

HONG KONG / JUDGMENT

RE POLY INVESTMENTS HOLDINGS LTD

COURT

Court of First Instance

DECIDED

23 January 2007

CASE / FILE NUMBER

HCMP2511/2006

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REASONS FOR JUDGMENT

This petition was presented by Poly Investments Holdings Limited (the Company) to seek a confirmation of the cancellation of the share premium account and a reduction of its capital, under section 59(1) of the Companies Ordinance, Cap. 32. The Company was incorporated on 11 September 1987 as a private company limited by shares under its former name. Its name was changed to its present name by a special resolution passed on 21 October 1993. The Company acts as an investment holding company and the principal activities of its subsidiaries consist of power generation, iron ore trading, provision of finance, and securities brokerage and investment. The present authorised share capital of the Company is \$900,000,000 divided into 1,800,000,000 ordinary shares of \$0.50 each. As at 13 November 2006, 1,214,117,000 ordinary shares have been issued and are fully paid up or credited as fully paid up. The issued and paid up capital amounts to \$607,058,500. The shares of the Company are listed on The Stock Exchange of Hong Kong Limited (the Stock Exchange). As at 29 November 2006, there is at present standing to the credit of the share premium account the sum of \$2,252,116.74. There is provision in the articles of association that the Company may by special resolution reduce its share capital, any capital redemption reserve fund or any share premium account in any manner authorised and subject to any conditions prescribed by law. By a special resolution of the Company duly passed at an extraordinary general meeting held on 8 November 2006, it was resolved that conditional upon the Listing Committee of the Stock Exchange granting the listing of and permission to deal in the shares of \$0.10 each in the issued share capital of the Company, and the capital reorganisation becoming effective on the registration of the order confirming reduction of capital,

- (1) the authorised capital be reduced from \$900,000,000 divided into 1,800,000,000 shares of \$0.50 each to \$18,000,000 divided into 1,800,000,000 shares of \$0.01 each and that such reduction be effected by cancelling capital paid up or credited as paid up to the extent of \$0.49 per share upon each of the shares and by reducing the nominal value of all the issued and unissued shares from \$0.50 to \$0.01 per share;
- (2) subject to and forthwith upon the capital reduction taking effect: every 10 shares of such 1,800,000,000 shares of \$0.01 each be consolidated into one share of \$0.10 each in the capital of the Company; the authorised share capital be increased to \$900,000,000 by the creation of 8,820,000,000 new shares of \$0.10 each;
- (3) the share premium account of the Company be reduced to nil and the credit arising from such reduction be set off against the accumulated losses of the Company;
- (4) subject to the capital reduction taking effect, the credit arising from the capital reduction be set off against the accumulated losses of the Company and the balance be credited to the share premium account or such other reserve as the court may direct. The details of the proposed capital reorganisation and capital reduction were set out in a printed circular dated 16 October 2006 and despatched to all shareholders and served on the auditors of the Company. The reasons for the proposed capital reduction and cancellation of the share premium account were given in the circular. The reasons are two-fold: to enable the Company to apply the credit arising from the capital reduction to eliminate its accumulated losses, so as to bring forward the time when the Company would be in a position to declare and pay dividends; and to facilitate future equity fund raising exercises by the Company, in light of the fact that the shares have been trading at below par value for some time. As at 30 June 2006, the Company had accumulated losses to the extent of \$160,114,100.90, which were mainly attributable to general and administrative expenses, finance costs, loss on disposal of fixed assets, loss on disposal of investments in listed securities, loss on disposal of a subsidiary, loss on disposal of an associated company, provision for investments in listed securities, provision for amounts due from subsidiaries, provision for investments in subsidiaries, and extraordinary items. That part of the paid-up capital has been lost effectively and is no longer represented by available assets. It is proposed to apply in full the entire credit of \$2,252,116.74 arising in the books of account as a result of the cancellation of the share premium account, and part of the credit of \$594,917,330 arising in the books of account as a result of the cancellation of capital paid up to the extent of \$0.49 per share upon each of the issued shares, towards the elimination of the accumulated losses. By reason of section 79B, the Company will remain unable to pay dividends while substantial accumulated losses exist. The proposal to set off the accumulated losses with the credit arising from the capital reduction and cancellation of the share premium account would bring the Company's accounts more nearly into line with its available assets and if the Company should return to profit from the operations of the group, bring forward the time when it would be in a position to pay dividends. Since July 2001, the shares of the Company have been trading on the Stock Exchange at prices below their nominal value of \$0.50 per

share. Under section 50, a company may not issue shares at a discount to the nominal value of such shares unless, inter alia, the issue is authorised by a resolution of the members of the company and is sanctioned by the court. On the premise that the market price of the shares of the Company would remain depressed in the near future, and if the Company were to raise capital by issuing new shares, the directors considered the procedure under section 50 too cumbersome and costly and would not best serve the needs of the Company. Furthermore, due to the time frame involved in an application under section 50, underwriters and placees would not be willing to assume the inherent risk of movement in the share price. The directors considered it desirable to reduce the nominal value of the shares so as to avoid the necessity for an exercise under section 50 to be undertaken each time the Company should wish to raise funds. The Company is unable to invoke section 58(3), which allows a company to undergo a reduction of capital to re-designate the nominal value of its shares without confirmation by the court, as its net assets as at 31 December 2005 were less than its paid-up share capital, and does not satisfy the condition in section 58(3)(b). The proposed reduction of the nominal value of the shares and the consolidation of every 10 shares into one share of \$0.10 each will enable the shares to trade at above their nominal value and thereby give greater flexibility to enable the Company to raise capital by the issue of new shares. The proposed cancellation of the share premium account and reduction of capital do not involve the diminution of any liability in respect of unpaid share capital or the payment to any shareholder of any paid up capital or of any sum standing to the credit of the share premium account. It does not involve any reduction in the net assets of the Company, except for the costs associated with this application. The accumulated losses can be traced back to the year ended 31 March 1992. In the supporting affirmation of the chief executive officer, he has given a breakdown of the losses for each year down to the six-month period ended 30 June 2006 and accounted for the manner in which the losses arose. He also confirmed in a subsequent affirmation there have been no material changes to the accumulated losses since the date of the latest management accounts made up to 30 November 2006. The auditors have confirmed that the accumulated losses are reflected in the books and accounts of the Company for those years and periods. I agree with the classification of permanent and non-permanent losses by the Company. The total amount of non-permanent losses amounted to \$84,095,000. The Company is willing to give an appropriate undertaking to the court for the protection of its creditors in the event of its making any future recoveries in respect of the non-permanent losses, based on the form of undertaking accepted by the court in *Re Goldbond Group Holdings Ltd.*, HCMP No. 1891 of 2003, Kwan J, 27 June 2003, with some modifications. The full terms of the undertaking are set out in the schedule attached. By the undertaking in *Goldbond*, the amount by which the proposed capital reduction exceeded the accumulated losses was to be paid into a further capital reserve. Under the present undertaking, it is provided in paragraph 2 that the excess of the credit arising from the reduction of capital over the accumulated losses is to be credited to the share premium account. This is in fact the requirement under section 58(3)(e), if a reduction of capital had been carried out without court sanction. Section 58(3) was enacted in 2003. This is a more stringent requirement as compared to the undertaking in

Goldbond and gives more protection to creditors. I have accepted the undertaking. Being a holding company, the Company's creditors are relatively few in number. All three creditors have consented to the petition. At the hearing of the summons for directions on 19 December 2006, an order was made to dispense with the settlement of a list of creditors and directions were given for the advertisement of a notice of the petition. These directions have been complied with. No creditor or shareholder appeared at the hearing of the petition. The shareholders are treated equally in the proposed reduction and the proposal was properly explained in the circular sent before holding the extraordinary general meeting. I am satisfied the proposed capital reduction and cancellation of the share premium account are for discernible purposes. I am also satisfied there would be adequate protection for the interests of creditors. I have made an order in terms of the draft submitted and approved the draft minute. (S Kwan) Judge of the Court of First Instance High Court Mr Godfrey Lam, instructed by Messrs Richards Butler, for the Petitioner Schedule UPON the Company by its Counsel undertaking that after the Capital Reduction and Share Premium Account Reduction take effect:

1. So long as there shall remain outstanding any debt of or claim against the Company which would be admissible to proof in a winding-up of the Company commencing on the day on which the Capital Reduction and Share Premium Account Reduction take effect (the effective date) and the persons entitled to the benefit of such debts or claims shall not have agreed otherwise, in the event of its making any future recoveries in respect of the assets identified in the First Schedule hereto, in respect of which provision for diminution in value was made in the accounts of the Company during the loss-making years as stated in paragraphs 35 to 55 of the Affirmation of Sue Ka Lok herein filed on 12th December 2006, beyond their written down value as stated in the Company's management accounts as at 30th June 2006, all such recoveries beyond that written down value up to an amount of HK\$84,095,000 (the limit), will be credited to a special capital reserve in the accounting records of the Company (Capital Recovery Reserve) and such reserve shall not be treated as realized profits of the Company for the purposes of section 79B of the Companies Ordinance (Cap. 32) and shall be treated as an undistributable reserve of the Company for the purposes of section 79C of the Companies Ordinance (Cap. 32), or any statutory re-enactments or modifications thereof PROVIDED THAT
 - (1) the Company shall be at liberty to apply the Capital Recovery Reserve for the same purposes as a share premium account may be applied;
 - (2) the limit in respect of the Capital Recovery Reserve may be reduced by the amount of any increase, after the effective date, in the paid up share capital or the amount standing to the credit of the share premium account of the Company as the result of the payment up of shares by the receipt of new consideration or the capitalization of distributable profits;

- (3) the limit in respect of the Capital Recovery Reserve may be reduced upon the disposal or other realization, after the effective date, of any of the assets identified in the First Schedule hereto by the amount of the provision made in relation to such asset as at 30th June 2006 (which amount is set out in the First Schedule hereto) less such amount, if any, as is credited to the Capital Recovery Reserve as a result of such disposal or realization; and
 - (4) in the event that the amount standing to the credit of the Capital Recovery Reserve exceeds the limit thereof after any reduction of such limit pursuant to provisos (2) and/or (3) above, the Company shall be at liberty to add the amount of any such excess to the retained profits of the Company and the same shall become available for distribution or to use any such excess to offset the accumulated losses of the Company, as the case may be.
2. The amount of HK\$437,055,345.84, representing the amount by which the total credit arising from the Capital Reduction and the Share Premium Account Reduction exceeds the total accumulated losses of the Company as at 30th June 2006, will be credited to the Share Premium Account of the Company. AND UPON the Company by its Counsel further undertaking that, for so long as the undertakings set out in paragraphs 1 and 2 hereof remain effective, it will:-
- (1) cause or procure its statutory auditors to report by way of a note or otherwise a summary of such undertakings in its audited financial statements or in the accounts of the Company published in any other form; and
 - (2) publish or cause to be published in any prospectus issued by or on behalf of the Company a summary of such undertakings. [The First Schedule to the Undertaking sets out the provision fo 1udk 1udk P Q R S T U V i\$&`G hccw (for Susan Kwan only).dot setup Microsoft Word 9.0 Judiciary Hong Kong Title Microsoft Word Document MSWordDoc Word.Document.8

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