Jurisdiction: The court's jurisdiction over foreign companies in shareholder disputes:

a comparison of Hong Kong and U.K

There has been a most interesting recent HK CFA case concerning a company by the name of Yung Kee Holdings Limited ("YKL")[1] . It was such a run-of-the-mill case on its face which yet gave rise to difficult jurisdictional issues. The CFA's leading judgment was jointly given by Ma CJ and Lord Millett NPJ.

YKL was a company incorporated in the British Virgin Islands, an off-shore jurisdiction much favoured hitherto by owners of businesses based in Hong Kong and the Far East. YKL was a pure holding company at the top of the corporate tree. Its sole asset was the issued share capital of another investment holding company, also incorporated in the BVI for good measure. Beneath that company were the real assets, principally the Yung Kee restaurant business in Wellington Street.

It was a classic shareholders' dispute in a "family company". Regrettably, but as is so common, the younger generation had fallen out between themselves and could not compromise their differences. The petitioners sought relief in the usual way under what used to be the provisions of the Companies Ordinance (Cap 32), section 168A (the unfair prejudice remedy) and in the alternative section 327(3)(c) (winding up on the just and equitable basis). [2]

Hong Kong has followed English statute and precedent in the field of company law relatively closely over the years.[3] The very first English Companies Act was passed in 1862. By section 79 the court was given power to wind up companies incorporated under it on the ground either that they were unable to pay their debts or that it was just and equitable to do so. And by section 199 that power to wind up was extended to a company even if it was incorporated under another statute in another jurisdiction.[4] And nothing much has changed so far as concerns this remedy since 1862, whether in England or all the other jurisdictions round the world which have followed in the English legal tradition, such as Hong Kong, the Cayman Islands and the BVI.

As is trite law, there is a fundamental difference between a winding up sought on the ground of insolvency and one sought on the just and equitable ground. A winding up on the ground of insolvency is generally available only to creditors, because shareholders will generally have no tangible interest in the outcome of an insolvent liquidation, whereas a winding up on the just and equitable ground is generally available only to shareholders and generally it must be shown that the company is solvent. And the leading case on the principles underlying the grant of a winding up order to a shareholder on the just and equitable ground is, of course, *Re Westbourne Galleries* [1973] AC 360. As that case and subsequent cases show, the just and equitable remedy is essentially a weapon in the court's armoury where the majority are unfairly oppressing the minority by breaking the terms of the joint venture. The classic case of such oppression is the exclusion of a minority shareholder in a quasi-partnership from participation in the management of the business.

[1] [2015] HKEC 2370, allowing appeal against [2014] 2 HKLRD 313 (HKCA)

[2] There has been a substantial restructuring of company legislation in Hong Kong with effect from March 2014, but it is believed not as to affect the law for present purposes.

[3] Their paths have diverged since 1986 in the field of insolvency, both corporate and individual.

[4] Provided it had at least 7 members

But the winding up remedy is obviously a blunt instrument, a death sentence on the company so to speak. What was needed was a more flexible remedy, in particular the ability to order one side in a shareholders' dispute to buy out the other. So what has changed considerably since 1862 is that, with varying speeds, all the jurisdictions following in the English legal tradition have introduced into their company statutes a remedy whereby, upon certain grounds being established (essentially although not exclusively[5] the same as the grounds for winding up on the just and equitable basis), the court has the power to order the oppressor majority to buy out the oppressed minority, or other remedies, instead of passing the death sentence of a winding up order.

The question then arises: when should a court entertain a claim by an oppressed minority shareholder for winding up, as opposed to a claim for the more flexible remedy? As will be seen, this became eventually an important issue in the Yung Kee case. The mere fact that a petition claims winding up has the tactical advantage of putting pressure on the respondents, since a winding up petition always entails the risk that dispositions of the company's assets after the petition will be rendered void in the event of the making of a winding up order, even if this risk will usually be only theoretical in the case of a shareholders' petition. A petitioner seeking winding up in the alternative, if challenged at the outset, bears the burden of persuading the court that his choice of the death sentence remedy of winding up over the more flexible remedy is a tenable one.[6] The remedy of winding-up is one of last resort, and an exceptional remedy in the context of disputes between shareholders: *Fulham Football Club (1987) v Richards [2012] Ch. 333* at [54]–[56].

In England, the oppression remedy is now to be found in section 994 of the Companies Act 2006, which traces its ancestry back to the original and narrower oppression remedy in section 210 of the Companies Act 1948. But it only applies to companies incorporated under UK company law.[7]

Hong Kong also has a statutory oppression remedy, now Part 14 of the Companies Ordinance. Unlike the UK Companies Act, however, by section 722(1) of the Companies Ordinance, Part 14 applies not only to companies incorporated under Hong Kong company law but also to any "non-Hong-Kong company", i.e. any company which has established a place of business in Hong Kong.

To return to the dispute between the owners of the Yung Kee restaurant business, the petitioners sought relief by way of winding up on the just and equitable ground in the alternative to a share purchase order on the unfair prejudice ground. No application appears to have been made at the outset to strike out the claim for winding up. Presumably the view was taken that it would not be clear prior to trial whether or not the claim for winding up was hopeless.

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[5] See e.g. *Re Neath Rugby* [2009] 2 BCLC 427, CA.

[6] The following are cases where the petitioner has failed to discharge this burden and the claim for winding-up has been struck out: *Re Company (No.003028 of 1987) (1987) 3 B.C.C. 575* Ch D (Comp); *Re Company (No.004415 of 1996) [1997] 1 B.C.L.C. 479* Ch D; *Re Wong To Yick Wood Lock Ointment Ltd [2001] 2 H.K.C. 618 (CFI); [2003] 1 H.K.C. 484 (CA)*; *Re Health & Care Group Ltd unreported 16 May 2012, HCCW 404/2011, Hong Kong CFI*; *Sun Light Elastic Ltd (CFI) [2013] 5 HKLRD 1*; *China People (Hong Kong) Ltd [2014] 2 HKLRD 808*. But there also many cases where the petitioner has discharged this burden, e.g. *Re Company (No.001363 of 1988) (1989) 5 B.C.C. 18* and *Re Copeland & Craddock [1997] B.C.C. 294*. It is by no means always clear prior to trial whether the claim for winding up is hopeless.

[7] And even in the case of UK companies, the court may very exceptionally decline jurisdiction on the usual *forum non conveniens* ground: see e.g. *Re Harrods (Buenos Aires) Ltd.* [1992] Ch. 72, CA. See also *Konamaneni v. Rolls Royce Industrial Power (India) Ltd.* [2002] 1 WLR 1269.

The trial took place before Harris J, whose judgment may be found at http://legalref.judiciary.hk/lrs/common/ju/ju_frame.jsp?DIS=84102 . Unusually, the court was not pressed to determine as a preliminary issue whether it ought to be entertaining the petition given that the company was not incorporated in Hong Kong, given the Judge's indication that the jurisdiction challenge made by the respondents should be adjourned to the trial: see para. 10 of his judgment following the trial. Instead, the learned trial judge was evidently persuaded to make findings of fact as if the court did have jurisdiction, whilst also determining the issue of jurisdiction. He held that he had no jurisdiction, on the basis that, for the purposes of the unfair prejudice remedy, the company did not have a place of business in Hong Kong, and that, for the purposes of the winding up remedy, the claim could and should be litigated in the BVI. But he went on to find, in case he was wrong on jurisdiction, that there had been unfairly prejudicial conduct by the majority.[8]

The petitioners appealed. It is noteworthy that the petitioners, no doubt making the tactical calculation that their best shot at establishing jurisdiction lay in the winding up remedy, shifted their position and now said that the winding up remedy was the relief that they primarily claimed. The Court of Appeal dismissed the appeal.[9]

The petitioners appealed to the CFA. The CFA agreed that the appeal failed insofar as concerned the availability of the unfair prejudice remedy, because it could not be shown that the company had established a place of business in Hong Kong. However, it allowed the appeal insofar as it concerned the availability of the winding up remedy on the just and equitable basis, and it is in this respect that the case is of considerable interest. It held that the following principles applied in determining whether the HK court should accept jurisdiction in the case of such a remedy:

- Whilst the jurisdiction was "abnormal", this meant no more than it must be shown that there was "good reason" for exercising it: ¶19
- The test of whether there was "good reason" in a shareholders' claim for winding up on the just and equitable basis was the same as in a creditor's claim for winding up on the insolvency ground, namely whether there was a sufficient connection between the company and the jurisdiction: ¶24
- Applying that test on the facts would be very different, depending upon whether it is a creditor's claim based on insolvency or a shareholder's claim based on the just and equitable ground. In the former case, the prospect of the petitioner deriving a benefit from a winding up order will always be necessary and often be sufficient (¶24). In the latter case, the presence of shareholders within the jurisdiction will be an extremely weighty factor (¶27).

Applying the above test, the CFA held that the HK courts should assume jurisdiction to wind up the parent company and held that such an order should be made on the facts. That did not mean, of course, that the restaurant business in HK would close – on the contrary, it meant that it would have to be sold if, and only if, the shareholders could not agree terms for one side to buy out the other.

There is reason, however, to believe that this decision may come to be seen as a product of its own procedural eccentricities and may not be followed in other jurisdictions.

[8] The Court of Appeal reversed him on the issue of liability but the CFA restored his findings.
[9] [2014] HKLRD 313

First and foremost, as has already been noted, it is well established that the remedy of winding-up is one of last resort, and an exceptional remedy in the context of disputes between shareholders. It is prima facie surprising that the petitioners failed in their case that the HK courts had jurisdiction to grant the unfair prejudice remedy and yet the HK courts were prepared nevertheless to grant the winding up remedy. This incongruity appears to have caused the CFA no concern, given the course that the case had taken in the HK courts: ¶61. The CFA was naturally appalled at the prospect of the parties, having gone through a full trial on the merits and exhausted the appeal process in HK, having to relitigate what was essentially a mundane Hong Kong family dispute in the BVI.

Secondly, it is conceivable that another jurisdiction might take the view that the test for the acceptance of jurisdiction should be more stringent in the case of shareholders' just and equitable winding up petitions than in creditors' insolvency petitions. In the latter case there is nothing unusual in multiple jurisdictions accepting jurisdiction and for co-operation between them. In contrast, it is arguable that, in the case of shareholders' petitions, greater weight should be accorded to the natural forum for the resolution of the dispute, namely the courts of the country of incorporation of the company, since (i) it is that country's laws which will usually govern the rights of the shareholders and (ii) the choice of that jurisdiction by the shareholders may be compared to a choice by the shareholders of that jurisdiction for the resolution of their disputes, and the burden should shift to the petitioners to show why the courts of that country were not a convenient forum. Compare *Konamaneni v. Rolls Royce Industrial Power (India) Ltd.* [2002] 1 WLR 1269 at [66 and 128].[10] That was a case concerned with the issue as to which jurisdiction was the appropriate forum for determining whether a derivative claim may be brought, which is analogous to the issue with which the Yung Kee case was concerned, namely which was the appropriate jurisdiction for determining a claim for winding up on the just and equitable basis.

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[10] Followed in Hong Kong: *Waddington Ltd v Chan Chun Hoo Thomas [2009] 2 B.C.L.C. 82* CA; *Mehta v Mehta H.C.A. 411/2006*; *East Asia Satellite Television (Holdings) Ltd v New Cotai LLC [2011] 3 HKLRD 734*; *Wong Ming Bun v Wang Ming Fan [2014] 1 HKLRD 1108*.