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The Commercial Unit, Civil Division
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What's inside

Editorial

We feature three articles in this edition. The first article is an overview of the legislative proposals of the improvement of corporate insolvency law exercise. As the last major amendment exercise of the corporate insolvency and winding-up provisions in Hong Kong was conducted back in 1984, the Government now wishes to conduct a comprehensive review to ensure that our legislation does not lag behind other major jurisdictions. The second article talks about the execution of documents by a company by use of a seal and without a seal under the new Companies Ordinance (Cap. 622). The third article is an overview of the Insurance Companies (Amendment) Bill 2014 under which an independent Insurance Authority will be established to enhance the regulation of the insurance industry in Hong Kong.

We also feature three case reports in this edition. The first case is about the equitable doctrine of undue influence in the context of a third party legal charge – whether the evidence justifies a conclusion that the impugned transaction was procured by undue influence. The second case is about the issue of choice of law in an agreement for the transfer of shares in two Mainland companies. The Court of Final Appeal held that a three-stage approach should be adopted. The third case is about the interpretation of regulation 56 of Table A of the old Companies Ordinance (Cap. 32) – whether a single member can constitute a quorum at a general meeting of the company.

YUNG Lap-yan

An Overview of the Legislative Proposals of the Improvement of Corporate Insolvency Law Exercise

Introduction

The corporate insolvency and winding-up provisions in Hong Kong were first introduced in 1865 and those in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) ("C(WUMP)O") are broadly based on the Companies Act 1929 and the Companies Act 1948 of the UK. As the last major amendment exercise of these provisions was conducted back in 1984, there is a need to conduct a comprehensive review to ensure that our legislation does not lag behind other major jurisdictions.

In April 2013, the Financial Services and the Treasury Bureau ("FSTB") launched a public consultation[1] regarding legislative proposals to improve the corporate insolvency and winding-up regime in Hong Kong.

Major Proposals

Some highlights of the legislative proposals include:

Appointment and release of provisional liquidators or liquidators

FSTB proposes to expand the list of persons disqualified for appointment as provisional liquidator or liquidator to cover those with a conflict of interest, e.g. creditors, debtors, directors, company secretaries, auditors, receivers/receivers and managers. These persons are not qualified for such appointment except with the leave of the court. Similarly, a person who is subject to a disqualification order under Part IVA of C(WUMP)O may only accept such appointment after obtaining leave of the court.

A new statutory system of disclosure of information on potential conflicts of interest is proposed for the appointment of provisional liquidators and liquidators whereby a prospective provisional liquidator and liquidator will be required to make a statement of relevant relationships and to provide it to the relevant party empowered to make such appointment such that the appointing party could make an informed decision.

To enhance regulation of liquidators, FSTB proposes to introduce provisions to the effect that liquidators would not be absolved from liabilities arising from their misfeasance or breach of duty notwithstanding their release by the court.

Standalone unfair preference provisions

FSTB proposes to introduce standalone provisions in C(WUMP)O on "unfair preferences" which would largely reflect the relevant provisions in the Bankruptcy Ordinance (Cap. 6) ("BO") and rectify the existing anomalies arising from applying those provisions to the winding-up context. For example, in the application of the definition of "associate" under the BO, while the term "debtor" refers to the bankrupt in the bankruptcy context, the same term can only mean the debtor company but not a director of the debtor company in the winding-up context. Thus, this definition of "associate", which covers the spouse and relatives of the bankrupt, does not cover the spouse and relatives of a director of the debtor company when applied in the winding-up context. Moreover, in the definition of "associate" under the BO, a company is an associate of a debtor if that debtor has control of the company or if the debtor and persons who are his associates together have control of the company. When applying the definition in the winding-up context, a subsidiary of the debtor company is included as its associate, but not its holding company or another subsidiary of its holding company.

The only major change of the new standalone provisions from the position in the present law is that instead of making reference to an "associate of the debtor", the new provisions would make reference to a "person who is connected with the company", namely a director or shadow director of the company or an associate of the same, or an associate of the

[1] Consultation Document – Improvement of Corporate Insolvency Law Legislative Proposals (http://www.fstb.gov.hk/fsb/ppr/consult/doc/impcill_consult_e.pdf).

company. The proposed definition of "associate"[2], which largely follows the existing definition under the BO and the equivalent UK provisions, includes family members and relatives, those in an employment relationship, those in a trustee/beneficiary relationship and circumstances of inter-company control.

New provisions on "transactions at an undervalue"

Currently, there is no provision in C(WUMP)O which is specifically designed to avoid transactions at an undervalue. FSTB proposes that a transaction will only be caught if the court is satisfied that a company makes a gift or enters into a transaction under which it receives no consideration or a consideration the value of which is significantly less than the value of the consideration provided by the company, and that at that time the company is unable to pay its debts or becomes unable to pay its debts as a result of the transaction, within the period of 5 years ending with the commencement of its winding-up. The company will be presumed (unless the contrary is shown) to be unable to pay its debts at that time or becomes unable to pay its debts as a result of the transaction where the transaction is entered into with a "person who is connected with the company" (otherwise than by reason only of being its employee). Where the company has entered into the transaction in good faith and for the purpose of carrying on its business and at that time there were reasonable grounds for believing that such transaction would benefit the company, it is proposed that the court will not set aside the transaction.

Invalidation of floating charges for no new value created before winding-up

At present, a floating charge created within 12 months of the commencement of the winding-up of a company (unless it is proved that the company immediately after creation of the charge was solvent) shall be invalidated, except for the amount of any cash paid to the company at the time of or after the creation of and in consideration for the charge ("new value").

As the existing provisions in C(WUMP)O do not distinguish between floating charges created in favour of persons connected with the insolvent company and those created in favour of persons not so connected, FSTB proposes that the clawback period for a floating charge created in favour of a "person who is connected with the company"[3] be extended to 2 years, and that the requirement to ascertain whether the company was solvent immediately after creation of the floating charge be removed where the chargee is a "person who is connected with the company".

Currently, new value is limited to "cash paid to the company". To address the restrictiveness of the existing provision for exempting genuine credit transactions from invalidation, FSTB proposes to expand the scope of exemption to include "money paid to or at the direction of the company" and "property or services supplied to the company".

Current state of play

The Administration is now studying carefully the comments on the legislative proposals received in preparing the necessary legislation.

Ida Chan
Ted Tyler

Execution of Documents under the new Companies Ordinance

Common seal optional

Under section 124 of the new Companies Ordinance (Cap. 622) ("new CO")[4], it is optional for companies to have a common seal.

Execution of documents by use of seal

Where a company has a seal and wishes to use it for execution of documents, it may do so in a manner similar to the previous law. That is, the seal is to be affixed on the document in accordance with the company's articles of association: new CO section 127(1)-(2). For example, under the new default articles (referred to as the Model Articles), the seal can only be used under the authority of the board of directors, and the document to which the seal is affixed must also be signed by: (a) 2 directors; (b) a director and the company secretary; or (c) a director

[2] The proposed definition of "associate" will apply to the definition of a "person who is connected with the company" used in relation to both the proposed provisions on unfair preference and those on transactions at an undervalue.

[3] The expression "a person who is connected with the company" shall have the same meaning ascribed to it for the purposes of the proposed provisions on transactions at an undervalue and unfair preferences.

[4] Effective 3 March 2014.

and a person authorized by the board to sign documents to which the seal is affixed: Companies (Model Articles) Notice Schedule 1 article 102 (public companies), Schedule 2 article 81 (private companies). That requirement is similar to regulation 114 of the former Table A of the predecessor Companies Ordinance (Cap. 32)[5].

Execution of documents without a seal

Not all documents or contracts executed by a company must be under seal. It is only in particular situations, such as where a document is to be executed as a deed, that the document would need to be executed under seal. For companies which do not have a seal or do not wish to use its seal, new CO section 127(3)-(5) is relevant where the document needs to be under seal. Under those provisions, a document has effect as if it had been executed under a common seal if the document is signed by either 2 directors or by a director and the company secretary, and so long as the document is expressed to be executed by the company. Where the company only has one director, then the above requirement for signatures is satisfied by having that sole director signing.

Since the commencement of the new CO, some questions have been raised as to the interaction between section 127 and provisions in companies' articles dealing with the use of the common seal. The following points may be noted.

There is no need for the articles to contain an express provision authorizing the company to rely on new CO section 127(3)-(5) before the company is entitled to execute a document without a seal pursuant to those provisions. The power of companies to do so is derived simply from the Ordinance.

The above position applies even if the company's articles have a provision on the use of seals in a form similar to the Model Articles. Those provisions do not mandate the use of the common seal but only provide for how the seal is to be used.

Even where the articles of a company specifically provide that documents or particular types of documents must be executed under the common seal, it would appear that the company may still rely on section 127(3)-(5). This is because section 127(5) deems the document to be executed as if it was under seal. Since signatures in accordance with section 127(3)-(5) means that the document is executed as if under the common seal, this should satisfy the requirement in the articles for execution under seal.

A company's articles could specify that documents can only be executed with the signatures of more than 2 authorised persons. Where the provision is dealing with the number of signatures to accompany the affixing of the seal, then prima facie there must be compliance with the articles such that all the required persons must sign on the document to which the seal is affixed. This follows from new CO section 127(2) which requires compliance with the articles. However, notwithstanding non-compliance, there is a presumption, in favour of a person dealing with a corporation in good faith, that a deed is duly executed by the corporation if it bears the seal of the corporation and is affixed in the presence of and attested by either two directors or by a director and the secretary: Conveyancing and Property Ordinance (Cap. 219) section 20. A person who knows that the articles have not been complied with would not be entitled to rely on the statutory presumption[6].

Similar to the above, it is conceptually possible that a company's articles could specify that documents must be signed by more than 2 authorised persons though the seal need not be used. For example, the articles might simply state that certain company documents must be signed by 3 directors. What is the position if only two directors sign, in compliance with new CO section 127(3)-(5), but contrary to the articles? The document is deemed to be executed under seal (section 127(5)), but that does not necessarily mean that the document is enforceable against the company. Even a document affixed with the seal and signed by the persons specified in the articles is potentially unenforceable against the company if the persons did not have authority to enter into the transaction or if there were other requirements in the articles for entering into the transaction that were not complied with.

Assuming that the company has authorized the transaction, the document is enforceable against the company where new CO section 127(6)-(7) applies. Under those provisions, in favour of a purchaser acting in good faith for valuable consideration, a

[5] For companies which previously adopted Table A, the provisions in Table A continue to apply, subject to any amendments which the particular company chooses to make, and subject also to any provisions of the new CO which override inconsistent articles.

[6] As to whether persons would be treated as having constructive notice, see below on new CO section 120.

document is to be regarded as having been executed by a company if the document purports to have been signed in accordance with section 127(3). Where the third party dealing with the company had actual notice that the articles were not complied with, then it may be that the third party would not be regarded as having acted in good faith and would not be able to rely on section 127(6)-(7). Even in the absence of actual notice, there is a possibility that a third party can be imputed with constructive notice of the non-compliance, in which case it is possible that such a person can also be regarded as not acting in good faith for the purpose of the above provisions. A person is not to be regarded as having notice of any matter 'merely' because the matter is disclosed in the articles: new CO section 120[7]. However, a person may still be imputed with constructive notice depending on the nature of the transaction or other circumstances[8].

Accordingly, for transactions with companies where there is a reasonable opportunity for checking the company's articles before entering into the transaction, it remains prudent for the third party to check the articles to ensure that the execution of the document would comply with the articles[9].

Execution of deeds

New CO section 128 provides that a company may execute a document as a deed by executing it in accordance with section 127, having it expressed to be executed as a deed, and delivering it as a deed. "Delivery" means an intention to be bound by the deed. A document is presumed, unless the contrary is proved, to be delivered as a deed on its being executed in accordance with section 127: section 128(2). Therefore a company may now execute a deed either with the use of a seal or simply by signatures of the requisite persons in accordance with sections 127, 128.

Stefan Lo

[7] Equivalent of section 5C of the predecessor Companies Ordinance (Cap. 32).

[8] See Hansard (8 January 1997) pp 98-99, on the Companies (Amendment) Bill 1996 which introduced the predecessor section 5C.

[9] This applies for both where the seal is used and where the seal is not used.

An Overview of the Insurance Companies (Amendment) Bill 2014

Background

The establishment of an independent Insurance Authority ("IIA") to enhance regulation of the insurance industry is the most important regulatory reform in the insurance sector in the past 30 years since the passage of the Insurance Companies Ordinance ("ICO") in 1983. The Government made its first attempt in 2003 which was met with strong opposition from the industry. The proposal was raised again in 2011. The Government conducted two rounds of public consultations, which culminated in the Insurance Companies (Amendment) Bill 2014 ("the Bill").

Objectives of the Bill

The policy objectives of setting up the IIA are to modernize and strengthen the regulatory infrastructure to facilitate the stable development of the insurance industry, provide better protection for policyholders, and align with international practice that insurance regulators should be financially and operationally independent of the Government.

Major features of the amendments

Functions of the IIA

Insurance has the social value of cushioning the public financially against unfortunate events. In addition to promoting best practices among insurance practitioners, it is equally important to educate the public on the nature of insurance, features of particular insurance products and assessment of insurance needs against various risks. The following new functions of the IIA are therefore proposed –

(a) facilitating sustainable market development of the insurance industry;

(b) promoting understanding by policyholders and potential policyholders of insurance products and the insurance industry; and

(c) conducting studies relevant to the insurance industry and sharing the research findings with the industry.

Governance and Funding Mechanism

The IIA will be a body corporate with perpetual succession. To ensure that the IIA is financially independent of the Government, the IIA will be financed by a 0.1% levy on all newly paid insurance policy premiums and licence fees payable by insurers and insurance intermediaries.

Licensing of Insurance Intermediaries

Under the new regime, a person requires a licence granted by the IIA to carry on "regulated activities", which are defined to cover activities in relation to giving advice on insurance and sale and after-sale administration of insurance policies (e.g. policy renewal or insurance claims), in the course of their business or employment or for reward. Persons such as lawyers and accountants providing advice wholly incidental to their professional practice, and clerical or administrative staff of an insurance company will be exempted.

More than 80,000 insurance intermediaries currently registered with the three self-regulatory bodies will be allowed to continue to work for three years before they need to apply for licences from the IIA.

Conduct Regulation and Consequences of Misconduct

Fair and credible regulation of the conduct of insurance intermediaries will enhance public confidence in insurance which will in turn be conducive to the sustainable development of the insurance industry. Conduct regulation is aimed to ensure that insurance intermediaries act professionally, fairly and honestly, and that the licensees are fit and proper persons, e.g. they are professionally competent, financially sound and have a good track record of legal and regulatory compliance.

Following from the above, the IIA will be vested with appropriate powers of inspection and investigation of misconduct. The IIA will also have the power to impose sanctions on those found guilty of misconduct, ranging from reprimand, suspension or revocation of licence of insurance intermediaries or authorization of insurers to a civil fine of up to HK$10 million or 3 times the amount of the profit gained or loss avoided by the person as a result of the misconduct, whichever is the greater.

Banks' Insurance Intermediary Activities

At present, banks also operate insurance agency services through their retail networks. Given the integrated asset and wealth management services offered by banks, as well as the Hong Kong Monetary Authority ("HKMA")'s role as the primary and lead regulator of banks, it is proposed that the IIA may delegate its powers of inspection and investigation to HKMA for the frontline regulation of banks' insurance intermediary activities.

The IIA and HKMA will have to establish collaborative arrangements on regulatory cooperation, reciprocal staff secondment, regular liaison meetings, etc. The IIA will remain the single authority to set regulatory requirements, grant licences and impose disciplinary sanctions.

Checks and Balances

At the governance level, the Bill proposes that the IIA will comprise a majority of non-executive directors in order to ensure effective oversight of executive decisions. It prescribes that certain powers of the IIA will be non-delegable, e.g. the power to make subsidiary legislation. The Director of Audit may conduct value for money audit on the IIA whereas IIA's practices and procedures are subject to examination by the Independent Commission Against Corruption.

At the regulatory level, the Bill requires the IIA to consult the insurance industry before introducing new regulatory requirements by way of subsidiary legislation. Its regulatory decisions, including licensing, authorization and disciplinary decisions are subject to review by a statutory and independent quasi-judicial body, the Insurance Appeals Tribunal ("IAT"). The IAT will be chaired by a person qualified to be appointed as a High Court judge. In addition, the internal process and procedures of the IIA in exercising regulatory powers will be reviewed by an independent Process Review Panel to be established by the Chief Executive.

Removal of Outdated Regulatory Requirements

Under the existing self-regulatory regime for insurance intermediaries, the insurers are laden with certain statutory responsibilities for supervising insurance agencies and agents. Failure to fulfil these responsibilities is a criminal offence. For example, an insurer is required to keep a register of insurance agents appointed by it, comply with the Code of

Practice for the administration of insurance agents, and follow up a complaint referred to it by the self-regulatory body (including investigation, reporting findings of investigation to and taking disciplinary action as required by the self-regulatory body). With the new statutory licensing regime for insurance intermediaries, such statutory responsibilities imposed on insurers will become outdated and would therefore be removed.

Danny Yuen

Bank of China (Hong Kong) Ltd v Tsang Sheung Bun [2013] 5 HKLRD 62

The essence of the equitable doctrine of undue influence is that one party has acted unconscionably by exploiting his influence to direct the conduct of another which he has obtained from the relationship between them[10]. This commentary focuses on the issue of undue influence considered by the Court of Appeal (the "Court") in the captioned case.

Facts

A legal charge (the "Charge") was entered into between Bank of China (Hong Kong) Ltd (the "Plaintiff") as lender, Tsang Sheung Bun (the "Defendant") as mortgagor and a company as borrower (the "Borrower"). The Defendant was a friend of the shareholders of the Borrower. The Charge over the Defendant's property served as security for facilities granted by the Plaintiff to the Borrower. It contained a joint and several covenant of the Borrower and the Defendant to repay all monies due to the Plaintiff.

The Borrower subsequently defaulted under the facilities. Pursuant to the Charge, the Plaintiff claimed vacant possession of the Defendant's property and monies due by the Borrower, while the Defendant counterclaimed for a declaration that the Charge was null and void on various bases, including undue influence. At trial, judgment was given in favor of the Plaintiff and the Defendant's counterclaim was dismissed. The Defendant appealed.

Decision

The Court considered that for the Defendant to succeed in his defence on undue influence, he had to persuade the Court to reverse the trial judge's finding of fact that the Defendant was not subject to any undue influence. The Court noted that the trial judge had referred to the Court of Final Appeal judgment in *Li Sau Ying v Bank of China (Hong Kong) Ltd*[11], in which it was held that the real issue should be "*whether the evidence justifies a conclusion that the impugned transaction was procured by undue influence*". The Defendant was found at first instance to have failed to prove that the Borrower's shareholders unduly influenced him into executing the Charge. The trial judge therefore did not further consider the issues below:

(a) whether the shareholders had unduly influenced the Defendant as the Plaintiff's agent;

(b) whether the Plaintiff was put on inquiry as to undue influence and if so, whether the Plaintiff would regard the transaction under the Charge to be apparently disadvantageous to the Defendant; and

(c) if the Plaintiff had constructive notice, whether it had taken reasonable steps to dispel constructive notice.

It was the above issues not considered by the trial judge that the Defendant sought to raise before the Court. Issue (c) and the first limb of issue (b) were first dealt with. The Court applied *Bank of China (Hong Kong) Ltd v Personal Representative of Fu Kit Keung*[12] and held, where on a balance of probabilities the evidence did not justify an inference that the transaction under the Charge was procured by undue influence, the Plaintiff could neither be said to have constructive notice of any alleged impropriety of the said transaction, nor should the Plaintiff be put on inquiry such that it could not rely on the apparent consent from the Defendant in respect of the said transaction. The Court regarded it unnecessary to further consider if the Plaintiff had taken reasonable steps to dispel constructive notice, which was simply absent.

The Court then dealt with issue (a) and applied *Bank of China (Hong Kong) Ltd v Wong King Sing*[13], where

[10] Halsbury's Laws of Hong Kong [280.019]

[11] [2005] 1 HKLRD 106

[12] [2009] 5 HKLRD 713

[13] [2002] 1 HKLRD 358

it was held that the mere fact that a debtor approached a surety upon request from bank to obtain security for facilities did not mean that the debtor was acting as the bank's agent. Such fact could also be found in the present case. The Court held that the argument that the Borrower's shareholders were acting as the Plaintiff's agent to procure the Charge did not have any evidential basis.

The Court finally dealt with the second limb of issue (b). *Bank of China (Hong Kong) Ltd v Leung Ngai Hang*[14] was applied. The Court held that given the Plaintiff did not have actual or constructive notice of any relationship between the Defendant and the Borrower's shareholders that indicated any risk of abuse, the mere fact that the transaction under the Charge might be (or even was) manifestly disadvantageous to the Defendant was not sufficient to give rise to a presumption that the Charge was obtained by undue influence. The Court concluded that the defence of undue influence must fail on the evidence.

Further thoughts

The present case did not involve actual undue influence (if actual undue influence had been established, the Charge would become automatically voidable) but presumed undue influence. It requires a determination of whether a dominant party can be presumed to be in a position to exercise undue influence; and whether undue influence can be presumed to have been exercised as the agreement in question calls for an explanation. If the aforesaid are satisfied, the agreement in question would be voidable unless rebutted by the dominant party.

The relationship between the Defendant and the Borrower's shareholders did not fall under the special category where a position to exercise undue influence would be presumed. Accordingly, the first hurdle to be overcome by the Defendant was for him to prove that the evidence justified a finding that the transaction under the Charge was procured by undue influence. On the facts of the present case, the Defendant had failed to discharge the said burden of proof.

Quinnci Wong

[14] CACV 250/2005

First Laser Ltd v Fujian Enterprises (Holdings) Co Ltd & Anor [2013] 2 HKC 459; (2012) 15 HKCFAR 569

The commentary below focuses on aspects of the governing law of contract considered by the Court of Final Appeal ("CFA").

Facts

The first defendant, Fujian Enterprises (Holdings) Co Ltd ("D1"), was a company incorporated in the Hong Kong Special Administrative Region ("HKSAR") and a "window company" of the Fujian Provincial People's Government of China, of the People's Republic of China ("Mainland"). D1 set up a joint venture ("JV") in the Mainland with another Mainland company, Fujian Research Institute of Material Structures of the Academy of Science ("FRIM"), for the production of non-linear crystals. D1 later bought up all the interests in the JV owned by FRIM after disputes arose between D1 and FRIM.

Subsequently, D1 approached the plaintiff, First Laser Ltd. ("P"), a company incorporated in Macau, as a new partner of the JV. P and D1 entered into various agreements, under one of which D1 was to transfer 51% of the shares of two Mainland companies, namely Fujian Casix Laser Inc ("FCL") and Fuzhou Casix Optronics Inc. ("FCO"), to P whilst P was to provide capital contribution to the JV ("Agreement").

After P made the required capital contribution, the FCO shares were transferred to the JV (but not to P), and the transfer of the FCL shares never took place. D1 subsequently sold all the FCL shares to a third party.

Court proceedings were commenced in HKSAR by P to enforce the Agreement and in the Mainland by D1 to avoid it. A dispute over the choice of law arose as the Agreement did not specify the governing law.

In 2004, the Supreme People's Court of the Mainland ("SPC") decided that Mainland law applied and that the Agreement was therefore invalid as the transfer of the FCO and FCL shares lacked the required approval from the relevant authority.

Subsequently in 2008, the Court of First Instance of HKSAR ("CFI") ruled that HKSAR law applied and that D1 was in breach of contract, but this was overturned by the Court of Appeal of HKSAR.

CFA's decision

CFA dismissed P's appeal unanimously.

Reasoning

Issue estoppel

CFA held that at common law, a judgment of a foreign court of competent jurisdiction which is final and conclusive and on the merits would be conclusive in HKSAR proceedings if the parties are the same and the issues are identical (the principles on issue estoppel in the case of Carl Zeiss Stiftung v Rayer & Keeler Ltd (No 2), [1967] 1 AC 853 applied).

For the purposes of the conflict of law question, CFA held that HKSAR and Mainland are separate law districts and that a judgment of SPC is a "foreign judgment". In the present case, the judgment of SPC on, inter alia, the applicable law and the validity of the Agreement, was a judgment of a foreign court of competent jurisdiction which was final and conclusive and on the merits and was therefore conclusive in the present HKSAR court proceedings. P defended the proceedings before the SPC and thereby submitted to the jurisdiction of SPC. In other words, the judgment of SPC gave rise to an issue estoppel.

Common Law's Approach to Choice of Law Question

CFA further held that even if their hands were not tied by issue estoppel, they would have decided, under the common law principles, that Mainland law applied to the Agreement.

CFA held that at common law, the choice of law issue is, in theory, considered in three stages and in the following order: (i) in the absence of an express choice of law as the first test ("First Stage"), (ii) the court would consider as a second test whether there are any other indications of the parties' intention ("Second Stage") and (iii) only if there are no such indications would the court go on to consider as the third test what system of law the contract has its closest and most real connection ("Third Stage"). CFA made the observation that, in practice, the courts frequently moved straight from the First Stage to the Third Stage.

Applying the three stages to the present case, in the absence of an express choice of law, CFA jumped to the Third Stage and concluded that Mainland law applied having regard to the fact that the subject matter was shares in Mainland companies and the only possible place of performance in relation to the transfer of shares was the Mainland.

Remedies

CFA accepted experts' evidence on Mainland law that if the Agreement was invalid, P as an "innocent party" would be entitled under Mainland law to two remedies, namely, restitution and compensation.

Considered that D1's offer of restitution had been rejected by P, CFA ordered the issue of restitution under Mainland law be remitted to CFI. On the other hand, CFA found no basis for remitting the claim for compensation.

Annie Cheung

Re China Star Enterprise Hong Kong Ltd [2013] 5 HKLRD 271

This is an appeal to the Court of Appeal on whether a member would be regarded as a quorum at a general meeting of a company.

Facts

Mr Koo and Mr Hung are the shareholders as well as directors of China Star Enterprise Hong Kong Ltd (the "Company"). Pursuant to regulation 51 of Table A, Schedule 1 of the Companies Ordinance (Cap. 32) (now repealed – see Companies (Model Articles) Notice, Cap. 622H) which was adopted by article 1 of the Company's articles of association, Mr Koo gave notice to Mr Hung to convene an extraordinary general meeting on 11 October 2011. Mr Koo attended the meeting, but Mr Hung did not. As a quorum was not present, pursuant to regulation 56 of Table A, the meeting was adjourned to the same time the following week. Mr Hung did not attend the adjourned meeting. Mr Koo argued that pursuant to regulation 56 of Table A, after 30 minutes the meeting was deemed quorate and he passed a resolution to appoint his son as an additional director.

Mr Koo asked the Court to determine, inter alia, that such appointment was valid and effective.

Court of Appeal's Decision

The Court found for Mr Koo and took the view that, properly interpreted, regulation 56, enabled one member to constitute a quorum.

Reasoning

The Court applied the purposive and contextual approach in legislative interpretation as affirmed in *Vallejos and Domingo v Commissioner of Registration*[15] and took into account the established law on meetings and the legislative history of regulation 56.

Under common law, "meeting" means a coming together of more than one person[16]. This principle applied even when the single member was present in more than one capacity, i.e. holding proxy for another member as illustrated in *Re Prain & Sons Ltd*[17].

The Court in this case, however, took the view that the general principle that a meeting necessarily involved two persons could be abrogated by legislation. An example was section 114B of the CO which empowered the court to direct that one member of the company present in person or by proxy should be deemed to constitute a meeting.

In this case, what constituted a quorum at a meeting of the Company would be determined by reading section 114A as well as Table A of the then Companies Ordinance (Cap. 32) (the "CO").

Section 114A(1)(c) of the CO provides that:

"(1) Subject to …, the following provisions shall have effect in so far as the articles of the company do not make other provision in that behalf;

(a) …;
(b) …;
(c) 2 members personally present shall be a quorum;
(d) …;
(e) …"

The requirement of "2 members personally present" in section 114A(1)(c) had been replaced with article 22 of the articles of association of the Company, which provided:

"For all purposes, the quorum for all general meetings shall be two members personally present or by proxy and no business shall be transacted at any general meeting unless the requisite quorum be present at the commencement of business."

The change is simply that, instead of requiring a quorum of two members to be present, under article 22, the quorum of two members is only required at the commencement of the meeting.

Regulation 56 further provides that:

"56. If within half an hour from the time appointed for the meeting a quorum is not present, the meeting, if convened upon the requisition of members, shall be dissolved; in any other case it shall stand adjourned to the same day in the next week, at the same time and place or to such other day and at such other time and place as the directors may determine, and if at the adjourned meeting a quorum is not present within half an hour from the time appointed for the meeting, *the members present shall be a quorum*. (Emphasis added.)"

The question in the present case was whether regulation 56 had the effect of abrogating the general principle.

The Court took the view that case law[18] and textbooks[19] recognised the fact that the general principle could be excluded by the provisions of the articles of the company.

If section 7 of the Interpretation and General Clauses Ordinance (Cap. 1) which provides that words in the plural include the singular is adopted, the plural "members" in regulation 56 is to be read as a singular "member" and a quorum was properly constituted by the presence of Mr Koo only.

Regulation 56 was amended in 1984 but no change was made to the word "members".

The Court recognized that the provisions of Cap. 1 was subject to contrary intention in Cap. 1 or from the

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15 [2013] 2 HKLRD 533, [75] – [77].

16 *Sharp v Dawes* (1876) 2 QBD 26 and *Re Sanitary Carbon Co* [1877] WN 223.
See also *Palmer's Company Law*, Vol.2, paras. 7.601 and 7.603; and
Annotated Ordinances of Hong Kong: Companies Ordinance (Cap.32) (2006), at para. 111.03 by Tomasic, Tyler and Scott.

17 [1947] SC 325.

18 *Daimler Co Ltd v Continental Tyre and Rubber Co (Great Britain) Ltd* [1916] 2 AC 307.

19 *Farrar's Company Law* (4th ed., 1998) p. 317.

context of any other ordinance. As there was no contrary intention in regulation 56 or in CO which precluded the application of section 7 of Cap. 1, the Court believed that regulation 56 clearly was to override the two member quorum provision and to prevent deadlocks from being perpetuated where there was only one member present at the original meeting and later at the adjourned hearing. In short, regulation 56 enabled one member to constitute a quorum.

The Court thus took the view that the amendments to the CO in 1984 and the inclusion of "member" or "members" in other provisions of Table A were not clear indications that the legislature intended the quorum to be more than one member. It believed that using the word "members" in regulation 56 while allowing it to be construed in the singular where the context required would provide it with a degree of flexibility as regulation 56 might be adopted by companies with different numbers of members and with different quorum provisions. Hence the presence of Mr Koo at the adjourned meeting would be considered a quorum and the resolution to appoint Mr Koo's son as an additional director was valid and effective.

Elen Lau

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