IN THE GRAND COURT OF THE CAYMAN ISLANDS

FINANCIAL SERVICES DIVISION

Cause No FSD No. 112 of 2017(RPJ)

IN THE MATTER OF THE COMPANIES LAW (2016 REVISION)

AND

IN THE MATTER OF KONGZHONG CORPORATION

IN CHAMBERS

Appearances: **Mr James Elliott and Ms Madeleine Heal of Harney Westwood & Riegels in Cayman on behalf of the Company.**
Mr Robert Levy QC via video link in London, Mr Rocco Cecere and Ms. Nicosia Lawson of Mourant Ozannes on behalf of Maso Capital Investments Limited, Blackwell Partners LLC – Series A,, Kevin X Lu and Haifeng Tang

Before: **The Hon. Justice Parker**

Heard: **4 December 2017**

Draft Judgment Circulated: **19 December 2017**

Judgment Delivered: **2 February 2018**

HEADNOTE

Section 238 Companies Law (2016 Revision) - Court's approach to Directions hearing-overriding objective-dissenter discovery-industry experts-management meetings.

Introduction

1. On 4 December 2017 I heard a contested summons for directions issued by Maso Capital and Blackwell Partners (the terms of which were agreed by the two individual dissenters, Kevin X Lu and Haifeng Tang) (together the dissenters) in proceedings under section 238 of the Companies Law (2016 Revision) by which it

will be this court's function to determine at trial the fair value of shares in KongZhong Corporation (the company).

2. The company is a Cayman Islands exempted limited company whose operations and business has been conducted in the People's Republic of China (PRC). In the Petition the company has described itself as an:

"Online games developer and operator based in the PRC operating three main business units namely Internet games, mobile games, and wireless value-added services".

3. The dissenters were all shareholders in the company and until completion of the merger transaction the company's American Depository Shares were listed on the NASDAQ global market exchange.

4. The company was "taken private" using the statutory merger provisions found in Part XVI of the Companies Law. To effect the merger the company made its shareholders a cash offer in exchange for which the shares would be cancelled. The dissenters rejected the offer. The merger took effect shortly after 13 April 2017 and as part of the process the dissenters exercised their rights to dissent from the merger in accordance with section 238 of the Companies Law.

5. As the dissenters and the company were unable to agree upon a price to be paid for the dissenters' shares the company issued a Petition to determine the fair value of its shares on 5 June 2017.

6. The volume of mergers and acquisition activity concerning Cayman domiciled entities within a corporate structure where the ultimate operating company is in the PRC has grown markedly over recent years. There have been a number of section 238 cases since Jones J considered and gave guidance on the Court's approach to the process in *Integra* (28 August 2015 (unreported)).

7. Since *Integra* these cases have attracted some further interlocutory activity in the Financial Services Division of the Grand Court and the judges have begun to establish the legal framework, principles and procedures applicable to fair value cases. Two such cases have proceeded to a trial. No doubt many others have settled on the way.

8. The directions for such cases are specifically tailored to the court's approach and its designated function pursuant to the statute. In some cases there has been a dispute about the directions which has led to a reasoned ruling. In most cases however, it appears that many of the principal directions have been agreed by the parties.

9. These directions usually relate to arrangements for the establishment of an electronic data room, and the way in which data is uploaded with certain specific

classes (of obviously relevant documents that the company ought to possess) to be uploaded quickly. Other documents which are relevant to the consideration of fair value are subsequently uploaded. Dissenters have not to date been ordered to provide discovery of documents.

10. There are then usually provisions relating to the interrogation by the experts of the information provided by the company providing always that the company may apply to the court to be relieved of any such request. And finally there are provisions relating to meetings to be held between the experts and the company's management to obtain further or better information to allow them to prepare their evidence with which to assist the court.

11. In at least two cases, namely *Homeinns* (12 August 2016) and *Qunar* (20 July 2017) (both unreported) the directions were heavily contested. The former was a decision of Mangatal J and the latter was my own decision which is currently on appeal before the Court of Appeal.

12. This summons is likewise heavily contested and I agreed with counsel who appeared at the hearing, Mr Levy QC on behalf of the dissenters, and Ms Heal on behalf of the company, that I would reserve and deliver a reasoned judgment which dealt with the principal issues in dispute between the parties and which provided an indication of my views on the other, more minor issues, that had not been agreed. This is so that both counsel and their respective teams could finalise a draft Order for me to approve in relation to the disputes on the competing draft orders which had been exchanged.

13. Before I do so I set out my approach to these case management issues in section 238 cases.

14. First, I direct myself as to the correct approach to follow from the cases decided in this jurisdiction, starting with the decision of Jones J in *Integra* (and the other cases to which I have already referred) that have dealt with section 238 Companies Law cases.

15. Second, I of course apply the overriding objective to deal with the case in a just, expeditious, and economical way. In this regard unnecessary delay needs to be avoided.

16. Third, I have regard to, (but am not bound by), the directions orders made in the s.238 Companies Law cases that have been made available to me (I have reviewed those in *Qunar, Qihoo 360, Homeinns, Bona Films, Mindray and Shanda Games*).

Principal issues in dispute

Adjournment

17. Ms Heal urged me to adjourn the hearing of this summons because, she submitted, most of the issues were the subject of argument before the Court of Appeal from my decision in *Qunar* which was heard fairly recently in November 2017. Having reviewed the transcript of the hearing I am not persuaded that most of the issues between the parties in relation to this directions hearing are in fact currently before the Court of Appeal.

18. Mr Levy QC who appeared in the Court of Appeal, referred me to a number of places in the transcript which suggested that some parts of the appeal were not being pursued and/or were abandoned.

19. Be that as it may, there is certainly one live issue which is before this court and the Court of Appeal: namely dissenters' discovery. This at first instance has been consistently refused by the Grand Court. However, in circumstances where there is no specific date upon which the Court of Appeal's decision is expected, it seems to me that the overriding objective would be best served by proceeding to finalise these directions. If the Court of Appeal provides guidance in relation to this issue which overturns the decisions in *Homeinns*, *Qunar* and *Trina* (2 November 2017, unreported, Segal J) I do not consider that there would be any prejudice to the company as no doubt it would renew its application for discovery (with or without grounds) from the dissenters in accordance with any such guidance. I therefore refused to adjourn the hearing.

Discovery by dissenters

20. I can deal with this point quite shortly. Unless and until the Court of Appeal overturns the approach taken in the three cases I have referred to above, dissenter discovery is not automatic in section 238 cases. In *Qunar* an application for specific disclosure was made and I decided that I was not persuaded by the evidence adduced by the company that I should order it in that case and gave my reasons. These seem to accord with Segal J's observations in a subsequent case when similarly refusing such an application - *Trina*.

21. I did not rule out disclosure by dissenters in s.238 cases but held that:

> *"The court would require very clear grounds upon which to make such an order which would be solely directed towards assisting the court in determining fair value. The court would, under order 24 rule 8, have to be satisfied the discovery was necessary under rule 3 and would not make an order if it was not necessary either for disposing fairly of the cause or matter or for saving costs. The overriding objective would also need to be satisfied to ensure that the substantive law was rendered effective and that it was carried out consistently with saving expense and dealing with the matter proportionately."*- Paragraph 65.

22. In this matter the company has provided no evidence in support of its contention that dissenter disclosure is necessary either for disposing fairly of the matter or for saving costs. Of course if the appeal in *Qunar* is successful and it is decided that disclosure can be ordered against dissenters without clear grounds being made out to the satisfaction of the court, it is open for the company to reapply for disclosure in the terms sought. It is also of course open to the company to apply for specific discovery at any stage under the "Liberty to apply" provision together with evidence to support the application.

Industry experts

23. Ms Heal, for the company, argued that industry experts should be appointed at the direction of the court and asked to opine (among other things) on the macro economic climate facing the online gaming industry, the competitive environment, emerging markets, the regulatory environment and other factors determining a company's market position. Again the company produced no evidence to explain why the gaming sector is so distinctive that to properly understand how to approach the valuation of a company within it, an industry expert (in addition to valuation experts) is needed to further assist the court. The experts who will be of critical assistance to the court are of course those appointed by the parties at the direction of the court who are experts at valuing companies. In the *Shanda* case (25 April 2017 unreported) Segal J was assisted by experts in company valuation (with no additional industry experts). From his careful and detailed judgment I note that the expert evidence showed a good understanding of the company's business (which also happened to be online gaming in China). I am not persuaded at this stage that the time and costs associated with the appointment of industry experts is justified or proportionate, applying as I do the overriding objective. If the company wishes to make an application supported by evidence for industry experts it is at liberty so to do. In this regard I note in passing that in *Trina* the parties agreed to an industry expert. It may be that if the company were to provide evidence to show why the court would be assisted by industry experts notwithstanding the increased time and expense which would follow as a consequence, the matter could be looked at again more favourably by both the dissenters and the court.

Management meetings

24. Again I have received no evidence from the company on this point, but I understand from the submissions made by Ms Heal that the company is not content to allow the experts to meet with appropriate members of its management team. It is clear from Segal J's decision in *Trina* that he decided that the court has jurisdiction to order such a meeting to take place. I respectfully agree with him.

25. I also take the view that in this case the parties should proceed on the basis that such a meeting is "open" so that the experts are entitled to refer to and rely upon

any information obtained during the course of such meetings in helping them to prepare their reports, unless good arguments are advanced as to why that should not be the case. I note in passing that I am not following Segal J's approach in *Trina* as to the status of discussions held at such meetings (i.e. that they should be held "without prejudice" so that nothing said in the meeting is admissible as evidence unless the parties agree to waive the without prejudice privilege). I am of course not privy to the specific facts and circumstances which pertained in *Trina.*

26. It seems to me that it would be much more productive if the experts were able to rely on information obtained at such meetings. If in this case any party wishes to suggest that the experts should not rely on information obtained at these meetings for the purposes of their reports (i.e. to the extent that they consider it relevant to the question of fair value) they may apply to the court with reasons as to why that should be so.

Delaware expert

27. Ms Heal accepted that at this stage the company has not produced evidence so as to comply with paragraph B5.1 (a) of the FSD Guide to identify which issues in the proceedings the proposed expert evidence related to. For the time being she was content that to the extent that Delaware law expert evidence is required, the parties will be able to apply under the 'Liberty to apply' provisions of the directions order at the appropriate stage. That to my mind is a very sensible outcome and is in keeping with the overriding objective.

28. I turn now to my views on the respective directions sought by each party in their draft orders.

Other issues

29. I will indicate the paragraph number of the draft relating to each of the directions proposed by the parties, first the dissenting shareholders and then the company at the beginning of each issue for ease of reference.

    1:1 I prefer the language proposed by the dissenters. There is no need for the additional wording proposed by the company.

    2:2 The period should be one week from the date that the order is approved by the Judge.

    3:3 The wording should be: *"The costs of hosting the data shall be costs in the proceedings. The Company shallbear the ongoing costs while the proceedings are extant."*

4:4 I have given my decision on industry experts and the term 'advisers' will include counsel. I prefer the language proposed by the dissenters.

5:5 I have given my decision on dissenter discovery. There is no need for written consent in relation to usage reports. I prefer the language proposed by the dissenters.

6 I am content with the language proposed by the dissenters. The documents should be uploaded in their native form without password protection. Clearly if they are protected in their native form by passwords, they should be provided so that the documents may be reviewed by the experts. All parties should be given access rights to the documents including the right to download and print documents from the data room.

7:6 The period should be two weeks from the date that the order is approved by the Judge. There is no reason to shorten the period of disclosure to anything less than five years prior to the valuation date. That is a reasonable period of time over which to assess the relevant matters. Absent any evidence from the company as to why this should not be the case this seems to me to be a necessary and proportionate period concerning the exercise of a fair valuation and was adopted in Qunar. There is also no reason to limit the documents as suggested by the company to categories (a) to (f) of Appendix 2. The company should initially upload all of the classes of documents in Appendix 2.

8:7 All *other* documents should also be uploaded. The period should be three weeks from the date that the order is approved by the Judge.

8 (company proposal) For the reasons I have given there should be no dissenter discovery at this stage.

9 The period should be three weeks from the date that the order is approved by the Judge and I am content with the language proposed by the dissenters.

10:9 I have given my decision on dissenter discovery and prefer the language proposed by the dissenters.

11:10 I prefer the language proposed by the dissenters.

Factual evidence

15:11 and 16:12	I prefer the language proposed by the dissenters, save that 21 days' notice (as proposed by the company) should be given (rather than 14 days) in relation to attendance for cross-examination at the hearing.

Valuation Experts

13 to 21 (company proposal)	I have given my decision as to industry experts.
12:22	I prefer the language proposed by the dissenters and have given my decision on industry experts.
24 (company proposal)	I am content to approve that the valuation experts reports should be prepared in accordance with the rules for expert witnesses in the FSD guide - see also paragraph 17(ii) of the dissenters' draft.
13:25	I prefer the proposed language in the dissenters' draft.
14	I have given my decision on the management meetings and am content with the dissenters' draft language.
17:26	Valuation reports should be exchanged simultaneously 90 days from the second tranche of documents - I prefer the language and the dissenters' proposed draft.
18/19:27	I prefer the language that the company proposes allowing as it does for electronic communications.
20:29 and 21:30	No real difference between the parties and I am content to approve language which reflects that only one set of experts is ordered at this stage.
31 (company proposal)	I have given my decision refusing permission at this stage to adduce evidence of Delaware law which is related to the dissenter discovery issue.
26:38	I am content that for the time being, in keeping with the decisions I have made, a seven (not nine) day trial is ordered.

THE HON. JUSTICE PARKER
JUDGE OF THE GRAND COURT

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