[2014] SC (Bda) 74 Com (23 September 2014)

In The Supreme Court of Bermuda

CIVIL JURISDICTION
(COMMERCIAL COURT)
2014 No. 313

IN THE MATTER OF TITAN PETROCHEMICALS GROUP LIMITED

(PROVISIONAL LIQUIDATORS APPOINTED)

AND IN THE MATTER OF SECTION 99 OF THE COMPANIES ACT 1981

REASONS FOR DECISION
(in Chambers)

Date of Hearing: September 15, 2014

Date of Reasons: September 23, 2014

Mr. Mark Diel and Mr. Kevin Taylor, Marshall Diel & Myers Limited, for the Company

Mr. John Riihiluoma, Appleby (Bermuda) Limited, for the Joint Provisional Liquidators ("JPLs")

Introductory

1. Applications for directions in relation to convening meetings at which schemes of arrangements will be proposed to a company's creditors or shareholders are typically an uneventful ex parte affair, focussing solely on the constitution of classes, the adequacy of the draft explanatory statement and procedural formalities relating to the convening and conduct of the meeting(s). At the hearing of the present application by

the Company under section 99 of the Companies Act 1981 for leave to convene meetings of creditors in Hong Kong to consider and potentially approve a scheme of arrangement, counsel for the company and the JPLs both addressed the Court, *inter alia*, on the apparently novel Bermudian law point of the ability of note-holders to vote as contingent creditors at their class meeting. It was common ground that this Court should follow persuasive judicial authority and practice from a variety of common law jurisdictions and permit voting on this basis.

2. On September 15, 2014, I granted leave to convene the two scheme meetings (Note Creditors and non-Note Creditors) on terms that the Note Creditors would be permitted to vote as contingent creditors at their class meeting. I now give reasons for this decision.

3. Obviously any decision made at an ex parte hearing attended only by parties who were, in practical terms, joint proponents of the proposed Scheme is strictly interlocutory in character. On the other hand, if the Scheme attracts the requisite support and no objector appears to challenge the validity of the votes taken at the meeting, this decision will take effect in final terms.

Structure of Notes

4. The draft Scheme Document contained a chart, 'Diagram of Structure of Notes in Global Form'. This was referred to in Mr. Diel's helpfully fleshy Skeleton Argument. It shows Cede and Co. registered holder of various notes, with Note Creditors holding for their own account, in most instances, through custodians and one or more intermediaries. The Company explained that it was proposed that only Note Creditors would vote on the Scheme. It was submitted that as a matter of law they were contingent creditors because under section 2.04 of the Note Documentation, Note Creditors had the right to call for the issue of a certificated note. Although I did not review the Note Documentation, the terms of clause 2.04 (e) were set out in Mr. Diel's Skeleton Argument as follows:

> "*If at any time the Depositary notifies the Company that it is unwilling or unable to continue as Depositary for such Global Notes or if at any time the Depositary shall no longer be a clearing agency registered under the Exchange Act, the Company shall appoint a successor Depositary with respect to such Global notes. If (i) a successor Depositary for such Global Notes is not appointed by the Company within 90 days after the Company receives such notice or becomes aware of such ineligibility, or (ii) an Event of default has occurred and is continuing with respect to the Notes, the Company will execute, and the Trustee, upon receipt of an Officer's*

Certificate of the Company[1] *directing the authentication and delivery thereof, will authenticate and deliver, Certified Notes (which may bear the Securities Act Legend) in any authorised denominations in an aggregate principal amount equal to the principal amount of such Global Notes in exchange for such Global Notes.*"

5. I understood the structure of the Notes to be as follows. For reasons of administrative and commercial convenience, Note Creditors did not actually hold legal title to the relevant Notes. These were held by a trustee on a global basis although, if they wished, and assuming the Notes were in default, Note Creditors as ultimate beneficial owners could demand the issuance of an individual note, the payment rights relating to which could be enforced on an individual basis against the Company. The Notes were in default. In the event that the Note Creditors exercised their contractual right to convert their indirect pooled interests in the Global Note into individual certificated notes, they would become actual creditors of the Company.

The legal question defined

6. Section 99 of the Companies Act 1981 provides in salient part as follows:

> "(1) *Where a compromise or arrangement is proposed between a company and its creditors or any class of them or between a company and its members or any class of them, the Court may, on the application of the company or of any creditor or member of the company, or, in the case of a company being wound up, of the liquidator, order a meeting of the creditors or class of creditors, or of the members of the company or class of members, as the case may be, to be summoned in such manner as the Court directs.*"

7. This section falls within Part VII of the Act, and the term "creditor" is not defined, either for the purposes of Part VII or the Act as a whole. On the other hand under Part XIII of the Act, it is made explicit that winding-up petitions may be presented by contingent or prospective creditors (section 163), that contingent or prospective creditors may prove in a liquidation (section 234) and that the rules of bankruptcy govern what debts are provable and the valuation of future or contingent liabilities (section 235).

8. Since the Company is in insolvent provisional liquidation, albeit without the directors being displaced so that the Company itself still has standing to apply under section 99(1), a reasonable starting assumption is that the same standing rules should apply to:

[1] It was explained, somewhat elliptically, in the Company's Skeleton Argument that the Company under a deed of covenant was itself obliged to issue certified notes to Note Creditors, in contradistinction to the position in *Re Bio-Treat Technology Limited* [2009] SC (Bda) 26 Civ (28 May 2009); [2009] Bda LR 29. This point should be clarified at any subsequent sanction hearing.

(a) proposing and/or voting on a section 99 scheme promoted in relation to an insolvent company;

(b) presenting a winding-up petition against an insolvent company; and

(c) proving in the liquidation of an insolvent company.

9. The problem with this line of reasoning was that this Court had previously decided that 'note-holders' who did not actually hold notes did not qualify as contingent creditors for the purposes of presenting a winding-up petition: *Re Bio-Treat Technology Limited* [2009] SC (Bda) 26 Civ (28 May 2009); [2009] Bda LR 29 (Bell J). Counsel accordingly felt compelled to distinguish the present case from *Re Bio-Treat Technology Ltd* and/or to demonstrate why it ought to be followed.

10. The crucial legal question placed before the Court was whether or not Note Holders qualified as "creditors" for the purposes of section 99 because they were contingent creditors of the Company.

Why the Note Creditors qualify as creditors for the purposes of section 99 of the Companies Act 1981

Overview

11. I found it easy to conclude that Bell J's decision, which I had myself unquestioningly cited with approval in two previous judgments (one at an earlier stage of the present proceedings)[2] should not be followed in the present case, for three main reasons. Firstly, since judgment was handed down in that case, a new judicial consensus has emerged in several common law jurisdictions with which we have strong commercial and legal ties, that persons the underlying beneficial interest owners in a Global Note has sufficient standing to vote as a creditor at a scheme meeting. Secondly, the crucial facts of the earlier decision as regards the legal relationship between the underlying beneficial owners and the scheme company were materially different. And, thirdly, Bell J's narrow definition of who qualified as a contingent creditor arose in the analogous but different context of determining who had standing to petition to wind-up a company.

12. Although the present Scheme was not being implemented in conjunction with a parallel scheme in Hong Kong, this Court frequently approves parallel schemes linking Bermuda, the UK, Hong Kong and/or Singapore. Those jurisdictions have companies legislation regulating schemes of arrangement which are either identical or substantially similar to sections 99-100 of our own Companies Act. As Bell JA (Acting) more recently himself observed in *Kader Holdings Company Limited-v-*

[2] *Re Gerova Financial Group Ltd.* [2012] Bda LR 20, [2012] SC (Bda) 18 Com (19 March 2012) ; *Saturn Petrochemicals Ltd.-v- Titan Petrochemicals Ltd*. [2013] Bda LR 42, [2013] SC (Bda) 43 Com (10 May 2013).

Desarrollo Inmobiliario Negocios Industriales de Alta Technologia de Hermosilio, S.A. de CV [2014] CA (BDA) 13 Civ (10 March 2014): "*It seems to me sensible that the position in Bermuda should mirror that in England, as well as that in other common law jurisdictions…*" (at paragraph 24). It is true that this observation was made in the context of determining the content of common law rules of private international law. However, the general desirability of a common approach is no less compelling when it comes to construing statutory provisions derived from the same legal roots and which often apply to companies whose operations and restructurings traverse multiple jurisdictional shores.

13. Mr. Diel submitted that it was now common practice in England, Hong Kong and Singapore for underlying beneficial owners of notes to be accepted as eligible to vote as contingent creditors in relation to approval of a scheme. Mr. Riihiluoma submitted that it is equally common for this Court to approve schemes together with parallel Chapter 11 plans in which the underlying owners of notes would vote under the plan. The technical position was that votes under the plan were usually the operative votes, with no separate voting under the scheme actually taking place.

14. To my mind, in substantive and tacit terms, if not in formal and explicit terms, this Court has in the past accepted the principle that the underlying owners of notes ought to be entitled to vote at a scheme meeting, notwithstanding the fact that legal title is vested in a single global note-holder. This acceptance has in the past been based on a practical desire to make legal voting rights reflective of economic reality, in a context where the unified legal title represented by a global note appeared to be based on administrative and commercial convenience rather than legal substance. It has not been based on any considered and technically rigorous legal analysis as to who qualifies as a creditor for the purposes of section 99 of the Companies Act.

15. This intellectually-light approach has also been informed by an appreciation that section 99 is designed to facilitate commercial bargains which attract the support of majorities in value (75%) higher than those required for Chapter 11 plans. Either that support is forthcoming and no sustainable challenges to the fairness of the meeting procedures are advanced at the sanction hearing, or the scheme fails to attract the

requisite support and/or overcome objections advanced at the sanction stage. Where a majority in number representing 75% in value of creditors of an insolvent company agree that the underlying beneficial holders of notes should be entitled to vote and other candidates for voting rights waive those rights, the weight of such commercial consensus provides no encouragement for the sanctioning court to explore theoretical legal impediments to approving the proposed scheme.

<u>Persuasive authority on the meaning of "creditor" in section 99 of the Companies Act</u>

16. Mr. Diel provided highly persuasive authority for the proposition that the term "creditor" should be construed broadly in the section 99 context. In *Re Lehman Brothers International (Europe) (in administration)* [2009] EWCA Civ 1161, the English Court of Appeal was considering whether or not the holders of proprietary trust claims over the company's assets qualified as creditors for the purposes of a proposed scheme of arrangement. The unanimous decision of the Court of Appeal was that creditor claims were wholly distinct from trust claims. In the course of reaching this conclusion, approval was given to earlier judicial pronouncements about the breadth of the term "creditor" in the scheme context. Patten LJ, delivering the leading judgment and summarising the arguments of the Respondent's counsel which he ultimately accepted stated:

> "*29.There is no statutory definition of "creditor" or "arrangement" for the purposes of Part 26 and, in relation to "arrangement", the courts have been careful not to attempt to provide one beyond the limited criteria described in Re NFU Development Trust Ltd. But Mr Snowden contends that, in order to be a creditor of the company, it is necessary to be owed money either immediately or in the future pursuant to a present obligation or to have a contingent claim for a sum against the company which depends upon the happening of a future event such as the successful outcome of some litigation. Although a creditor for the purposes of Part 26 is not therefore limited to someone with an immediately provable debt in a liquidation, it does require that person to have a pecuniary claim against the company which (once payable) would be satisfied out of the assets as a debt due from the company.*
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> *30.As support for this, we were referred to the decision of the Court of Appeal in Re Midland Coal, Coke & Iron Company [1895] 1 Ch 267 in which it was accepted that a person with a contingent claim against*

the company qualified as a creditor under a scheme of arrangement made under the Joint Stock Companies Arrangement Act 1870. Lindley LJ (at page 277) said that he agreed that:

> *'... the word "creditor" is used in the Act of 1870 in the widest sense, and that it includes all persons having any pecuniary claims against the company. Any other construction would render the Act practically useless."*

31. Based on this decision, David Richards J concluded in Re T&N Ltd [2005] EWHC 2870 Ch that persons with contingent claims for damages against a company were creditors within what is now Part 26:

> *'[40] In my judgment, "creditors" in s 425 is not limited to those persons who would have a provable claim in the winding-up of the company, although it clearly includes all those who would have such a claim. As was submitted by Mr Snowden and other counsel, one of the recognised purposes of s 425 is to encourage arrangements with creditors which avoid liquidation and facilitate the financial rehabilitation of the company: see, for example, Sea Assets Ltd v PT Garuda Indonesia [2001] EWCA Civ 1696 at para 2. This suggests that as wide a meaning as possible should be given to "creditors" in the section. Having said that, it is important to bear in mind that s 425 is designed as a mechanism whereby an arrangement may be imposed on dissenting or non-participating members of the class and such a power is not to be construed as extending so as to bind persons who cannot properly be described as "creditors".'*"

17. This *dictum* supports the proposition that a more liberal test for creditor potentially applies under section 99 of the Bermudian 1981 Act than arises in relation to determining who can petition and/or prove in a winding-up under sections 163 and/or 174-175 of the same Act. The Master of the Rolls in *Re Lehman Brothers International (Europe) (in administration)* [2009] EWCA Civ 1161 agreed with Patten LJ both generally and on the general approach to construing the term "creditor" in relation to schemes of arrangement. Lord Neuberger[3] stated:

[3] The transcript does not name the Master of the Rolls, but the case was heard on October 26 and it is a matter of record that Lord Neuberger assumed this office on or about October 1, 2009.

> "*74. It has been held that the expression "creditors" in section 895 should be given a wide meaning (see Re Alabama, New Orleans, Texas, and Pacific Junction Railway Co [1891] 1 Ch 213, 236-237 and Re Midland Coal, Coke and Iron Co [1895] 1 Ch 267, 277), and the same principle seems to apply to the meaning of "arrangement" (Re Savoy Hotel Ltd [1981] Ch 351, 359 and 361). Bearing in mind the purpose of section 895, as discussed by David Richards J in Re T&N Limited (Number 1) [2006] 1 WLR 1728, paragraphs 32-40, and in Re T&N Limited (Number 3) [2007] 1 BCLC 563, paragraphs 43-55, it is plainly right that that is so.*"

18. The Company's Skeleton Argument also referred the Court to recent English authority which has directly considered the question of whether underlying note-holders qualify as contingent creditors for the purposes of voting on a proposed scheme of arrangement. Mr. Riihiluoma for the JPLs referred the court to the most comprehensive analysis on what contingent claims were admissible for voting purposes, followed by two cases concerning the specific topic of voting by the economic interest owners in notes: *In re T & N Ltd et al* [2006] 1 WLR 1728, [2005] EWHC 2870 (Ch) (David Richards J); *Re Castle Holdco 4 Limited* [2009] EWHC 3919 (Ch) (Norris J); and *Re Cooperative Bank Plc* [2013] EWHC 4072 (Ch) (Hildyard, J).

19. *In re T & N Ltd et al* [2006] 1 WLR 1728 concerned whether or not contingent tort claimants could vote on a proposed scheme of arrangement. The apparently novel finding was that persons who might in future suffer loss and acquire a claim in tort were creditors for the purposes of voting on a proposed scheme even though they could not prove in a winding-up. The reported judgment of David Richards J runs to 63 pages, and his central reasoning was approved by the Court of Appeal in the *Lehman Brothers* case referred to above. Mr. Riihiluoma referred me to the following paragraph in the judgment which I accept represents the Bermudian law position in relation to section 99 of the Companies Act 1981:

> "*46.The present state of the authorities therefore shows that (i) the holder of a contingent claim is a creditor for the purposes of the provisions governing both schemes of arrangement and CVAs and (ii) the claim need not be a provable debt. The nature of contingent claims is such that a creditor for these purposes need not have an accrued*

> *cause of action. To take the simple example of an uncalled guarantee, the person with the benefit of the guarantee will be a "creditor" of the guarantor, even though there has not been, and may never be, any default on the principal debt or any call on the guarantee.*"

20. David Richard J's judgment was handed down on December 14, 2005. Just over three years later, Norris J, seems to have considered it obvious that the underlying beneficial owners of notes ought to be permitted to vote on a proposed scheme. His decision in *Re Castle Holdco 4 Limited* [2009] EWHC 3919 (Ch) is particularly persuasive, because the facts were remarkably similar to those in the present case. Norris J held (at pages 8 to 9 of the transcript):

> "23. *When the Scheme of arrangement comes to be considered, it ought obviously to be considered by those who have an economic interest in the debt, that is to say, by the ultimate beneficial owner or principal. Castle Holdco itself is not generally concerned with who is the ultimate beneficial owner. Indeed the security documents themselves contain a provision that Castle Holdco shall treat the common depository or its nominee as the absolute owner of the global security for all purposes. However, the security documentation does contain a mechanism whereby the beneficial owner can upon request become a direct creditor of Castle Holdco.*
>
> *24. On the occurrence of an event of default, there is a provision that the global security is to be transferred to the beneficial owners in the form of definitive securities upon the request by the owner of a book entry interest. It has been submitted to me, and I accept, that the ultimate beneficial owners may therefore be properly regarded as contingent creditors of the company and indeed of each of the subsidiaries who have provided a guarantee.*
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> *25. Accordingly, when the meeting is convened, it is to those principals or beneficial owners that the relevant notices ought ultimately to be directed, and it is their vote not the vote of the common depository or of the nominee which will count. To avoid any danger of double-proof or*

double-counting of votes, in each Scheme the common depository has undertaken not to vote."

21. That judgment was given on an application which was not opposed. However, it was followed by Hildyard J in a case which was contested in *Re Cooperative Bank Plc* [2013] EWHC 4072 (Ch). Mr. Riihiluoma referred me to the following instructive passages in Hildyard J's judgment which I fully adopt:

> "36.*It remains for me to determine matters of procedure in respect of the single class meeting. In that regard there is one what one might call a wrinkle. This is that instead of the trustees under the trust deeds on which the notes are held voting, it is proposed that those beneficially interested in the relevant debt instruments should vote in the place of trustees, who will therefore not vote.*
>
> *37. This caused me some initial anxiety, since of course the statutory enabling of a scheme depends upon the votes of creditors by the prescribed margin. I was concerned lest, for all the economic sense of the matter, nevertheless persons beneficially interested under a trust might not be considered to be creditors for the purposes of the statutory jurisdiction.*
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> *38. I was assisted in this regard by reference to three decisions of Mr Justice Norris: In the matter of Castle Holdco 4 Limited [2009] EWHC 3919 (Ch), In the matter of Gallery Capital SA and In the matter of Gallery Media Group Limited [2010] WL 4777509. None of those schemes was opposed, so the Judge did not have on either occasion the benefit of dialectic argument, but nevertheless the conclusion that he reached (which was that in the particular context the beneficiaries could be treated as contingent creditors and that as such they could be treated as creditors for the purpose of the relevant provision in the Act) seems to me to be both logical and justified. I say that with diffidence, but his reasoning seems to me to be entirely justified.*
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> *39. I note also that in the case of Re T&N Limited and others [2005] EWHC 2870 (Ch) Mr Justice David Richards included contingent creditors within the definition of creditors. That appears also to be justified by subsequent authority: the right of those beneficially interested to call for the legal interest is analogous to the position of a contingent creditor.*
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> *40. I have stressed that my conclusion in that regard is case-specific, it being the case here that the beneficiaries have an absolute right to require the Bank to issue definitive notes directly. It seems to me that since there is such a mechanism to trigger a direct right and therefore obtain control over that contingency, which is defined, they are properly described as contingent creditors and thus as creditors for the purposes of the relevant provision of the Act.*" [emphasis added]

22. This analysis appears to me to follow a traditional approach to determining who qualifies as a contingent creditor, not discernibly different from the test applicable in the winding-up petition or proof of debt contexts. I found that it supported the submission that the Note Creditors ought properly to be accepted as entitled to vote on the proposed Scheme as contingent creditors.

The status of *Re Bio-Treat Technology Limited*

23. For completeness I should add that this finding is based on facts which are crucially different to those in *Re Bio-Treat Technology Limited,* referred to above. It is true that the same test as to who is a contingent creditor has been applied in both cases. However here, the position has been represented as being that under the Note Documentation the Note Creditors have the contingent right to require the Company to issue a definitive note in the event of default. The corresponding right in *Re Bio-Treat Technology Limited* could only be asserted against the global note holder or trustee. In that case, Bell J pivotally concluded:

> "*49.Indeed, as Mr. Hargun pointed out, this appears to have been Highbridge's understanding; when Highbridge wished to take advantage of the Company's default and convert its interest in the global bond to definitive bonds, it wrote not to the Company, but to the Bank of New York, by letter dated 25 February 2009, and it directed its notices towards the Bank of New York as opposed to the Company, in the following terms:*
>
> > *'We hereby give BoNY notice that we require the Company to exchange the global bond for definitive bonds. We require BoNY to convey our direction to the Company and take all necessary steps to effect an exchange within the timeframe contemplated by the Bonds.'*
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> *50. I do therefore accept Mr. Hargun's contentions on behalf of the Company, and find that, prior to the issue of definitive bonds, Highbridge cannot be said to have the requisite contractual relationship with the Company, as is necessary to found the status of contingent or prospective creditor. I therefore find that pending the issue of the definitive bonds to Highbridge, it is neither a contingent nor a prospective creditor of the Company, and hence does not have locus on this ground to present a winding-up petition.*"

24. Nothing in the present Judgment should accordingly be read as in any way doubting the soundness of the factually and legally distinguishable case of *Re Bio-Treat Technology Limited* [2009] Bda LR 29, particularly as regards the standing of contingent creditors to present winding-up petitions.

Conclusion

25. For the above reasons on September 15, 2014 I found that the Note Creditors were entitled to vote on the proposed Scheme as contingent creditors.

Dated this 23rd day of September, 2014______________________

IAN RC KAWALEY CJ