It is not unreasonable for the Petitioners to reject this proposition.

10. Finally, Mr. McDonough makes the point that the "buy out offer" is not an adequate alternative remedy because it does not give the Petitioners the opportunity to buy the Respondent's shares at the same fair value. If a solvent company in liquidation owns a business which would be worth more than its net asset value if sold as a going concern, its official liquidator would be bound to consider selling it and the circumstances may be such that all the shareholders would have the opportunity to bid for it. The possibility of an official liquidator proceeding in this way does not arise in the circumstances of this case and so I do not think that it can be said that the "buy out offer" is inadequate as an alternative remedy merely because it does not give the Petitioners the opportunity to buy the Respondent's shares.

11. For these reasons I do not regard the Respondent's "buy out offer" as an adequate alternative remedy and so it cannot be said that the Petitioners are acting unreasonably by rejecting it and continuing to prosecute their Petition.

STRIKE OUT APPLICATION – IMPROPER PURPOSE

12. If an action is not commenced *bona fide* for the purpose of obtaining the relief sought, but for some improper ulterior or collateral purpose, it may be struck out as an abuse of the process of the Court. See *RCB v. Thai Asia Fund Limited* [1996] CILR 9. Ms Dobbyn argues that this Winding Up Petition has been presented to "undermine and sabotage" the Connecticut Proceedings. She says that, in reality, it has been brought by Mr. Chugh, who controls the Petitioners, for the purpose of impeding the Company's ability to pursue a legitimate claim for breach of fiduciary duty against him. Conversely, the Petitioners' position, articulated in their Verified Shareholder Derivative Complaint filed in the New York Proceedings, is that Mr. Kalra (acting through the Respondent and various other entities) has "looted" the Company and diverted business opportunities for his own personal benefit. The Connecticut Proceedings are characterized as an illegitimate means of reducing the Company's value and preventing the Petitioners from recovering their 50% share of its NAV in a liquidation.

13. Having heard the arguments and having read the affidavits, I have reached the following conclusions. Firstly, as Quin J. has already concluded, the Company must be characterized as a quasi-partnership between the Petitioners and the Respondent, represented by Mr. Chugh and Mr. Kalra respectively. There has been a complete

breakdown of trust, with the result that it is wholly impossible for the Company to carry on any business so long as it is jointly owned. Secondly, on the basis of the evidence presently before the Court it is not possible to make any finding, no matter how tentative, that the breakdown of this business relationship is attributable to bad behavior (whether or not amounting to a breach of fiduciary duty) on the part of Mr. Chugh or Mr Kalra or both of them. Thirdly, the Company has not carried on any business since 2009 and there is no prospect of any new business being put into it so long as it continues to be jointly owned. Fourthly, Mr. Chugh's purported removal from the Company's board of directors is *prima facie* invalid because it was done at a meeting of which he was not given notice. The timeline of the Connecticut Proceedings tends to suggest that the purpose of removing him from the board was to enable Mr. Kalra to convert the Connecticut Proceedings from a derivative action into one which is now being pursued in the name of Company. By converting it into a company action, Mr. Kalra clearly expected that he would be able to pay for it out of the Company's assets irrespective of the ultimate outcome. In these circumstances, I conclude that it is not illegitimate for the Petitioners to seek a winding up order which will not, by itself, prevent the two shareholder groups from pursuing derivative claims against Mr. Chugh and Mr. Kalra in the Connecticut and New York Proceedings.

14. The Respondent's application for a temporary stay of the Petition pending the outcome of the Connecticut Proceedings is put on the following grounds. It is argued that if the Company should be awarded damages against the Petitioners in the Connecticut Proceedings, this will become a debt due to the Company which will then have a lien over the debtors' shares. This would also be the case if the Company is awarded damages against the Respondent in the New York Proceeding. In both cases this result depends upon establishing that the corporate shareholders are properly to be treated as the *alter ego* of Mr. Chugh and Mr. Kalra respectively. However, the possibility that the Company might be able to assert a lien in this way does not lead to the conclusion that "The Petitioners' status as Shareholders is sub-judice in the USA". Ms Dobbyn also relies upon the fact that the Company is asking the Connecticut Court to make an order for the forfeiture of the Petitioners' shares. Even if the Connecticut Court has jurisdiction to make such an order as a matter of Connecticut law (which is disputed by the Petitioners' Connecticut attorney), Ms Dobbyn did not explain the basis for recognizing this result. The fact that these remedies are being sought is not, in my view, a good reason for staying this Petition.

15. Ms Dobbyn's best point is that the allegations of malfeasance made by and against Mr. Kalra and Mr. Chugh in the Connecticut and New York Proceedings will also be made in the Cayman proceeding. The Respondent will contend that the breakdown in their business relationship was brought about by Mr. Chugh's behaviour. Conversely, the Petitioners have given notice of their intention to amend the Petition to include the allegations of malfeasance made in the New York Proceedings against Mr. Kalra. The key witnesses in all these proceedings will be Mr. Kalra and Mr. Chugh. There will be an overlap in the evidence, but the causes of action are obviously different. Evidence about the way in which Mr. Kalra and Mr. Chugh have behaved towards the Company and each other will be relevant in determining whether or not it is just and

equitable to make a winding up order, but this Court will not be required to determine whether either or both of them have acted in breach of fiduciary duty. However, the mere fact that there will be some overlap in the evidence does not lead to the conclusion that the Petition should be stayed. The issues likely to be raised on the Petition are far less complex and more easily adjudicated than those raised in the Connecticut and New York Proceedings. The Petition will be adjudicated long before either of the US proceedings are brought to trial. The remedy of a winding up order is one which can be granted only by this Court. For these reasons I concluded that the Petition should not be stayed.

APPLICATION FOR APPOINTMENT OF PROVISIONAL LIQUIDATORS

16. In order to succeed on their application for the appointment of provisional liquidators, the Petitioners must establish that there is a *prima facie* case for a winding up order and that the appointment is necessary in order to prevent the dissipation or misuse of the Company's assets or prevent mismanagement or misconduct on the part of its directors. I came to the conclusion that the Petitioners have made out a *prima facie* case for a winding up order for the following reasons. As Quin J. has already concluded, the Company is and always has been a quasi-partnership and the Petitioners had a legitimate expectation that they would continue to participate in its management through representation on its board of directors. In the absence of any agreement to the contrary, it is reasonable to infer that the quasi-partners reasonably expected that they would have joint control of the Company through equal representation on its board of directors. By purporting to remove Mr. Chugh from the board, Mr. Kalra succeeded in taking over control of the Company. The Respondent puts forward two defences. First, it relies upon the "buy out offer" which I do not regard as an adequate alternative remedy. Second, it relies upon Mr. Chugh's allegedly flagrant breaches of fiduciary duty as justification for removing him from the board and depriving the Petitioners from exercising any influence or shared control over the Company. Based upon the affidavit evidence, I am unable to reach even a tentative conclusion about the relative merits of the claims and counterclaims which Messrs Chugh and Kalra are making against each other. However, the evidence does point to the conclusion that the Company ceased to carry on its business in 2009 and that no new business will be introduced so long as it is jointly owned. For these reasons I concluded that the Petitioners have made out a *prima facie* case.

17. Mr. Kalra has made it perfectly clear that he intends, if at all possible, to use the Company's money for the purpose of funding both the Connecticut Proceedings and the defence of this Petition. I have no doubt that he will adopt the same approach in respect of the New York Proceedings. In his judgment given on 9th March 2012, Quin J. decided that the Company's money should not be used for funding the Respondent's defence of this Petition. The same considerations apply to the Connecticut and New York Proceedings. Although the cause of action in both cases is a breach of the fiduciary duties owed by Messrs Chugh and Kalra to the Company, they are representatives of the Petitioners and the Respondents for whose benefit this

litigation is being pursued. Even if Mr. Chugh is not the sole beneficial owner of both the Petitioners, they are in fact acting in concert. The Company has no independent interest in the outcome of this litigation. In reality this is litigation between shareholders represented by Mr. Chugh on one side and Mr. Kalra on the other side. The analysis adopted by Quin J. in respect of the Petition applies equally to the Connecticut and New York Proceedings. However, I am not at present satisfied that it is necessary to appoint provisional liquidators in order to prevent Mr. Kalra from misusing and dissipating the Company's money in this way. Assuming that counsel's description of the Company's assets, as they exist today, is not materially inaccurate, it seems to me that it should be possible to secure those assets by means of an injunction without the need to incur the expense of appointing provisional liquidators. In order to ensure that the Court's order is effective and capable, I ordered that Mr. Kalra swear an affidavit verifying the existence and value of the Company's assets. In the event of any failure to comply with this Order, I will give further consideration to the need for appointing provisional liquidators.

DATED this 4th day of September 2012

The Hon. Mr. Justice Andrew J. Jones QC
JUDGE OF THE GRAND COURT

GRAND COURT - CAYMAN ISLANDS