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UPDATE

Seahawk China Dynamic Fund: Grand Court dismisses application to wind-up on the just and equitable basis

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In a recent decision,[1] the Grand Court of the Cayman Islands dismissed a petition for a winding-up order on the just and equitable basis. Based on the evidence before it, the Court found there was no lack of probity and/or justifiable loss of confidence, nor any oppression that was sufficient to justify the relief sought. The Court considered whether the need for an investigation into the affairs of a company could be a stand-alone ground for presenting a winding-up petition. While this issue was not required to be determined on the facts of this case, the commentary from the Court seems to suggest this could be possible in the right circumstances.

Background

Mr Lau Chun Shun (**Mr Lau**) invested in Seahawk China Dynamic Fund (the **Company**), a Cayman company founded by Mr Hao Liang (**Mr Liang**) in August 2017. Pursuant to an investment management agreement (the **IMA**), Gold Dragon Worldwide Asset Management Limited (the **Manager**), a Hong Kong company owned by Mr Lau and his family, was appointed investment manager of the Company. However, Mr Liang directed management of the investments of the Company himself and received a majority of the fees that would normally be payable to the Manager. The Company at all relevant times was solvent and since its inception had been producing significant financial returns for its shareholders.

The relationship between the two deteriorated, with Mr Lau claiming that Mr Liang had:

(a) attempted to siphon approximately US$20m for his own benefit from the Company through the creation of new class of performance shares for himself (the **Unauthorised Scheme**);

(b) diverted monies to a separate entity which he and his wife controlled causing the Company to suffer losses of approximately US$8m (the **Late Trade Allocations**); and

(c) made significant amendments to the Company's constitutional documents and the IMA between the Manager and the Company without formal notice to him (the **Amendments**).

Mr Lau petitioned for the Company to be wound-up on the just and equitable basis, asserting that the Company was a quasi-partnership and the relationship of mutual trust and confidence had irretrievably broken down. Mr Lau further claimed that his legitimate expectations were breached when he was removed as a director of the Company; he had lost confidence in the Company's management on account of serious lack of probity and oppression; and the seriousness of the improprieties asserted by Mr Lau required an investigation into the affairs of the Company.

The Law

The Court set out a useful reminder of when a company may be wound up on the just and equitable basis:

[1] *In the Matter of Seahawk China Dynamic Fund* (unreported, 9 August 2022).

(a) Lack of confidence in management: serious misconduct or serious mismanagement of the affairs of the company by the directors or the majority of shareholders.[2]

(b) Lack of probity in the conduct of the company's affairs: allegations of breaches of fiduciary duties.[3]

(c) Irretrievable breakdown in trust and confidence: where the company is a corporate quasi-partnership and such a breakdown occurs between its participating members. This occurs on the same grounds as would justify the dissolution of a true partnership.[4]

The question of whether the need for an investigation could be a stand-alone ground for a winding-up order was considered in some detail, which included a review of the previous Cayman decisions on this point. A number of first instance decisions such as *GFN Corporation*,[5] *In re Parmalat*,[6] *Paradigm Holdings*,[7] *Madera Technology*,[8] *ICP Strategic Credit Income*[9] and *Washington Special*[10] all held the view, albeit in *obiter*, that the need for an investigation into the affairs of a company was a free-standing ground for the making a just and equitable winding-up order. None of those authorities required an express decision on the point since there was no need to go beyond the consideration of other grounds for winding-up.

Decision

In dismissing the petition, the Court held that none of Mr Liang's actions amounted to conduct that would warrant a winding-up of the Company on the just and equitable basis. The Unauthorised Scheme was not dishonest or lacking probity in the overall context of the relationship and was something Mr Liang was entitled to as part of his performance fees. The Late Trade Allocations amounted to regulatory breaches and could be subject to separate personal legal action, however these trades would not be sufficient to justify a winding-up. The failure to give notice regarding the Amendments was poor corporate governance and the Court signalled its disapproval, but these actions did not amount to dishonesty.

The Court was not satisfied that the relationship between Mr Lau and Mr Liang amounted to a quasi-partnership; Mr Lau and Mr Liang's relationship was only an investor-manager one and there was no agreement or understanding that Mr Lau would significantly participate in the conduct of the business.

Importantly, the Court held that even if it was satisfied that there was some merit to the winding-up petition it would not have granted the order on the basis that there was an alternative remedy available to Mr Lau, namely that Mr Lau could redeem his shares in full, and that he had been unreasonable in not exploring that option seriously.

The Court found the oral evidence provided by Mr Lau lacked credibility and that there was no need for an investigation into the affairs of the Company. On the question of whether such a ground could be a stand-alone basis for the making of a just and equitable winding-up order, the Court commented that it did not consider the first instance judges in the abovementioned cases to be plainly wrong on this point – perhaps hinting that if the question was necessary to address in the future, the Court would hold that such a ground could, on its own, justify a winding-up in certain circumstances.

Comment

While this decision does not break any new ground in the context of the just and equitable jurisdiction of the Court to wind up Cayman entities, it does further demonstrate that the Court will be slow to make such a

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[2] *Tianrui (International) Holding Company Limited v China Shanshui Cement Group Limited* [2019 (1) CILR 481] at para 22.

[3] *In the Matter of Aquapoint LP* (unreported, 23 November 2021) at para 10(11).

[4] *Chu v Lau* [2020] UKPC 24 at para 15.

[5] [2009 CILR 135] at para 37. The Cayman Islands Court of Appeal left the point open for future consideration: [2009 CILR 650] at para 32.

[6] [2006 CILR 171] at para 18.

[7] [2004-05 CILR 542] at para 35.

[8] Unreported, 3 November 2021 at para 76.

[9] Unreported, 10 August 2010 at para 8.

[10] Unreported, 1 March 2016 at para 122.

winding-up order unless there is strong evidence of a lack of confidence in management and/or lack of probity in the company's affairs. Given the serious consequences of making a winding-up order and in effect killing the company, the Court will carefully scrutinise whether the petitioner has considered all alternative remedies, to the extent appropriate.

It remains to be seen whether an investigation into the affairs of a company can be a stand-alone ground for a winding-up petition, although this case seems to be a step closer to recognising that it is.

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