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Roast Goose, Family Disputes and Offshore Companies Lessons from the Yung Kee Saga

Seminar for Hong Kong Institute of Certified Public Accountants

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Topics covered

1. Introduction
2. The “unfair prejudice” remedy under the CO
3. Hong Kong courts’ jurisdiction to grant unfair prejudice remedy regarding foreign companies
4. The “place of business” test
5. The “just and equitable” ground of winding up
6. Conditions for exercising jurisdiction to wind up an unregistered company
7. What constitutes “sufficient connection” for exercising winding up jurisdiction
8. Equitable considerations for family business
9. Valuation issues
10. Action to pre-empt petition

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Yung Kee Saga

- The business of Yung Kee was founded by the late Kam Shui Fai ("**Kam Senior**").
- The business started as a cooked stall in Sheung Wan in the 1930s.
- In the 1970s, the business developed a corporate structure.

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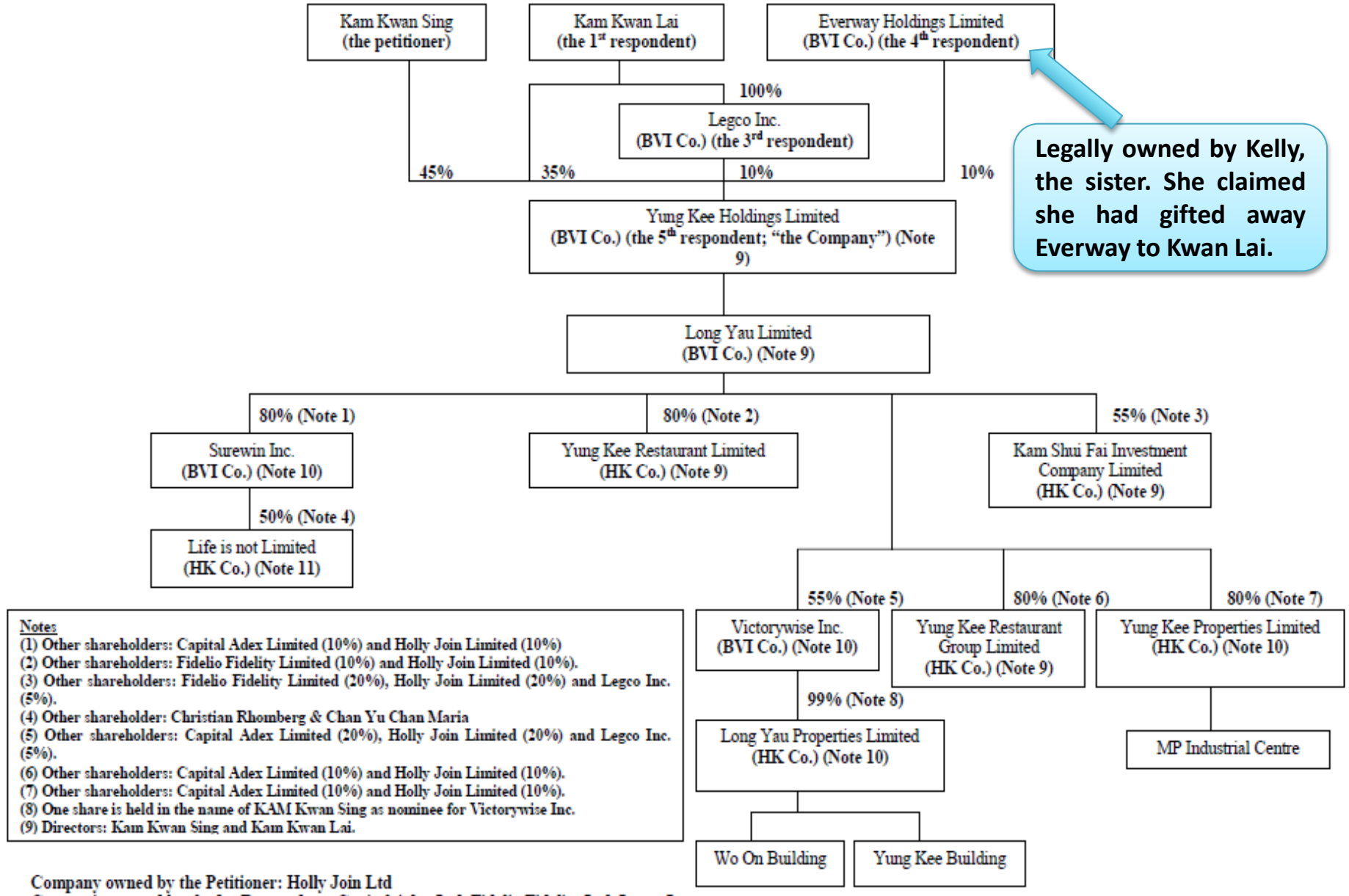
Yung Kee corporate structure

Annex



Legally owned by Kelly, the sister. She claimed she had gifted away Everway to Kwan Lai.

Notes
(1) Other shareholders: Capital Adex Limited (10%) and Holly Join Limited (10%)
(2) Other shareholders: Fidelio Fidelity Limited (10%) and Holly Join Limited (10%).
(3) Other shareholders: Fidelio Fidelity Limited (20%), Holly Join Limited (20%) and Legco Inc. (5%).
(4) Other shareholder: Christian Rhomberg & Chan Yu Chan Maria
(5) Other shareholders: Capital Adex Limited (20%), Holly Join Limited (20%) and Legco Inc. (5%).
(6) Other shareholders: Capital Adex Limited (10%) and Holly Join Limited (10%).
(7) Other shareholders: Capital Adex Limited (10%) and Holly Join Limited (10%).
(8) One share is held in the name of KAM Kwan Sing as nominee for Victorywise Inc.
(9) Directors: Kam Kwan Sing and Kam Kwan Lai.

Company owned by the Petitioner: Holly Join Ltd
Companies owned by the 1st Respondent: Capital Adex Ltd. Fidelio Fidelity Ltd, Legco Inc

Yung Kee Saga

Background:

1. The subject company, Yung Kee Holdings Limited (the "**Company**"), was incorporated in the BVI. It is a holding company of another BVI company, Long Yau Ltd, which in turn operates two Hong Kong subsidiaries.
2. The assets of Yung Kee now comprise the Yung Kee restaurant, a club and various properties in Hong Kong, including the Yung Kee building.
3. After the death of Kam Senior in December 2004, the two brothers, Kam Kwan Lai and Kam Kwan Sing became shareholders of the Company, each holding directly or indirectly 45% of the shares, with the remaining 10% being held by their sister.
4. Initially, the two brothers worked well together. But as years passed, they ultimately fell out.

Yung Kee Saga

5. Kwan Sing (now deceased) (the "**Petitioner**") brought proceedings in the Hong Kong court seeking an order that Kwan Lai buy him out on the ground that the affairs of the Company were being carried on in a manner that was unfairly prejudicial to him pursuant to s.168A of the Old Companies Ordinance (now s.724 of Cap 622).
6. In the alternative, the Petitioner sought an order that the Company be wound up on the just and equitable ground under s.327(3)(c) of the Ordinance.

The unfair prejudice remedy

- Section 168A of Old Companies Ordinance (Cap 32), now in s.724 of the Companies Ordinance (Cap 622)

- Under s.168A/724, the aggrieved shareholders can petition the court for reliefs if the affairs of the company are being or have been conducted in a manner *unfairly prejudicial* to the interests of the shareholders generally or one or more shareholders, including the petitioner.

- The conduct complained of by the petitioner must be both “unfair” and “prejudicial”. It is not sufficient if the conduct satisfies only one of those tests.

The just and equitable ground of winding-up

- S.177(1)(f): A Hong Kong company may be wound up by the court if the court is of opinion that it is just and equitable that the company should be wound up.

- The words “just and equitable” carry a wide meaning. It is ultimately a question of fact and each case depends on its own facts.

The just and equitable ground of winding-up

- Section 177(1)(f) applies to Hong Kong companies only.
- But there is a similar provision, namely s.327(3)(c), which applies to overseas companies.
- S.327(3)(c): The court has a discretionary power to wind up an unregistered company if the court regards it is as just and equitable to do so.
- “Unregistered company” usually refers to foreign companies and is declared to include registered non-Hong Kong companies.

The just and equitable ground of winding-up

- Winding up on just and equitable ground can broadly be categorized into the following heads:

  (1) loss of trust and confidence in quasi-partnership cases;
  (2) deadlock in the management of the company's affairs;
  (3) loss of substratum of company;
  (4) oppression on the minority shareholders by the majority shareholders company formed to carry out fraud or illegal purposes;
  (5) justice or equity;
  (6) failure to comply with directions of regulatory authority; and
  (7) where the conduct of the management calls for the fullest investigation, for example where the persons in control of the company are guilty of fraud.

Main Complaints of the Petitioner (Kwan Sing)

Changing the fundamental basis upon which the Group had been managed

(1) Taking control of the board of the Company by purportedly causing Carrel, son of Kwan Lai, to be appointed a director.

(2) Causing Carrel to be appointed a director of Long Yau and YKR Group.

(3) Causing the Company to resolve that Kwan Lai act on behalf of the Company in its capacity as registered shareholder of Long Yau.

Misapplication of Group Assets

(4) Allowing Carrel and Yvonne, daughter of Kwan Lai, to use the premises in Chai Wan for their own personal business without the Petitioner's knowledge and consent.

Excessive Remuneration to Carrel and Yvonne

(5) Carrel and Yvonne, who worked only part time in the Company, have been paid monthly remuneration of $45,000.

Exclusion from management

(6) Usurping the Petitioner's control over promotion, appointment and termination of staff working in the Restaurant.

Yung Kee Saga

Court of First Instance:

- Harris J held that the court did not have jurisdiction to make an order under s.168A.
- Moreover, the Company's connection with Hong Kong was not sufficiently strong to justify the exercises of its jurisdiction to make a winding-up order under s 327(3)(c).
- Nevertheless, on the substantive merits of the petition, Harris J found that the affairs of the Company had been carried on in a manner that was unfairly prejudicial to the deceased.
  - There had been a common understanding between Kwan Sing and Kwan Lai that they would have equal say in Yung Kee's affairs.
  - Thus, when Kwan Lai took steps to control Yung Kee, it was inconsistent with the way in which Kwan Sing and Kwan Lai had previously conducted the business and lack of regard for Kwan Sing's reasonable expectation.

Yung Kee Saga

Court of Appeal:

- Affirmed the rulings of Harris J in relation to court's jurisdiction under both s 168A and s327(3)(c).
- Reversed the judge's finding on the existence of unfair prejudice.
  - There was insufficient evidence to suggest that there was a mutual understanding.
  - Harris J's approach in determining the fairness of the conduct of Kwan Lai by reference to the legitimate expectation of Kwan Sing was wrong. The correct approach is to examine whether Kwan Sing can pray in aid of any equity to restrain the exercise of Kwan Lai's majority voting power. If such equity could not be identified, it matters not that Kwan Sing's expectation was upset and the trust and confidence between the brothers were destroyed.

The case finally came before the Court of Final Appeal.

Section 168A / 724: unfair prejudice

- "Aggrieved member of a specified corporation can petition the court that the affairs of the specified corporation are being or have been conducted in a manner *unfairly prejudicial* to the interests of the members generally or one or more shareholders, including the petitioner."

- "Specified corporation" is defined in s.2(1) to mean "a company" or "a non-Hong Kong company".

- Now in s.724 of the Companies Ordinance (Cap 622).
  - "~~specified corporation~~" → "company"
  - s.722: company includes a "non-Hong Kong company"

Section 168A / 724: foreign company

- Therefore, whether a foreign company can claim relief for unfair prejudice depends on whether the company is a “non-Hong Kong company”.

- A “non-Hong Kong company” is defined in s.332 as a company “**incorporated outside Hong Kong which … has established a place of business in Hong Kong**”.

- There is no statutory definition of “place of business”, but it is declared to include a share transfer or share registration office.

- What does case law say?

“Establishing a place of business”

CFI (Harris J):

- Business is not confined to commercial transactions or transactions which create legal obligations.
- But it does not cover purely internal activities and administrative activities, such as changes to the composition of the board or payment of dividends.
- The word “establish” indicates that some degree of permanence as being a location of the company’s business is required.
- Merely having a place where the company carries on business in Hong Kong is insufficient as many instances could be envisioned of companies which have staff visiting Hong Kong frequently on business trips working out of the same hotel or business center.

“Establishing a place of business”

A variety of factors were cited to support the court’s view that Yung Kee had not established a place of business in Hong Kong:

(1) The Company did not have an office or leased premises in Hong Kong.

(2) The company did not have a bank account in Hong Kong.

(3) The company had no financial dealings or records, liabilities, creditors or employees and no income apart from dividends from Long Yau Limited.

(4) The Company is a mere “passive investor in another BVI company”.

(5) The two-tiered system of ownership by Yung Kee was a corporate structure effectively distancing Yung Kee from Hong Kong. It is therefore inferred that the Company did not intend to establish a place of business in Hong Kong.

(6) Its board functions were limited to changing the membership of the board and payment of dividends.

(7) It did not trade or run business in Hong Kong

- Therefore, there is no jurisdiction for the court to make a buy-out order under s.168A.
- Harris J's rulings were affirmed by CA and CFA.

Section 327(3)(c): just and equitable winding-up for “unregistered companies”

- Section 177(1)(f) applies to Hong Kong companies only.
- But there is a similar provision, namely s.327(3)(c), which applies to overseas companies.

- S.327(3)(c): The court has a discretionary power to wind up an unregistered company if the court regards it is as just and equitable to do so.
- “Unregistered company” usually refers to foreign companies and is declared to include registered non-Hong Kong companies.

Three core requirements

- Strong presumption: The most appropriate jurisdiction in which to wind up a company would be its place of incorporation. (*Re Gottinghen Trading Ltd* [2012] 3 HKLRD 453)

- Therefore, in the context of the winding-up of an unregistered company, the court should not exercise its jurisdiction unless the following three core requirements have been satisfied (*Re Real Estate Development Co* [1991] BCLC 210):-

  (1) there is a sufficient connection with Hong Kong;

  (2) there is a reasonable possibility that the winding up order would benefit those applying for it; and

  (3) there are persons who had a sufficient economic interest in the winding up and would be subject to the court's jurisdiction, other than by virtue of being the petitioner.

1st core requirement: sufficient connection

- Whether there is sufficient connection depends on both the nature of the individual matters relied on and also the significance of the company's Hong Kong connection to its activities viewed *as a whole*.
- In other words, the Court will ask how Hong Kong fits into the overall scheme of the company's activities viewed in their entirety.
- In the context of insolvency, the requirement of "sufficient connection" can usually be satisfied by the presence of assets within the jurisdiction.

A more stringent requirement in the context of shareholder disputes?

***Re Gottinghen Trading Ltd* [2012] 3 HKLRD 453:**

1. C1 was incorporated in the BVI and C2, in Samoa. Both are unregistered companies.
2. Due to shareholders' disputes, winding up petitions had been presented under s.327(3)(c).
3. The two companies were owned by the petitioner and the 1st respondent. Each held 50% of each company respectively.
4. Neither the petitioner nor the 1st respondent were resident in Hong Kong.
5. C1's business was based in Shanghai and had no connection with Hong Kong. C2 was used solely to apply for shares in two initial offerings and did not carry on a business.
6. Other than two Hong Kong bank accounts, the two companies did not have assets in Hong Kong.

Re Gottinghen Trading Ltd [2012] 3 HKLRD 453

Court's findings:-

1. There was insufficient connection with Hong Kong, despite the two Hong Kong bank accounts.

2. In today's world of global interconnectivity, liquid assets can easily be moved from one place to another through electronic means such as e-banking, and it was merely for convenience that the bank accounts were in Hong Kong. They did not demonstrate a sufficient connection.

3. Different thresholds apply when establishing sufficient connection on the "just and equitable" ground, which usually occurs in a scenario of shareholders' dispute.

Re Gottinghen Trading Ltd [2012] 3 HKLRD 453

- The purpose behind winding up insolvent companies is to pay creditor for a debt due from the company. Therefore, whether or not assets exist in Hong Kong is important.

- In just and equitable winding up cases, however, the courts are to determine disputes between parties over the conduct of the company. In such cases, considerations will be different. While the presence of assets will still be a relevant consideration, it is probably not as significant as in the case of a creditor's petition.

- The more pertinent factors would include whether the company carries on business in Hong Kong, if Hong Kong was the place where matters giving rise to the dispute occurred and whether the shareholders had a connection with Hong Kong.

CA explained why a more stringent threshold is required in the context of shareholder disputes

***Re Yung Kee Holdings Ltd* [2014] 2 HKLRD 313**

- First, creditors are not personally attached to the state of incorporation of a foreign company and they might suffer prejudice if their fate were subject exclusively to the law and process of the state of incorporation.

- Second, there is much less justification for a shareholder to seek to circumvent that law of the state of incorporation, which was the law of their choice, and resort to another jurisdiction to wind up the company.

Yung Kee case: CFA disagreed

- Shareholders, no less than creditors, are entitled to bring winding up proceedings in Hong Kong in respect of a foreign company.

- But the factors which are relevant to establish the sufficient connection are different in the two cases, due to the different nature of the dispute and the purpose for which the winding up order is sought.

Different considerations

- Creditors seek a winding up order against their debtor in order to obtain payment in or towards satisfaction of their debts. Therefore, the presence of significant assets in Hong Kong which may be available to the liquidator for distribution among the creditors will usually suffice.

- In a shareholder's petition, the dispute is between the shareholders. The company is the subject of the dispute rather than a party to it. Accordingly, the presence of the other shareholders within the jurisdiction is an extremely weighty factor in establishing the sufficiency of the connection between the company and Hong Kong.

CFA: Sufficient Connection

CFA's findings:-

1. The value of a parent company resides in the value of its subsidiaries' assets.
2. Any depletion of a subsidiary's assets causes indirect but real loss to the parent company and its shareholders.
3. The shareholder who applies to wind up a company does so in order to realize his investment in the company.
4. If the company is a holding company, then the shareholder does so in order to realize the value of the company's underlying assets.
5. There is no doctrinal reason to exclude a connection through subsidiaries.
6. The court should give effect to the close connection between a holding company and the assets of its direct and indirectly held subsidiaries.

CFA: Sufficient Connection

There were compelling factors in the Yung Kee Restaurant case which established sufficient connection with Hong Kong:

(1) The Company itself is merely a holding company of a group of directly and indirectly held subsidiaries and carries on no business of any kind whether in the BVI or Hong Kong.

(2) All the underlying assets of the Company, that is to say the assets of its wholly owned subsidiary Long Yau, are situate in Hong Kong.

(3) The business of the group is wholly carried on by the Company's indirectly held Hong Kong subsidiaries, all of which are incorporated in Hong Kong and carry on business exclusively in Hong Kong.

(4) The whole of the Company's income is derived from businesses carried on in Hong Kong.

(5) All the Company's shareholders and directors are and always have been resident in Hong Kong and none of them has ever set foot in the BVI where the Company is incorporated.

(6) All the directors of its directly and indirectly held subsidiaries are and always have been residents in Hong Kong and none of them has ever set foot in the BVI.

(7) All board meetings of the Company and its subsidiaries are held in Hong Kong and all administrative matters relating to the Company are discussed and decided in Hong Kong.

(8) Crucially the dispute is a family dispute between parties all of whom are and always have been resident in Hong Kong and the events giving rise to it and the conduct of which complaints is made all took place in Hong Kong.

The 2nd and 3rd core requirements

- 2nd core requirement: There is a reasonable possibility that the winding up order would benefit those applying for it.

- 3rd core requirement: There are persons who had a sufficient economic interest in the winding up and would be subject to the court's jurisdiction, other than by virtue of being the petitioner.

- The 2nd and 3rd core requirements are usually much easier to satisfy.

Locus vs. Need

Re G Ltd [2016] 1 HKLRD 167

- The subject Company was incorporated in the Cayman Islands and listed on the main board of the Hong Kong Stock Exchange.
- The Petitioner issued a winding up petition against the Company on the grounds of insolvency and in parallel applied to appoint provisional liquidators.
- At the hearing, it turned out that the Company had already issued a petition for its own winding up in the Cayman Islands as well as the appointment of provisional liquidators.
- Harris J adjourned the hearing pending the determination of the Cayman Islands Court. Winding-up order was subsequently granted and provisional liquidators appointed in Cayman Islands.
- The Petitioner argued that it had the requisite *locus* to present the petition against the Company in Hong Kong.

Re G Ltd [2016] 1 HKLRD 167

Harris J:-

- Hong Kong court has discretionary jurisdiction to wind up a foreign company: s.327 of the Old Companies Ordinance (Cap 32)
- Foreign companies, in the sense of having locus, are entitled to present the petition and apply for provisional liquidators.
- However, strong presumption → the appropriate jurisdiction to petition for a winding-up order is that of the company's place of incorporation.
- At common law the court has the power to recognize foreign liquidators and to assist them in carrying out their function: *Joint Official Liquidators of A Co v B* [2014] 4 HKLRD 374
- Therefore, in conventional cases, a foreign company is expected to be wound up in its place of incorporation and for its liquidators to consider whether or not it is necessary to seek recognition and potentially assistance from the court in Hong Kong.

Ruling:-

- Application to wind up the company and appointment of provisional liquidators dismissed.

Family Business

- *“All happy families resemble one another, each unhappy family is unhappy in its own way.”*

  \- *Leo Tolstoy*

- It is estimated that Hong Kong has half a million Chinese family companies.
- A family business is usually founded upon personal relationships between family members.
- It is not uncommon that there exists some kind of mutual understandings or informal agreements between the family members.

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Equitable considerations

- *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360 at p.379, per Lord Wilberforce:

- *"The words [just and equitable] are a recognition of the fact that a limited company is more than a mere legal entity, with a personality in law of its own: that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se which are not necessarily submerged in the company structure...The 'just and equitable' provision does not … entitle one party to disregard the obligation he assumes by entering a company, nor the court to dispense him for it. It does, however, enable the court to subject the exercise of legal rights to equitable considerations; considerations, that are, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights, or to exercise them in a particular way."*

Equitable considerations

- *O'Neill v Phillips* [1999] 1 WLR 1092, at p.1098, per Lord Hoffmann:

- *In an unfair prejudice petition, the background has the following two features. First, a company is an association of persons for an economic purpose, usually entered into with legal advice and some degree of formality. The terms of the association are contained in the articles of association and sometimes in collateral agreements between the shareholders…Secondly, company law has developed seamlessly from the law of partnership, which was treated by equity, like the Roman societas, as a contract of good faith, which was to restrain the exercise of strict legal rights in certain relationships in which it considered that this would be contrary to good faith.*

Equitable considerations

- *O'Neill v Phillips* [1999] 1 WLR 1092, at p.1099 , per Lord Hoffmann:
- The concept of "unfairness" is similar to the "just and equitable" ground for winding up. The notion of fairness must be understood in the context.

- *O'Neill v Phillips* [1992] 1 WLR 1092, at pp.1098-1099, per Lord Hoffmann:
- *"Although fairness is a notion which can be applied to all kinds of activities, its content will depend upon the context in which it is being used. Conduct which is perfectly fair between competing businessmen may not be fair between members of a family. In some sports it may require, at best, observance of the rules, in others it may be unfair in some circumstances to take advantage of them. All is said to be fair in love and war. So the context and background are very important."*

Equitable considerations

- *“The first of these two features leads to the conclusion that a member of a company will not ordinarily be entitled to complain of unfairness unless there has been some breach of the terms on which he agreed that the affairs of the company should be conducted. But the second leads to the conclusion that there will be cases in which equitable considerations make it unfair for those conducting the affairs of the company to rely upon their strict legal powers. Thus unfairness may consist in a breach of the rules or in using the rules in a manner which equity would regard as contrary to good faith.”*

Equitable considerations

- In *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360 , Lord Wilberforce identified three characteristics as commonly giving rise to equitable constraints upon the exercise of powers under the articles:

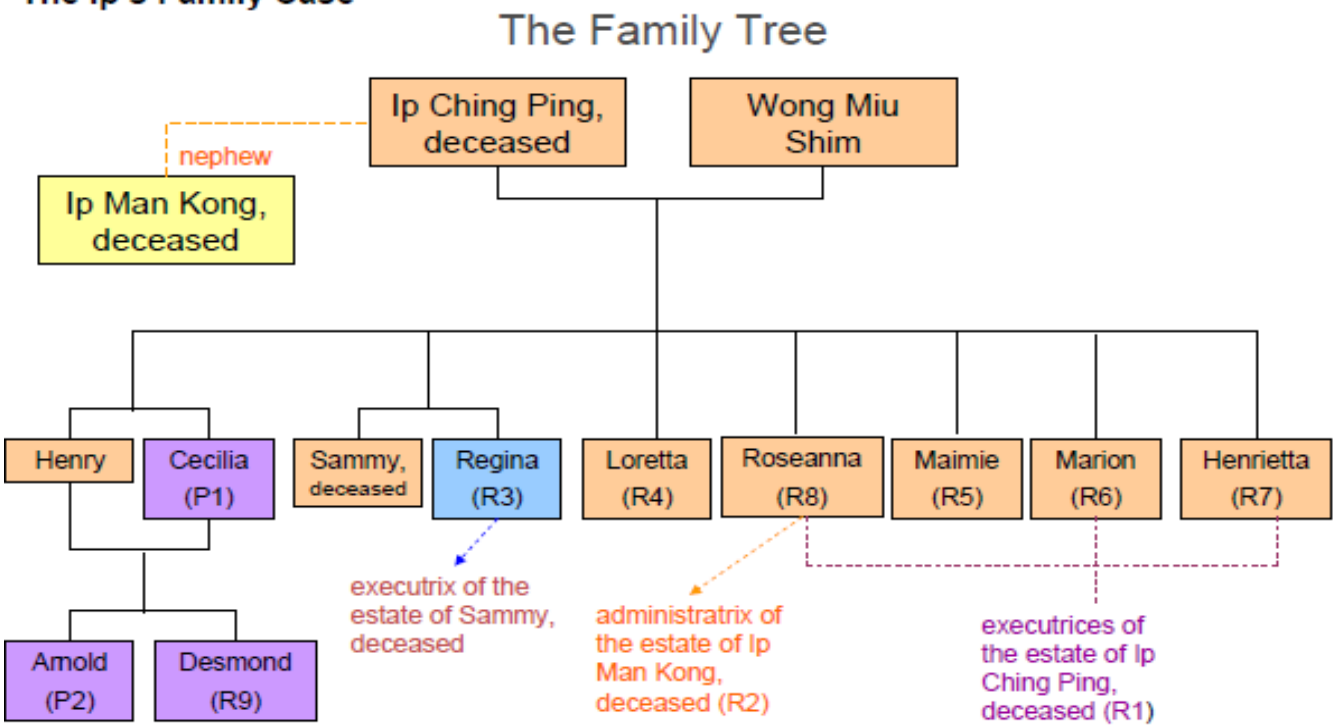
- (1) an association formed or continued on the basis of a personal relationship involving mutual confidence;
- (2) an agreement, or understanding, that all, or some, of the shareholders, shall participate in the conduct of the business; and
- (3) restriction on the transfer of the members' interest in the company.

Common Understanding

- ***Re Ching Hing Construction Co Ltd*** **HCCW 889/1999**

HCCW 889/1999

The Ip's Family Case



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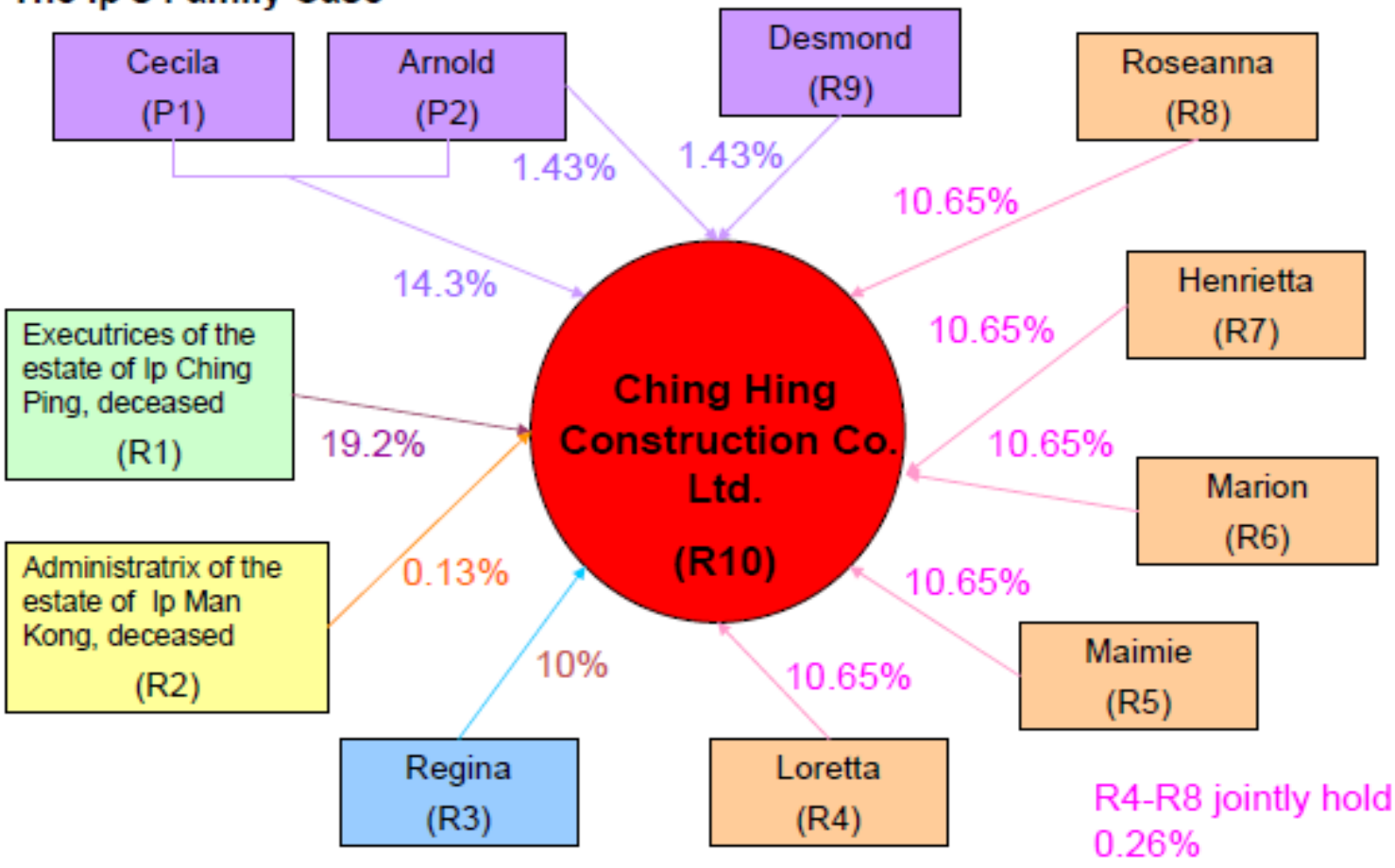
HCCW 889/1999

The Ip's Family Case



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The Ip's Family Case

1. The Company used to be in construction business, now mainly derives its income from leasing of properties (8 properties + 42 car park spaces, at estimated value of about $200m).
2. Petitioner petition for a buy out order under s.168A or alternatively for an order to wind up on the just and equitable ground.
3. The protagonists to these proceedings are on the one hand Cecilia and Arnold and on the other, the five daughters/sisters of the Ip family, in particular, Henriettta.

The Ip's Family Case

The complaints:-

1. Petitioners contended there was a common understanding and/or implied agreement amongst all shareholders that each of the shareholders would be:
    - appointed and be allowed to remain as a director so as to take part in the management of the Company's affairs (right to participate in management);
    - entitled to share the profits of the Company in proportion to their respective shareholding in the Company (right to share profits)

The Ip's Family Case

2. Petitioners said it is part and parcel of the Common Understanding that the Company's profits and assets were to be distributed by way of directors' enumeration in proportion to shareholding since 1992.

3. Petitioners alleged that the 5 daughters, in breach of this Common Understanding, had wrongfully expelled Arnold from the board in the 1996 annual general meeting, thereby depriving the petitioners' right to manage the Company's affairs and to share its profits.

4. Petitioner further alleged that irrespective of the Common Understanding, the petitioners are unfairly prejudiced because the wrongful expulsion of Arnold from the board had deprived the petitioners of their right to participate in the Company's distribution of profits and assets, which had since around 1986 taken the form of director's enumerations and allowances.

The Ip's Family Case

Court's findings:-

- The Company being a family company is by itself not an adequate basis for the allegation of an implied agreement or understanding.

- The personal relationships among the members were not such that equitable restraints would be imposed on the exercise of their rights under the articles of association.

The Ip's Family Case

- While the five sisters no doubt enjoy harmonious relationships among themselves, that does not extend to other members.

- Any suggestion that the relationships among the family members (with the exception of the five sisters as a camp) involved a mutual trust, understanding and confidence is unfounded.

- Desmond may have a better relationship with his aunts. But that is not sufficient to ground the Common Understanding with Arnold.

The Ip's Family Case

- Hence, there was no Common Understanding that Arnold should remain a director and participate in the management of the company and drew director's enumeration.

- The enumerations of the directors are not excessive in the circumstances of the case, hence there was no unfair prejudice in this regard.

- **Result: Case dismissed.**

- N.B. But if Common Understanding proved to exist, it could override the rights of the majority under the company's articles.

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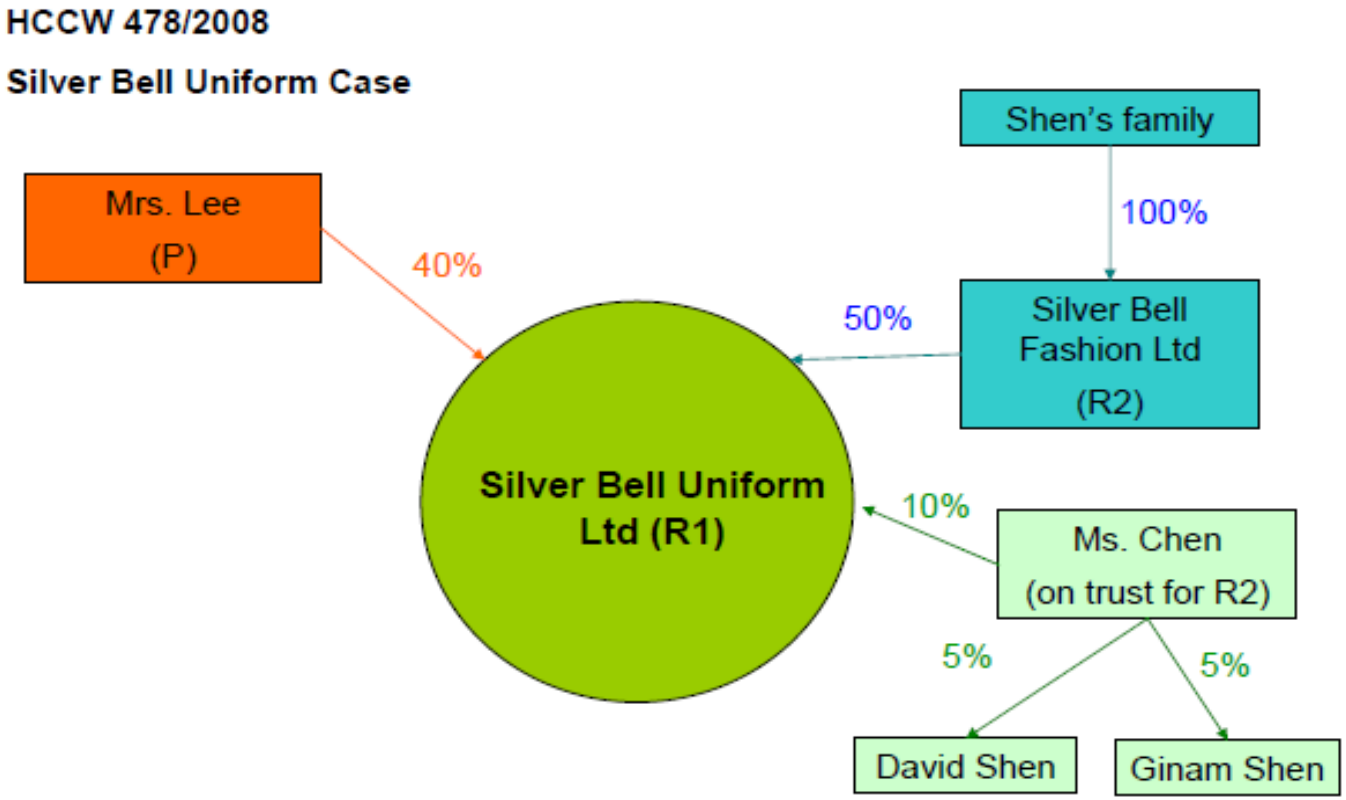
Common Understanding

- ***Re Silver Bell Uniform Ltd*** **HCCW 478/2008**



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Silver Bell Uniform Case

- **The Parties and the Background**

  - The Company: Silver Bell Uniform Limited
  - Petitioner **("P"):** Mrs. Lee, Ng Louise
  - 1st Respondent **("R1"):** Silver Bell Uniform Limited
  - 2nd Respondent **("R2"):** Silver Bell Fashion Limited (the Shen Family)

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Silver Bell Uniform Case

- P and Mrs. Shen Lian Yien Hwa (**"Shen"**) came to know each other when they both worked in a company which specialized in the business of the production and sales of uniforms.
- When the company ceased business in 1992, Shen and P decided to set up the Company to do the same kind of business.
- She acted as the managing director and P acted as its general manager.
- Shen became ill in 2006 and left P with the running of the Company until she died in April 2008.
- The Shen Family discussed appointing David Shen as Managing Director of the Company, to which P objected on the grounds that he did not have any experience of the business.

Silver Bell Uniform Case

Alleged unfair prejudice / unjust or inequitable conduct:-

1. The Shen Family circulated an announcement to staff and customers on 10 June informing them that David Shen would be managing director with effect from 16 June 2008, notwithstanding P's objection.
2. P then proposed that either the Shen Family buy her shares or the Company be wound up.
3. David and Ginam made it clear that they wished P to stay with the Company. P explained that she did not with to remain, and said that she wished to leave and set up a competing business.

Silver Bell Uniform Case

4. P resigned on 12 September 2008 effectively from 16 October 2008. She began to approach the Company's customers and staff.
5. As a result, the Shen Family purported to terminate P's employment on 23 September 2008.
6. P then wrote multiple letters repeating her offer to sell her shares, but the Shen Family maintained their refusal to buy them.
7. This eventually led to presentation of the Petition on 13 October 2008.
8. P claimed that at the time the Company was established, both P and Shen discussed the management of the Company and agreed that if either R2 or P wished to withdraw from the Company, either the remaining shareholder should buy the departing shareholder's shares or the Company should be wound up.

Silver Bell Uniform Case

Court's Findings:-

- The Court found that P and Shen did agree at the time of the Company was established that if one of them wished to leave the Company, the other shareholder would buy the departing Party's shares.
- The Court was concerned with whether or not the way in which the Company had been operated for 16 years and the understandings, implicit perhaps rather than express, underlying the way in which its affairs were conducted make it unjust to require the P to remain a shareholder.

Silver Bell Uniform Case

- Regard was had to the fact that between 2006 and 2008 the Shen Family did not take any steps to replace or assist the P in the management of the Company.
- This suggests that the Company was generally understood by the P, Shen and the other members of her Family to be a venture between the P and Shen.
- In those circumstances the Court considered it unjust to require the P to have to work with a new partner in whom she does not have confidence.

Silver Bell Uniform Case

- The Court concluded that the way in which the affairs of the Company were conduced prior to Shen's death gave rise to equitable considerations, which made it unfair for the Shen Family to insist on their legal right to appoint David Shen as Managing Director without offering to buy P's shares.

- P was found to be entitled to relief, and the Shen Family has to buy out P's shares.

Yung Kee case: is it just and equitable to wind up the Company?

The CFA's findings (agree with Harris J)**:-**

1. The business was started by Kam Senior. The intention was for his two sons to run the restaurant business together.
2. Both of the brothers began working in the restaurant from the bottom.
3. The business was run as an "integrated family operation".
4. There was mutual understanding between the brothers that each should fully participate in the running of the business and be properly consulted. And implicit in this understanding was mutual respect.
5. The deceased was entitled to have reasonable expectation, in the light of previous practices, that his views and position within the group be respected.
6. But such common understanding was breached by Kwan Lai.

Yung Kee case: is it just and equitable to wind up the Company?

7. The Court took into account following facts:
   (1) Kwan Lai had the Company's Articles of Association amended.
   (2) Kwan Lai appointed his son, Carrel, a director of the Company as well as of its subsidiaries.
   (3) The deceased was not properly consulted beforehand.
   (4) The deceased's proposal to hold a meeting first to discuss the proposals was ignored.
   (5) Later on, by the majority control in the board, Kwan Lai was appointed the authorized representative of Long Yau.
   (6) Despite objection from the deceased, Carrel and his sister Yvonne were given substantial increases in salary.
   (7) Despite objection from the deceased, one of the Company's property in Chai Wan was used by Carrel and Yvonne for their own business rent-free.

Yung Kee Restaurant Case

Conclusions:

- There was a common understanding between the brothers that each was entitled to fully participate in the running of the business and be properly consulted.

- Kwan Lai had behaved in a manner which was inconsistent with the way in which he and the deceased had previously conducted the business and behaved towards one another.

- In particular it is clear that Kwan Lai quite consciously took steps to control the Company and then exercised that control without proper regard to previous understandings.

Order made by the CFA

1. The court ordered winding-up of the Company.

2. But the winding up order was stayed for 28 days to give the parties an opportunity to agree the terms on which the petitioner's shares in the Company should be purchased.

3. If no such agreement is reached before the expiration of the period, the winding up order will take effect automatically.

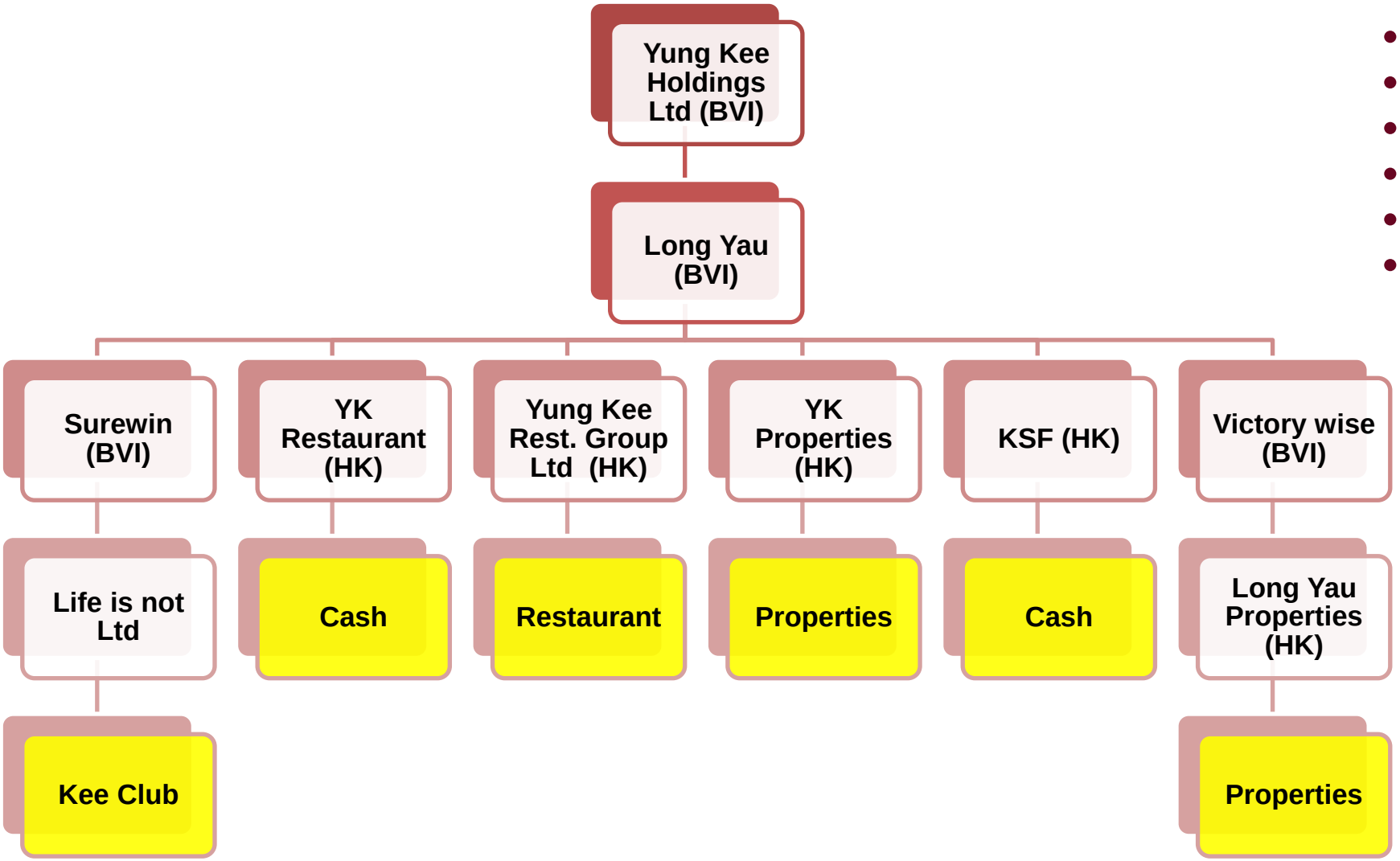
Valuation Issues

(1) Basis of Valuation

- Property valuation
- Company Valuation

(2) Should there be a discount for minority interest?

(3) Instances of unfairly prejudicial conduct for which specific allowances should be made


Yung Kee Holdings Ltd (BVI)
Long Yau (BVI)
Surewin (BVI)
YK Restaurant (HK)
Yung Kee Rest. Group Ltd (HK)
YK Properties (HK)
KSF (HK)
Victory wise (BVI)
Life is not Ltd
Cash
Restaurant
Properties
Cash
Long Yau Properties (HK)
Kee Club
Properties

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Valuation

Type of Co	Remarks	Asset / Income	P	R
YKR Group	Operating Co	Profit Making	Valued as Going Concern P/E basis	Valued as Going Concern - DCF
LY Properties, YK Properties	Properties holding	Rental income	Assets Approach	Assets Approach
Surewin Victory wise KSF Long Yau	Investment Holdings	Holding shareholdings, cash deposit etc	Assets Approach	Assets Approach
Life is not Ltd	Operating Co, net def.	Loss making	Assets Approach	Assets Approach
YK Restaurant	Dormant	Cash deposit	Assets Approach	Assets Approach

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Basis of valuation (Property)

- **Market Value: “**the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm’s-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.”

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Basis of valuation (Property)

- Special assumptions?
- Kwan Lai's assumptions: the existing tenants of the Properties including the restaurant and office areas in Yung Kee Building will continue in occupation at market rents, that the Properties will continue to be used by members of the Group as at present and will not be sold or redeveloped

- Kwan Sing: the properties should be valued on the basis of vacant possession and the best rent that can be obtained for the premises.

- As a result, the Respondent only used comparable transactions for restaurants and disregarded all the other retail or commercial properties comparable transactions when those users are likely to attract higher returns and thus higher value.

Basis of valuation (Property)

Harris J:-

- A valuer may make special assumption in his valuation.
- It was the intention of both parties that they should carry on the business of the Yung Kee Restaurant, should they end up as the owners of the Company.
- Therefore, Yung Kee Building should be valued on the basis that it would be used for restaurant and office purposes only, and would not be put to use in some other potentially more profitable way, so as to maximize its value.
- A valuer would be directed to ignore the possibility of the property being let out to a non-restaurant tenant, such as a retailer, who would, given the location of the property, be willing to offer substantially higher levels of rental that would be offered by an operator of a restaurant.

CA agrees.

Basis of valuation (Property)

Comparative Method vs. Investment Method

- Comparative Method: Valuers have to find close comparables. If they are available they provide an accurate and reliable method for determining valuations. If they are not available then the valuer has to find the closest comparables and make adjustments to them. The greater the adjustments the more room for error and disagreement.

- The 2 comparables chosen required adjustments of 74.2% and 74% respectively.

Harris J:-

- Difficulty in finding suitable comparables.
- Both the comparable method and the investment method should be used and the results averaged to produce the valuation of the properties.

Basis of valuation (Company)

P/E multiple vs. Discounted Cash Flow method

- The YKR Group should be valued as a going concern.
- A P/E (price to earnings) ratio approach is entirely dependent on identifying one or more comparable companies, whose P/E ratios can be used as a guide to what is appropriate for YKR Group.

  - Difficulty: YKR Group is unique.
  - Is Tao Heung directly comparable?

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Basis of valuation (Company)

Harris J:-

- **No.** Tao Heung is a very different type and scale of business :
  - Tao Heung operates restaurants and bakeries in Hong Kong and Mainland China;
  - It operates restaurants under 14 different brands;
  - It had a logistics center which could service 200 restaurants;
  - As of 31 December 2010 it operated 81 restaurants: 65 in Hong Kong and 14 in the Mainland;
  - It also provides food catering services and produces, sells and distributes food products including frozen foods, invest in properties, and had a large number of promotion services;
  - Its business is expanding rapidly in Hong Kong and Mainland China.

Basis of valuation (Company)

- Tao Heung is so different in important respects to YKR Group that it provides an unreliable guide to what a fair value of the latter is.
- No prudent businessman considering buying YKR Group would consider that Tao Heung's P/E ratio provided much of a guide to what he might pay to acquire YKR Group.
- DCF method is well accepted and widely used in large-scale transactions.
- Given the absence of any useful comparable for determining a P/E ratio the DCF method of valuing YKR Group should be used.

Discount for minority interest?

- In the case of a buy-out order made in relation to a **quasi-partnership** company under s.168A, the usual order is that the petitioner's shares be purchased without a discount for the fact that the interest is a minority interest.

- But where no quasi-partnership, in the absence of special circumstances, P's minority shareholding should be valued on a discounted basis: *Irvine v Irvine (No 2)* [2007] 1 BCLC 445

  - There is a quasi-partnership, so there would not be any discount for minority interest.

Specific allowance for unfairly prejudicial conduct

- The court will, in general, value the shares as if the unfairly prejudicial conduct had not taken place. This can be achieved by making specific allowance in the valuation for the unfairly prejudicial conduct: *Hollington, Shareholders' Rights*, 8-62

  - Increase in Carrel's remuneration 
    - although Kwan Lai should not have done that against Kwan Sing's will, the remuneration was not excessive. Valuer does not need to discount it
  - Excessive remuneration to Yvonne 
    - there was no justification in paying her $45,000 per month for working half day on Saturday on the Group's accounts. It need to be clawed back for valuation purpose
  - Use of Company's premises for personal benefit 
    - the evidence does not suggest that it had any adverse financial impact on the Company

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Action to pre-empt petition

- A reasonable offer to buy out the petitioner's shares at a fair price may be a bar to a winding up petition: *Boyle, Minority Shareholders' remedies, p.103*

- ***Re A Company (No.002567 of 1982)*** **[1983] 1 WLR 927**
  - P, C and R were shareholders in a company having one-third of the issued share capital each and acting as joint managing directors. The relationship between them broke down and P was excluded from management of the company. C and R offered to buy P's shares at a fair market value fixed by an independent expert, but P rejected the proposal and petitioned to have the company wound up on "just and equitable" grounds.
  - Vinelott J: the court had a direction to refuse a petition for winding up if a petitioner was acting unreasonably in refusing to accept the offer to purchase his shares at a valuation.
  - The petitioner was not entitled to a winding up order.

What constitutes a reasonable offer?

O'Neill v Phillips **[1999] 1 WLR 1092**, at pp.1106-1108:

1. The offer must be to purchase the shares at a fair value. This will ordinarily be a value representing an equivalent proportion of the total issued share capital without a discount for its being a minority holding. But there may be cases in which it will be fair to take a discounted value.
2. If not agreed, the value must be determined by a competent expert.
3. The offer should be to have the value determined by the expert as an expert. The procedure need not to be elaborate.
4. Both parties should have the same access to information about the company relating to the value of the shares, and should have the right to make submissions to the expert.
5. Normally the offer should cover the costs of the petitioner.

Lessons learned

1. The starting point to assess “unfair prejudice” and “just and equitable” ground is the company’s constitution documents, shareholder agreement and the Ordinance.
2. However, they may be overridden by the “common understanding” of the shareholders established by context, verbal agreement or conduct.
3. For foreign companies, the “unfair prejudice” remedy requires the establishment of “a place of business” in Hong Kong, i.e., the company must carry some substantial business here and has a permanent location.
4. For winding up foreign companies, the presence of shareholders within the jurisdiction is a weighty factor to satisfy the requirement of “sufficient connection”.
5. To pre-empt winding-up petition, the majority should make a reasonable offer to buy out the minority.

Thank you! 

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