

Client Alert

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Jurisdiction of the Hong Kong Courts re Winding Up and Unfair Prejudice Petitions — Are Offshore Companies Safe?

Hong Kong law contains a number of provisions designed to protect the interests of minority shareholders, including the “unfair prejudice” remedies under section 168A of the Companies Ordinance (the Ordinance) and the Ordinance’s “just and equitable” winding-up provisions. These protections can, in some cases, also be invoked by shareholders of *non-Hong Kong* companies.

However, as the Hong Kong Court’s recent judgment in *Re Yung Kee Holdings Limited*¹ demonstrates, a minority shareholder of a non-Hong Kong company would be wise to proceed cautiously before seeking to avail itself of these provisions.

This *Client Alert* analyses the circumstances in which the Hong Kong Court might allow minority shareholders of non-Hong Kong companies to make use of these protections, following the *Re Yung Kee* Judgment.

Background

The Yung Kee restaurant is a well-known icon in Hong Kong, visited by many locals on a regular basis, and seen as an enticing pit stop for tourists, who come to savour its famous roasted goose. As are many businesses in Hong Kong it is family owned, having been established by a Mr. Kam in the early 1930s. Over the years the business (the restaurant, associated businesses and property) became very valuable. Upon his death in 2004, ownership of the business was divided amongst Mr. Kam’s family members.

Unfortunately, disputes arose. Ultimately one of the family members (the minority shareholder, Kam Kwan Sing) (the Petitioner) determined to use the Hong Kong law provisions referred to above and petitioned to wind up the ultimate holding company (Yung Kee) in Hong Kong, unless his brother (the majority shareholder) bought his 45 percent stake or sold him his 55 percent share. The Petitioner’s primary claim was that the affairs of Yung Kee (which was incorporated in BVI) had been conducted in a manner unfairly prejudicial to him as a member.

On 31 October 2012, the Hong Kong Court dismissed the petition holding that it had no jurisdiction to make a buy-out/sell-out order in favour of the Petitioner, because Yung Kee had not established a place of business in Hong Kong; nor did it have jurisdiction to wind up Yung Kee, since Yung Kee did not have a sufficient connection with Hong Kong. The basis for these decisions is outlined on the following page.

“A minority shareholder of a non-Hong Kong company would be wise to proceed cautiously before seeking to avail itself of the ‘unfair prejudice’ remedies and the ‘just and equitable’ winding-up provisions under the Companies Ordinance.”

Unfair Prejudice and Buy-out/Sell-out Order: Place of Business in Hong Kong

Section 168A applies to "specified corporations". This is defined to include a "non-Hong Kong company", which is a company "incorporated outside Hong Kong which ... has established a place of business in Hong Kong". Before a petitioner might invoke section 168A in respect of a company incorporated outside Hong Kong it must therefore demonstrate that the company in question (in this case, Yung Kee) had established a place of business in Hong Kong.

Following *Re Yung Kee*, non-Hong Kong companies will not be considered to have established a place of business in Hong Kong "unless they have business activities of some substance, which have to be undertaken sufficiently regularly to justify establishing a base in Hong Kong". In this regard, the Judge gave the following examples:

Example of a place of business being established	Example of a place of business not being established
Foreign holding companies, which carry out significant activities here (and perhaps listed on the Stock Exchange of Hong Kong Limited) and are registered under Part XI of the Companies Ordinance	Companies which from time to time have staff visiting Hong Kong for short periods and working out of the same hotel or the same business center

In arguing that Yung Kee had established a place of business in Hong Kong the Petitioner submitted that since April 2009 (i) executive decisions of Yung Kee were made; (ii) the Group's books and records were kept; (iii) Yung Kee's correspondence address was; and (iv) dividends of the Group had been declared and paid, in Hong Kong.

Whilst accepting that Yung Kee conducted certain of its internal affairs in Hong Kong, the Court indicated that "*the fact that the directors of a company meet from time to time at a particular location and deliberate upon its affairs does not of itself turn that location into a place at which a company has established a place of business*".

In concluding that that Yung Kee had not established a place of business in Hong Kong, the Court took the following factors into account:

- It was an offshore investment holding company.
- Its sole asset was shares in another BVI company and it did not have a bank account in Hong Kong.
- It did not trade or run any business in Hong Kong, nor did it play any role or function in the business or operations of the Group.
- It had no creditors, employees or income other than dividends from a subsidiary.
- It had no accounts and its activities (which were directed to changing the membership of the board and the payment of dividends) did not necessitate establishing a place of business in Hong Kong.
- It had not entered into any agreement which allowed it to occupy any part of the Yung Kee Building, nor had it had any dealings or legal arrangements with any third parties in Hong Kong.
- It was not registered under Part XI of the Companies Ordinance, and none of its directors, shareholders or professional advisers had ever advanced a view or advised that Yung Kee should be registered under Part XI of the Companies Ordinance.

Just and Equitable Winding-up: Sufficient Connection

As an alternative to the buy-out order, the Petitioner sought to wind up Yung Kee on the “just and equitable” ground under section 327(3)(c) of the Ordinance. In order for the Court to exercise its jurisdiction in this regard, it had to be satisfied, *inter alia*, that Yung Kee had a “sufficient connection” with Hong Kong.

The Court determined that what constitutes “sufficient connection” will probably differ in the case of a petition presented on the just and equitable ground (as here) than where a petition is presented on grounds of insolvency. In particular, the presence of assets may not be as significant in the former case. The Court indicated that, whilst there may well be cases where the connection is sufficiently strong for the Hong Kong court to accept jurisdiction, those instances will be rare. The Court determined that in the case of a shareholders’ dispute, the relevant factors to take into account are likely to include (a) the location at which the company primarily carries on its business, (b) the shareholders’ connection (if any) with Hong Kong and (c) where the matters giving rise to the dispute occurred.

The Court indicated, by way of example, that the connection might be considered sufficiently strong for it to accept jurisdiction where the foreign company was registered as an overseas company under Part XI of the Ordinance and carried on business in Hong Kong, some or all of its directors and shareholders were resident in Hong Kong, and the principal complaint concerned the exclusion from management of the company’s business in Hong Kong of a Hong Kong resident shareholder.

In this case, where Yung Kee did not directly own the Hong Kong operating subsidiaries or have a place of business in Hong Kong, the Court held that there was insufficient connection with Hong Kong for the Court to assume jurisdiction to wind up Yung Kee under section 327.

Other Matters in Issue

As a result of the above determinations, the Petition was dismissed. Nevertheless, the Court chose to provide its views on a substantial number of other issues that would have fallen to be determined had the Court reached a different view on jurisdiction. For example, the Court clarified various issues regarding the circumstances in which a “quasi-partnership” may arise and explained the circumstances under which equitable constraints on the behavior of other members of a company will apply. Please contact one of the authors for further details in this regard.

Endnote

¹ HCCW 154/2010, unreported, 31 October 2012

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