

UPDATE

BVI Commercial Court provides guidance on adverse inferences and the duty to disclose advisors' internal documents

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On 22 September, the Commercial Court of the British Virgin Islands (**BVI**) handed down judgment in *Ace Lead Profits Ltd & Shao Baiqing (the Claimants) v Hollysys Automation Technologies Limited¹ (the Company)*. Mourant acted for the Company in successfully defending the claim, which challenged amendments made to the Company's articles of association (the **Amendments** and the **Articles** respectively). In the judgment, the Honourable Justice Jack provides useful guidance regarding a number of matters, including whether a company is under a duty to disclose its legal advisors' internal documents to shareholders in the context of these proceedings, where these advisors had advised the Company on the Amendments.

Introduction

The Company is a leading automation and IT solutions provider operating across Asia Pacific and other regions. It is incorporated in the BVI and is NASDAQ listed.

Mr Shao was the former CEO and Chairman of the Company. Mr Shao was removed from these posts in July 2020. Mr Shao is the registered shareholder of Ace Lead Profits Limited. Together, the Claimants are the Company's third largest shareholder.

In early 2020, during Mr Shao's tenure, the Company commenced a governance review process and instructed Latham & Watkins (**L&W**) as US Counsel and Maples as BVI Counsel to advise. L&W produced its governance review in April 2020. Other matters took over under Mr Shao's direction such that the corporate governance review was not progressed.

Mr Shao was removed as director and chairman of the Company in July 2020. Following his removal, the newly appointed Chairlady (Madam Qiao) and CEO (Mr Colin Sung) reignited the governance process, first dealing with a rights plan which was due to expire in August 2020, and then turning to other amendments to the Company's Articles to protect it from hostile takeovers.

The Claimants formed a consortium with CPE Fund Management Limited and on 7 December 2020, made a non-binding offer to acquire all outstanding shares of the Company for \$15.47 per share (the **Proposal**). The Company instructed L&W and Walkers (BVI) to advise in relation to the bid. Deutsche Bank was also engaged to assess the price offered. Alongside assessing the Proposal, the Company instructed L&W and Walkers (BVI) to advance the governance review and make recommendations to amend the Articles based on the April 2020 governance review as well as to consider other amendments to bring the Company's constitutional documents in line with current market practice.

The Proposal was rejected at a board meeting on 7 January 2021. At the same meeting, the Company's board passed several amendments to the Articles.

¹ BVIHC(COM) 2021/0015

The Claimants challenged the Amendments on two bases. First, pursuant to section 12(5) of the BVI Business Companies Act (the **Act**) claiming that the Amendments restrict the rights and/or powers of the members of the Company to amend the Articles. Second, that the Amendments are contrary to section 121 of the Act, as they were purportedly made to 'thwart' the Proposal.

The parties agreed to an order that the Company would not act upon the Amendments pending determination of the claim, and the Claimants would not seek to requisition a members' meeting, thereby preserving the status quo pending judgment. The trial timetable was truncated in light of this agreement.

The Judgment

Jack J handed down his considered judgment on 22 September 2021, finding that the Amendments did not contravene section 12(5) of the Act, nor were they implemented for the improper purpose of thwarting the Proposal. Instead, Jack J considered the majority of the Amendments to be clarificatory in nature.

Disclosure of Lawyers' Internal Documents

During the trial, the Claimants had raised issue with a lack of disclosure from the Company's US and BVI Counsel, L&W and Walkers (BVI), regarding the advice on the Amendments given to the Company.

Referring to Jack J's judgment in *IsZo Capital LP v Nam Tai Property Inc et al*² (**Nam Tai**) the Claimants alleged that adverse inferences should be drawn from the lack of disclosure of the lawyers' internal notes and files.

Jack J confirmed that where advice is produced for the benefit of a company, the members of that company have a right to see it,³ and even though that advice is produced by lawyers, a company cannot assert privilege over such documents.

The Company did not dispute that principle. Rather, the Company asserted that it had produced all documents within its power, possession or control (including legal advice) but that its lawyers' internal records were not disclosable as they were not in the Company's power, possession or control. Jack J agreed with that submission at paragraph 22 of the judgment, stating '*Documents created for a client would be within the client's possession power or control and thus disclosable. Internal records of a law firm would not be.*'

Conclusion

The decision confirms that the courts will only draw adverse inferences in circumstances where it can be shown that documents are created for the benefit of a client and have not been disclosed in proceedings or where there has been a deliberate decision to not generate any documents containing advice given to clients, as the court held the position to be in *Nam Tai*. Conversely, documents generated by lawyers for their own internal purposes are not in the power possession or control of their clients, and accordingly are not, without more, disclosable as part of the standard disclosure process in proceedings.

² BVIHC (COM)2020/0165.

³ Para 22.

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