

COURT OF FINAL APPEAL - WINDING UP FOREIGN COMPANIES IN HONG KONG

Introduction

On 11 November 2015, the Court of Final Appeal (the “CFA”) handed down its decision ending the 8-year family feud between members of the second-generation owners of the much-loved Yung Kee restaurant.

The CFA ruled that Yung Kee Holdings Limited (the “Company”), be wound up, but gave the parties 28 days within which to discuss a share buy-out. The decision has attracted the close attention of both Hong Kong’s legal community and fans of the iconic family restaurant as it represents a landmark determination on principles concerning the Hong Kong Courts’ jurisdiction to wind up foreign companies.

A copy of the full judgment can be found at www.gallhk.com.

Background

Yung Kee is a local family restaurant business set up in the 1940s by the Petitioner’s father, Kam Shui Fai (“**Kam Senior**”). The Company was incorporated in 1994 in the British Virgin Islands.

Inheriting the family business from Kam Senior, Kam Kwan Sing (the “**Petitioner**”) and his brother Kam Kwan Lai (the “**1st Respondent**”) carried the signboard of Yung Kee for a short while before ending up in a heated dispute over management of the business.

As the minority shareholder, the Petitioner sought:

1. a buy-out order against the 1st Respondent on the ground that the 1st Respondent had run the company in a manner unfairly prejudicial to the Petitioner; and
2. an order that the Company be wound up on just and equitable grounds.

In relation to the buy-out order, neither the CFA nor the lower Courts found that the Company had an established place of business in Hong Kong, being a necessary requirement for a minority buy-out order under section 168A of the predecessor Companies Ordinance (Cap. 32). As the Company owned the Yung Kee restaurant indirectly through its subsidiaries and did not directly own any other businesses in Hong Kong, the decision on this point was unsurprising.

However, in relation to an order that the Company be wound up, the CFA overturned the decisions of both the Court of First Instance (“**CFI**”) and the Court of Appeal (“**CA**”). In doing so, the CFA confirmed the following principles.

Core Requirements

Before exercising its statutory jurisdiction to wind up a foreign company, the following core requirements must be met:

- A. there must be a sufficient connection with Hong Kong;
- B. there must be a reasonable possibility that a winding up order would benefit the applicants; and
- C. the Court must be able to exercise jurisdiction over one or more persons in the distribution of the company's assets.

The decision reaffirmed the earlier decision in *Re Beauty China Holdings Ltd* [2009] 6 HKC 351. However, it was the way in which these core requirements were applied by the CFA that makes the Yung Kee decision interesting. In particular, the CFA's focus on the first core requirement, i.e. whether the Company had a sufficient connection with Hong Kong.

Sufficient Connection with Hong Kong

Creditors vs Shareholders' Petition

It has long been thought that a shareholders' petition should be subject to a more stringent "connection to Hong Kong" test than a creditors' petition. In overturning both the Court of Appeal and Court of First Instance in that regard, the CFA found that:

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

The CFA found the factors relevant to establish a "connection" were different between a shareholders' petition vs. a creditors' petition. This was due to the difference in the nature of the dispute and the purpose of the winding up. The differences can be summed up in the following table:

	Company Status	Parties	Nature	Purpose	Essential Factor
Creditors' Winding-Up Petition	Insolvent (generally presumed)	Petitioner vs. Company	A third party creditor seeking relief against the company	To obtain payment of debts	<u>Significant assets</u> within Hong Kong which may be made available to the liquidator for the distribution among the creditors
Shareholders' Winding-Up Petition	Solvent	Petitioner vs. Other Shareholders (although company is a party, it is merely the subject of the dispute)	Dispute between the shareholders based on equitable principles	To realise petitioner's investment in the company	<u>Shareholders</u> are within the jurisdiction (i.e. in Hong Kong)

In the context of a shareholders' winding-up petition, it is worth emphasising that the CFA considered it a highly relevant factor, if not the most important factor, that the shareholders and directors were all within the jurisdiction.

Together with other relevant factors (e.g. the underlying dispute involved a family dispute between parties who were all in Hong Kong, lack of any connection with the jurisdiction in which the Company was incorporated, and the fact that the whole of the Company's income was derived from business carried on in Hong Kong), the CFA was satisfied that the Company's connection with Hong Kong was "compelling".

Separate and Distinct Legal Entities

It is worth noting that in the lower Courts, the 1st Respondent argued successfully that the interposition of subsidiaries between the Company and the ultimate company operating the Hong Kong businesses effectively 'blocked' any connection between the Company and Hong Kong. This argument was premised upon the fundamental concept that each company was separate and distinct from its subsidiaries and shareholders.

Although the CFA acknowledged this point, the Court held that it did not prevent a finding of "connection" because the Petitioner was not seeking to "lift the corporate veil". Rather, the Petitioner was seeking to realise his investment in the Company. If the Company was a holding company, the Petitioner's purpose would be to realise the underlying assets. Accordingly, there would be no reason why assets of a subsidiary should be excluded from consideration when determining whether the Company had a sufficient connection with Hong Kong. The nature of the dispute and purpose of the proceedings was again, of primary importance.

Decision

Based on this determination, the CFA found that the Company had a sufficient connection with Hong Kong, and met the other "core requirements" for the Company to be wound-up.

With a view to giving the parties an opportunity to agree on a possible buy-out, the CFA ordered that the winding-up be stayed for a period of 28 days from the date of the decision. If no buy-out agreement could be concluded, the winding-up order would take effect automatically after expiry of the 28-day period.

Conclusion

The Yung Kee corporate structure involving multiple layers of holding companies outside the jurisdiction of Hong Kong is not uncommon. As aggrieved Hong Kong shareholders naturally come to the Hong Kong Courts for relief, this decision improves their chances of doing so despite popular usage of corporate structures involving foreign incorporated holding companies.

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