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BVI Commercial Court clarifies relevant date to assess Liquidators' sanction applications

The BVI Commercial Court recently delivered a landmark judgment[1] clarifying when a liquidator's decision should be assessed if 1) there has been a change in circumstances and 2) the stakeholders to the liquidation do not support a liquidators' decision.

Background

Luckin Coffee Inc ("**Luckin**") is a large café business which operates one of the largest coffeehouse businesses in PRC (referred to as the "Starbucks" of PRC). In the first half of 2020, a fraud was discovered in its accounting which resulted in it being placed into a light touch provisional liquidation in the Cayman Islands. Its shares which were listed and traded the on NASDAQ were suspended.

Summer Fame Limited and Haode Investment Inc, along with two Cayman entities Primus Investments Fund LP and Mayer Investments Fund LP, were vehicles through which the former chairman of Luckin (Mr Lu) held his shares. Summer Fame, Haode, Primus and Mayer (together, the "**Liquidation Entities**") were all placed in to liquidation in the summer of 2020 following the discovery of the Luckin fraud and the consequential crash in Luckin's share price. As part of the liquidation of Summer Fame and Haode and Primus and Mayer, the joint liquidators sought to sell the shares in Luckin held by the Liquidation Entities (which were, materially, their only assets) in order to satisfy creditors.

Sale of Liquidation Entities' Assets and Sanction Application

Following a thorough and transparent sales process which included three-way bidding after consultation with the stakeholders, the joint liquidators determined to enter into a securities purchase agreement on 14 August 2021 with Camel (the "**Centurium SPA**"). Under the Centurium SPA, the creditors of the Liquidation Entities would be paid in full (including accrued interest) and there would be a surplus of approximately US $80million to the shareholders of the Liquidation Entities (which included Mr Lu). At that time, over 52% of the creditors supported the Centurium SPA.

After the Centurium SPA had been signed on 14 August 2021, the make-up of the creditors to the Liquidation Entities changed such that only two creditors remained, Golden Planet and Guangshi Wealth, each of which had had purchased the debts of all other creditors. Golden Planet and Guangshi Wealth, along with the shareholders, objected to the Centurium SPA.

The liquidators sought Court sanction of their decision to cause the Liquidation Entities to enter into the Centurium SPA, as was required under the terms of that agreement. The sanction application was ultimately brought on 15 September 2021, by which time the joint liquidators had been made aware that the views of 100% of the stakeholders objected to the Centurium SPA[2].

The sanction application was heard by Justice Jack on 16 and 17 December 2021 where the key question before the Court was whether the Court should determine the sanction application based on the date the decision by the liquidators was taken to enter into the Centurium SPA, i.e. 14 August 2021, or the date that the application was being heard in December 2021.

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[1] *In the matter of Summer Fame Ltd and Haode Investment Inc (in liquidation), BVIHCOM 2020/55 and 56*

[2] Golden Planet, Guangshi Wealth, and the shareholders also entered into a debt restructuring agreement as between themselves through which they proposed to restructure the debts of the Liquidation Entities, and which they argued presented a better deal to the shareholders than the Centurium SPA.

Decision of the BVI Commercial Court

Justice Jack acknowledged the right of the liquidators to seek protection from the Court against criticism from and any liability to stakeholders in respect of 'Category 2' applications. These were defined in Re Nortel Networks UK Ltd [2016] EWHC 2769 (Ch) as a liquidator's decisions which are "*momentous"* in their nature. Justice Jack decided that the relevant date was the 14 August 2021 (despite the dearth of authority on the point) and noted that:

"*…post-agreement events are irrelevant.*

This accords with the purpose of the grant of sanction. The risk which a liquidator runs in making an agreement without the Court's sanction is that the liquidator might have a personal liability if he or she has erred in their assessment of the commercial desirability of the agreement. The Court when deciding whether to grant sanction applies essentially the same test: is the liquidator acting within the reasonable bounds of a commercial decision-maker when he or she makes the agreement in question. This points strongly to the test being that applicable at the moment when the liquidator makes the agreement for which he or she seeks sanction."

Justice Jack also held that, when assessing sanction applications more generally:

1. The Court was not bound to have regard to the views of creditors on an application for sanction, although it might be appropriate for it to do so;
2. The Court is not bound to act in accordance with the views of the majority of creditors nor even if there is unanimity amongst the creditors;
3. The Court will consider the wishes of creditors and contributories;
4. Creditors views may be discounted where they would be unaffected whichever way the decision of the Court goes;
5. Issues of non-commercial motive can potentially create difficulties (both abstract and concrete) to the giving of sanction

A copy of the judgment can be found here.

The Judgment will be of particular relevance to insolvency practitioners acting in a Court appointed capacity where the stakeholders do not hold unanimous views on or oppose a course of action the liquidators wish to take. Whilst the Court was sympathetic to liquidators wishing to protect themselves from criticism, it also noted that had the Centurium SPA not been entered in to in August, it would have not granted sanction because of the unanimity amongst stakeholders.

Bhavesh Patel of Travers Thorp Alberga and Stephen Atherton QC of Twenty Essex chambers successfully represented Camel Humps Ltd (the vehicle used by Centurium Capital to acquire the shares in Luckin) in this matter and obtained the sanction that was sought from the BVI Court (effectively making the application in the liquidators' stead). Consequent to the BVI Court's decision, Centurium Capital were able (being advised by a multijurisdictional legal team led by partners at Kirkland & Ellis and Travers Thorp Alberga) to complete the over $400m deal to purchase the shares of the Liquidation Entities, pursuant to which Centurium is now the majority shareholder of Luckin Coffee Inc, holding more than 50% of its voting interest.