EASTERN CARIBBEAN SUPREME COURT
TERRITORY OF THE VIRGIN ISLANDS

IN THE HIGH COURT OF JUSTICE

CLAIM NO. BVIHC (COM) 0126 OF 2011

BETWEEN

WANG ZHONGYONG
LIN HUI
ZHU YAQING
GONG YUDA
GAO YUNTAI
LU YIMIN
ZHU MINGXING
QIU JIAJUN

Claimants

-v-

UNION ZONE MANAGEMENT LIMITED
JIN XIAOYONG
WEN LIMING
MA GUOMEI

Defendants

Appearances:
Mr Matthew Collings QC, Mr Ray Ng and Ms Claire-Louise Whiley for the Claimants
Mr David Fisher and Mr René Butcher for the second to fourth Defendants
The first Defendant was not represented and did not appear

JUDGMENT

[2013: 30 September, 1-4, 5, 16 October]

(Unfair prejudice proceedings – Claimants minority shareholders in group holding company - whether conduct by majority of the affairs of a subsidiary amounted to breach of an understanding between the shareholders of holding company – just and equitable winding up

– **Virdi v Abbey Leisure**[1] and dictum of Lord Hoffmann in **O'Neill v Phillips**[2] considered)

[1] **Bannister J [Ag]:** This is a claim by eight of the eleven members of the first Defendant Company, Union Zone Management Limited ('Union Zone'). The other three members, who between them control 56.7% of the shares of Union Zone, are the second to fourth Defendants. Union Zone takes no part in these proceedings. It was incorporated in the Virgin Islands on 28 July 2004. It is the majority shareholder (51.94%) in a Nevada registered company called Aida Pharmaceuticals, Inc ('Aida USA'). The other members of Aida USA are (a) Tore Biotechnology Co. Ltd ('Tore') (31.296%) and (b) unidentified members of the public (16.764%). Aida USA is the sole owner of a Virgin Islands company called Earjoy and Earjoy in turn owns a PRC company called Hangzhou Aida, which was established to, and until 2011 was actively engaged in, the production of clinical pharmaceuticals. Hangzhou Aida has a number of PRC subsidiaries, which are engaged in related trades, and it holds a small stake in another PRC company which appears to operate in an unrelated commercial area.

[2] The Claimants are thus minority shareholders in a company, Union Zone, which indirectly controls, although it does not own, Hangzhou Aida and its mainland PRC subsidiaries.

[3] The second Defendant, Jin Xiaoyong, is the son of the late Jin Biao, who died unexpectedly on 14 July 2009. The third and fourth Defendants are Jin Xiaoyong's wife and mother. As the case was tried, they played no part in the narrative. The late Jin Biao was evidently a forceful and charismatic individual, who negotiated the changes experienced by the PRC during the second half of the last century[3] and ended up as a successful business man running not only Hangzhou Aida, which appears to have been spun off from a former Chinese State or Provincial pharmaceutical enterprise in around early 1999, but also a related company, Zhejiang Guobang Pharmaceutical Co Ltd ('Guobang'),which appears to have had its origins in a former village/trade union co-operative. Guobang produces veterinary pharmaceuticals and figures to some extent in the story.

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[1] [1990] BCLC 342
[2] [1999] 1 WLR 1092
[3] he was born on 5 August 1948

[4] In these proceedings, which were commenced in October of 2011, the Claimants claim various relief under section 184I of the Business Companies Act, 2004 ('section 184I'), on the grounds (in short) that the affairs of Union Zone have been conducted in a manner unfairly prejudicial to them in their capacity as members of Union Zone and, independently, for the appointment of a liquidator to Union Zone under section 169(1) of the Insolvency Act, 2003, on the grounds that it would be just and equitable to do so.

[5] The relief which is sought under section 184I is for the appointment of a liquidator under the Insolvency Act and in the alternative for an order that the Claimants be permitted to compulsorily purchase the shares in Union Zone held by the majority second to third Defendants.

[6] The pleaded grounds for seeking this relief are that 'the idea' behind all of the companies in the group headed up by Union Zone was for each of the Claimants and Jin Biao to work together as partners with active participation and responsibilities in the business. The Claimants plead that when or shortly after Union Zone was incorporated in 2004 it was the understanding between them and Jin Biao that each would share in the management of Union Zone and each of its subsidiaries ('the Group'); that they would form the entire management of the Group to the exclusion of all others; that each would be consulted on all major business decisions affecting the Group; and that each would have the right to veto any substantial commercial decision affecting the Group. On this basis, it is alleged that Union Zone was a quasi partnership company. It is further alleged that Hangzhou Aida was jointly owned by 'all the investors involved' as a quasi partnership company. It is alleged that following the death of Jin Biao, it was agreed between the Claimants and Jin Xiaoyong that he should join in the management of Hangzhou Aida on the terms of the understanding which I have set out above and that in breach of those terms he has excluded the Claimants from all aspects of the business of the Group. These allegations omit to mention that after his re-appointment, following the death of his father, the Claimants, or at any rate certain of them, acting in concert with the owners of Tore, had excluded Jin Xiaoyong, until he brought about his reinstatement with the assistance of the Chinese Courts.

[7] The pleaded grounds for seeking the appointment of a liquidator under the Insolvency Act are that Union Zone was incorporated for the purpose of 'having an investment platform for Aida USA' for its eventual public listing in the United States and that that has become impossible of

achievement following the death of Jin Biao. In those circumstances, it is said, it is just and equitable that Union Zone should be wound up.

[8] I shall have to consider in a moment whether on the evidence which has been presented to the Court the Claimants have established an entitlement to any of this relief, but before I do that I should sketch out a little of the history.

Background

[9] In around 2003 Jin Biao, who controlled each of Hangzhou Aida and Guobang, decided that he wished to make each company -a Wholly Foreign Owned Enterprise – in effect, to take its ultimate management and control offshore while leaving the operational entity in the PRC. At the same time, Jin Biao was looking for outside investment.

[10] Such an outside investor manifested itself in 2002 or thereabouts. The investor was Asia Business Corporation, referred to throughout as 'Yashang,'[4] and in May of 2004 a structure was put in place whereby Hangzhou Aida (and Guobang) were taken over by a BVI registered company called Best Nation Investments Limited ('Best Nation'), which was itself the wholly owned subsidiary of another BVI registered company called East Crown Group Limited ('East Crown'). East Crown's shares were issued to and held by Jin Xiaoyong (68.29%) and the eighth Defendant, Qiu Jiajun (31.71%). This was done in preparation for an investment by Yashang, made in July of 2004, in exchange for which Yashang[5] acquired 40% of Best Nation, reducing East Crown's holding to 60%. The result was that Yashang became the indirect owner of 40% of Hangzhou Aida (and Guobang), while control remained with Jin Bao.

[11] These arrangements were expanded upon in two agreements in writing. The first was a so-called framework agreement, entered into on 13 February 2004 between a Yashang entity, Best Nation and East Crown. This document envisaged a listing, to be accomplished by way of a reverse takeover, on an offshore capital market, for Best Nation. A Supplementary Agreement, executed on some date in 2004 not discernible in Arabic numerals but which it is agreed governed the Best Nation arrangements, provided, among other things, for Best Nation's board to comprise five directors, of whom three were to be appointed by

[4] the word apparently derives from the Mandarin pronunciation of the Group's name
[5] through its nominee, Winsummit China Growing Holdings Ltd

East Crown and two by Yashang. It further provided for the Articles of Association of each of Hangzhou Aida and Guobang to be amended to provide for boards of five directors in each case, with Yashang entitled to appoint two members. Business targets were to be set internally by each of Hangzhou Aida and Goubang, but if they were not met Yashang had the right to appoint replacement or additional (it is not specified which) management personnel. Yashang was given an express right to supervise the operations of Hangzhou Aida and Guobang and, in appropriate circumstances, to appoint an independent auditor. Each of these agreements was subject to the laws of Hong Kong, with a non-exclusive jurisdiction clause in favour of the Courts of the Hong Kong SAR.

[12] Although the details were never illuminated, it is clear that the 31.71% of East Crown held by Qiu Jiajun was intended to be held by him as nominee for the Claimants, of whom he and the first and second Claimants were active in the management of Hangzhou Aida and he, together with the third to seventh Claimants, in the management of Guobang. It is also tolerably clear, and I find, that these nominee holdings were intended to represent shares or entitlements originally held by the Claimants in Hangzhou Aida and Guobang but which had had to be surrendered when those companies became wholly owned subsidiaries of Best Nation. The details, fortunately, do not matter. Jin Xiaoyong held his East Crown shares upon trust for his father, Jin Biao.

[13] Jin Biao, Qiu Jiajun and Yashang then set about attempting to obtain a listing for Hangzhou Aida on a foreign stock exchange, since there was at that time no immediate intention to list Guobang, whose business model was different from that of Hangzhou Aida. The first step was to take Hangzhou Aida out of the Best Nation structure. Best Nation therefore transferred Hangzhou Aida to another BVI company called Earjoy. Yashang (and its nominees) were given 40% of Earjoy to reflect Yashang's 40% of Best Nation. The remaining 60% of Earjoy was issued to Union Zone, which had been acquired for the purpose. Union Zone's shares themselves were held by Jin Xiaoyong and Qiu Jiajun in the same proportions in which they held shares in East Crown (68/32). Again, it is clear that Jin Xiaoyong held his shares for his father and that Qiu Jiajun was given his Union Zone shares as nominee for himself and the other Claimants, to reflect the fact that Hangzhou Aida had been taken out of the East Crown structure and to leave the Claimants with the same overall entitlements to each of Guobang and Hangzhou Aida

as they had had when both those companies were subsidiaries of East Crown.

[14] No separate agreements governing the new Earjoy structure were referred to in evidence. The inference must be that the Best Nation arrangements were intended to apply to the spun off Earjoy group, although it is not necessary for me to decide that.

[15] The next step was to insert a 'listing' vehicle between Earjoy and Union Zone/Yashang. The chosen vehicle was Aida USA. Aida USA either was or became entitled to have its shares traded on the inter-dealer marketplace for non-listed securities known as the Over the Counter Bulletin Board ('OTCBB'). As I understand it, OTCBB is not an exchange and the securities traded by its market maker members (any share registered with the United States Securities and Exchange Commission ('the SEC')) are not considered by the markets 'listed,' since OTCBB has no listing requirements other than that shares traded on OTCBB must be SEC registered. There is evidence that shares in Aida USA were traded on OTCBB between December 2005 and some time in 2008, when Aida USA ceased to maintain its SEC filing on grounds of expense. By that time 16.764% of Aida USA was held by the public, while Union Zone's holding had been reduced to 51.94%. The former Yashang holding had been reduced to 31.296% in aggregate. The size of the various holdings has not varied since.

[16] On 19 December 2006 the shares in Union Zone were redistributed so that Jin Biao held 38.1% and Jin Xiaoyong's wife 18.6%, on trust for Jin Biao; Qiu Jiajun held 20.22%; and the Claimants other than Qiu Jiajun were given the remaining 23.08% in small parcels ranging downwards from 5.3% to 1.31%. Jin Xiaoyong and Ma Guomei, the widow of Jin Biao, are presently the holders of the shares held by Jin Biao before his death.

[17] In April 2010, some nine months after the death of Jin Bao, Yashang sold its 31.296% holding in Aida USA to Tore. Tore is owned in equal shares by Ge Xiaohu ('Mr Ge') and Li Kemin ('Mr Li'). Mr Ge has a background in the pharmaceutical industry and was a friend and occasional business associate of Jin Biao during the latter's lifetime. He has given evidence in these proceedings and his written evidence, at any rate, demonstrated some considerable animus towards Jin Xiaoyong. He was behind Jin Xiaoyong's exclusion from Hangzhou Aida in the autumn of 2010. He has funded these proceedings to date and is

alleged by Jin Xiaoyong to be doing so with the ultimate aim of acquiring control of Hangzhou Aida and its subsidiaries. I should make clear that I do not regard any of these facts or allegations as material to the questions which I have to decide.

Quasi partnership

[18] It is common ground that in order to regulate, if that is the right word, the conduct of the shareholders of Union Zone towards each other, the understanding relied upon must have been formed no earlier than the time of the incorporation of Union Zone in July 2004. Mr David Fisher, who appeared, together with Mr René Butcher, for the second to fourth Defendants, was able to establish without much difficulty that the claim that the understanding was that the Claimants and the late Jin Biao should be entitled to manage the affairs of Union Zone and all of its subsidiaries to the exclusion of all others was unsustainable, as was the allegation that it was understood that each of the Claimants should be able to veto any substantial commercial activities of Union Zone or any of its subsidiaries. Mr Fisher submitted that, as a result, the Claimants had failed to establish the understanding which they had pleaded and that the unfair prejudice claim fell, as it were, at the first post. He relied upon clear authority to the effect that a claimant alleging unfair prejudice in the management of a company of which he is a member must be confined to the allegations pleaded in its petition or statement of claim. I agree with the proposition as a matter of principle, but I do not accept that it is as rigid as Mr Fisher would have it. The rule is intended to prevent a claimant who pleads, for example, only breach of an understanding for mutual involvement in management, from relying at trial upon a failure on the part of a majority to pay appropriate dividends. It is not, in my judgment, designed to require persons, such as the Claimants in the present case, to prove each and every last word of a general allegation of an understanding that every shareholder is entitled to participate in the management of a company's business.

[19] Where I am with Mr Fisher, however, is over his submission that if, as in the present case, it can readily be shown that key elements of an alleged complex understanding (such as exclusivity and veto) are unsustainable, the Court is entitled to approach what is left of the understanding after they have been stripped out with some caution. In this case the Court is presented with an alleged understanding which has the appearance of having been assembled by the pleader (none of Counsel or the lawyers who represented the Claimants at trial) from a

text book. That is not to say that, if proved, the Court should not act upon it, but it does, in my judgment, mean that if significant elements of it fall off at the first moment when any stress is placed upon it, the Court should ensure that it really is satisfied (on a balance of probabilities) that what remains was indeed the real understanding of the parties and governed their behavior towards each other in respect of the company in question.

[20] I am satisfied that there was, between the original parties, no common superimposed understanding for mutual participation in the business affairs of Union Zone, let alone of Union Zone and its subsidiaries. In other words, that there was, to use the language of Lord Wilberforce,[6] no 'something more.' Quite apart from the striking fact that Union Zone's Articles of Association contain none of the provisions commonly to be found in the articles of association of a company formed upon the basis of mutual participation and control, it is clear that whatever arrangements had previously operated to define the relationship between Jin Bao and the Claimants, and I shall come to those in a minute, they cannot have survived the absorption of Hangzhou Aida and Guobang into the Best Nation structure.

[21] In his witness statement Qiu Jiajun describes meetings going back as far as 2002 to discuss the new structure with the Yashang representatives. He says while the first to seventh Claimants were aware of what was going on and that Lin Hui and the fourth Claimant occasionally attended, Jin Biao and himself represented the Hangzhou Aida members while he alone represented the Guobang parties. It is plain that the purpose of the meetings which Qiu Jiajun is there describing are meetings to decide the size of the stake to be given to Yashang and the terms upon which it was acquired. Lin Hui describes how she participated in this process, providing, in her capacity as Chief Financial Officer of Hangzhou Aida, input from that perspective. Although she had mentioned, earlier in her witness statement, how it had been agreed and understood, when she acquired her shares in Hangzhou Aida in 2002, that the shareholders would work together as equal partners, she mentions no similar agreement or understanding being formed in relation to Best Nation or Earjoy.

[22] In his witness statement Qiu Jiajun goes on to say that Jin Biao and the Claimants were all very clear with each other that the agreement which I

[6] **Ebrahimi v Westbourne Galleries Ltd** [1973] AC 360 at 379E

have summarized at paragraph [6] above would always continue and that each would be entitled to share and participate in the management of Hangzhou Aida and Guobang through their shareholdings in East Crown. In describing the hiving off of Hangzhou Aida to the new Union Zone/Earjoy structure, Qiu Jiajun says nothing in his witness statement about any discussion taking place as to the relationship between Jin Biao and the Claimants under the new arrangements or as to any special terms upon which each of them was to hold his or her share in Union Zone.

[23] In cross examination Qiu Jiajun accepted, first, that there could have been no sort of quasi partnership arrangement at all between the members of the two different companies, Hangzhou Aida and Guobang, before they came together in the Best Nation structure. He also accepted that any partnership going forward can only have been a sub-partnership between the Claimants and Jin Biao, the other partner being Yashang As for the supposed partnership with Jin Xiaoyong, that was expressed to be a 'continuation' of the alleged partnership between the Claimants and his father.

[24] In cross examination Lin Hui said that the collaboration, or equal relationship, between herself, Qiu Jiajun and Jin Biao in the management of Hangzhou Aida (of which she became a member only in 2002, three years after it had been established) was 'extended' to Union Zone. Zhu Yaqing, the third Claimant, who was the only spokesman, as it were, to represent the interests of the third to seventh Defendants, former members and, in some cases, still managers of Guobang, said that he understood that he would be entitled to participate in the management of Union Zone and its subsidiaries in the capacity of a non operational shareholder[7] in Hangzhou Aida. He said that his opinions were passed on through Qiu Jiajun, although there was no evidence that Zhu Yaqing ever expressed any particular opinion on Union Zone, whether to Qiu Jiajun or to anyone else.

[25] It was clear to me, and I find, that the evidence given by Qiu Jiajun and Lin Hui in cross examination, and by Zhu Yaqing in cross examination and re-examination and intended to prove the existence of a quasi-partnership in Union Zone and its subsidiaries, was evidence about their relationship with Jin Biao as members and managers of, respectively, Hangzhou Aida and Guobang during his lifetime. While I accept, as Zhu

[7] he actually said 'share,' but the meaning was clear

Yaqing told me, that there may not have been a rigid line of demarcation between their involvement in the two companies, what these witnesses were describing was a golden age of managerial harmony in Hangzhou Aida and Guobang under the benevolent direction of Jin Biao as *primus inter pares,* itself falling far short of any understanding upon the basis of which they, or any other of the Claimants, acquired their shares in either of those companies, or tending to establish that those companies were run on the basis of some overriding understanding in the nature of a quasi partnership. As for Union Zone, while they may, if they had ever thought about it, have expected that, if ever a management decision had to be taken in Union Zone (there was no evidence that, beyond the decision to acquire shares in Aida USA, any ever had been or needed to be and the Claimants plead that Union Zone was only ever an investment vehicle which has never conducted any business) the same atmosphere would prevail, that could not amount to evidence of an understanding remotely like that pleaded, reached between the Claimants and Jin Biao, covering the parties' relationship with respect to Union Zone and its subsidiaries and upon which they agreed to accept shares in Union Zone when that company acquired, indirectly, a sixty per cent share in Hangzhou Aida from Best Nation.

[26] If, contrary to my view and to the view of Qiu Jiajun, there ever had been a species of quasi partnership governing the parties' relationship in Hangzhou Aida and Guobang overall, that cannot possibly have persisted into the Union Zone/Earjoy structure. That structure was designed ultimately to exchange any network of private understandings that may previously have existed in Hangzhou Aida and Guobang for public control – indeed, one of the Claimants' complaints is that it failed in that objective. In any case, and public control aside, the relationship with Yashang as forty per cent outside shareholder meant that no special relationship between the Claimants and Jin Biao *inter se* could be of any practical value or effect, as confirmed by Yashang's rights under the Supplementary Agreement to which I have referred above.[8]

[27] Finally, if there had been any such understanding in the Union Zone/Earjoy structure, it appears to have escaped the notice of Mr Ge, whose activities after the death of Jin Biao were wholly inconsistent with the existence of a special relationship of any sort.

[8] see paragraph [11]

[28] In my judgment, upon the evidence which has been offered in this case, the shareholders in Union Zone were never bound together by an agreement or understanding other than that set out in Union Zone's Articles of Association.

[29] It follows from that conclusion that there was no understanding (of the general nature pleaded) to which Jin Xiaoyong can have agreed to become party when he became a director of Hangzhou Aida in September 2009. It further follows that his exclusion of Qiu Jiajun and Lin Hui from the management of Hangzhou Aida in 2010 infringed or disappointed no rights, entitlements or legitimate expectations of any of the Claimants as members of Union Zone. Any complaints in respect of those matters are properly for the consideration of the Courts or Tribunals of the PRC, to which, as would be expected, the parties have resorted in relation to the affairs of Hangzhou Aida. They have no connection with this jurisdiction.

[30] The claim under section 184I accordingly fails.

Just and equitable winding up

[31] Of course, had unfair prejudice been established and had the Court come to the conclusion that Jin Xiaoyong's exclusion of Qiu Jiajun and Lin Hui justified the granting of relief under section 184I, one remedy open to the Court would have been to order the winding up of Union Zone under section 184I(2)(f). Mr Matthew Collings QC, who appeared, together with Mr Ray Ng and Ms Clare-Louise Whiley, for the Claimants made clear, however, that he seeks winding up on the just and equitable ground in the alternative to relief under section 184I.

[32] Mr Collings QC submits that the purpose of Union Zone and 'its corporate structure' have been frustrated. He submits that the minority has been excluded and that the business of Hangzhou Aida is in disarray. The minority has not, of course, been excluded from Union Zone (indeed, Qiu Jiajun remains a director of Union Zone) and the only persons excluded from Hangzhou Aida are Qiu Jiajun and Lin Hui. It seems to me that Mr Fisher is right when he submits that unless the Claimants can show some reason why it was inequitable for Jin Xiaoyong to have excluded Qiu Jiajun and Lin Hui from Hangzhou Aida, those cannot be grounds for winding up Union Zone. Because I have found that there was no understanding between the Claimants and Jin

Xiaoyong which was violated by the dismissal of Qiu Jiajung and Lin Hui, those dismissals cannot, it seems to me, justify the winding up of Union Zone at the instance of the Claimants. The Claimants retain their shares in Union Zone and the fact that Hangzhou Aida is not presently producing is not, in my view, a ground for winding up Union Zone in circumstances where Jin Xiaoyang gave evidence, which I have no reason to reject, that he intends to restart production in due course using a new supplier.

[33] Mr Collings QC makes a different point. He submits that the purpose of the incorporation of Union Zone was to act as what he calls an investment platform in order to gain a listing for the group. He says that no listing has been achieved and that the purposes for which it was incorporated have accordingly become frustrated. Citing Virgil, he says that this entitles the Claimants to a winding up order, so that they can recover their investment.

[34] There was some debate at trial whether Aida USA's brief sojourn on OTCBB amounted to a listing, in the ordinary sense of that word. I am satisfied that it did not. No one would describe Aida USA, while it was on the OTCBB, as a listed company. That, incidentally, was also the opinion of Jin Xiaoyong expressed in cross examination.

[35] There is no doubt that where parties agree that a company in which they propose to invest is to engage in a specific business and no other, a minority will ordinarily be entitled to a winding up order if the majority, upon cesser of that business, intends to employ the company's capital in some different business.[9] However, even assuming, which is far from obvious to me, that Union Zone is properly to be treated as an 'investment platform/vehicle,'[10] rather than as the holding company of the Claimants' and Jin Biao's sixty percent interest in the Hangzhou Aida group, I do not think that this case falls within the principle.

[36] The principle is engaged where a shareholder is being forced to watch his capital employed in a venture which it was expressly agreed that the company should not embark upon. In the present case, it was agreed, or must be taken to have been agreed, that Union Zone would hold the Claimants' and Jin Biao's interest in Aida USA and its subsidiaries. The fact that it was hoped that ultimately Union Zone would become the

[9] **Virdi v Abbey Leisure Ltd** [1990] BCLC 342

[10] concepts which Mr Collings QC had some difficulty in elucidating as they might apply to Union Zone

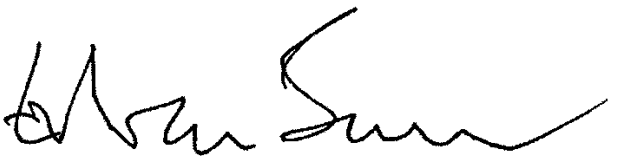
holder of shares in a listed company does not involve the consequence that the Claimants' capital is being employed in a venture which it was agreed should not be undertaken. It is true that the restructuring did not produce the fruits which it was hoped (how realistically may be open to question) that it would, but that goes to commercial disappointment, not to violation of an agreement reached between to co-venturers.

[37] In **O'Neill v Phillips**[11] Lord Hoffmann, without citing any particular authority, identified a slightly different principle which may justify winding up, not depending upon breach of an understanding, but on the occurrence of an event which destroys the basis of the parties' association. That is not this case. The parties' association as members of Union Zone is not grounded upon a state of affairs which no longer exists.

[38] In my judgment, therefore, the Claimants fail to show any grounds making it just and equitable to wind up Union Zone.

Conclusion

[39] This claim accordingly fails.



Commercial Court Judge
16 October 2013

[11] [1999] 1 WLR 1092 at 1101H-1102B