

**IN THE EASTERN CARIBBEAN SUPREME COURT
TERRITORY OF THE VIRGIN ISLANDS**

IN THE HIGH COURT OF JUSTICE

CLAIM NO. BVIHC (COM) 94 OF 2014

BETWEEN:

- 1. BEST NATION INVESTMENTS LIMITED**
- 2. EAST CROWN GROUP LIMITED**

Claimants

And

- 1. QIU JIAJUN**
- 2. ZHU YAQING**
- 3. LIN HUI**
- 4. GONG YUDA**
- 5. ANTOW HOLDINGS LIMITED**

Defendants

Appearances:

Mr David Fisher, Mr Robert Nader, instructed by Messrs Forbes Hare for the Claimant; Mr Peter McMaster, Q.C., Ms Sarah Masson, instructed by Messrs Appleby for the Defendant

2017: March 7, 8, 9, 15, 16, 17

March 28

JUDGMENT

- [1] **Wallbank J. [Ag]:** In this claim both sides accuse the other of improperly attempting to gain control over a company registered in the People's Republic of China ("PRC") called Zhejiang Guobang Pharmaceutical Co. Ltd. ("ZG"). The dispute is between two factions: the family of the late Mr JIN Biao ("Mr JIN B" and "the JIN Parties" respectively) and, on the other hand, Mr QIU Jiajun and his associates ("Mr QIU" and "the QIU Parties" respectively). A key person on the JIN Parties' side is Mr JIN Xiaoyong ("Mr JIN X"). By this Judgment the Court sets aside two series of transactions carried out by the QIU Parties. The effect is to restore the *status quo* prior to the transactions in terms of shareholder control of the Claimants and ZG. That is merely the secondary effect, not the Court's primary intention. I express no views on the merits of either side's claim to majority control, nor of the commercial wisdom of one side rather than the other being ultimately in control of ZG. The reason those transactions are to be set aside is that the QIU Parties, who were directors of the First Claimant, did not undertake those transactions honestly and in good faith and in what as directors they believed to be in the best interests of the company, and also, they did not exercise their powers for a proper purpose, but to pursue their own benefit. In respect of the second series of transactions, a key step was undertaken by Mr QIU without due authority, vitiating the entire second series.
- [2] Before February 2004 there were two companies in the PRC, ZG and Hangzhou Aida Pharmaceuticals Co., Ltd. ("Hangzhou Aida"). One produces veterinarian medication, the other human medication.
- [3] Mr QIU's evidence is that he founded ZG, together with the Fourth Defendant, Mr GONG Yuda. The Claimants say Mr JIN B controlled both ZG and Hangzhou Aida and that Mr QIU had a minority interest in both, and the remainder of the QIU Parties were minority shareholders in one or other of these companies, but not both. Mr JIN B and Mr QIU were business partners. They appear to have got on well during Mr JIN B's lifetime. Problems arose, or came to the surface, between the QIU and JIN Parties following Mr JIN B's death. Mr JIN B passed away unexpectedly on 14 July 2009.

- [4] Mr JIN B and Mr QIU had decided in around 2003 that they would combine ZG and Hangzhou Aida into a group of companies which would ultimately be held offshore.
- [5] The offshore holding vehicles were to be the Second Claimant (“East Crown”) and the First Claimant (“Best Nation”).
- [6] East Crown was incorporated in the TVI on 6 March 2003 with an authorized share capital of US\$50,000 divided into 50,000 shares with a par value of US\$1 each, of which 10,000 shares were issued and fully paid up. At all material times the Board of East Crown comprised two or more persons, and, at the material times included Mr JIN X and Mr QIU.
- [7] Best Nation was incorporated in the TVI on 13 May 2003. It had an authorized share capital of US\$50,000 divided into 50,000 shares with a par value of US\$1 each.
- [8] The relevant holding structure was that the JIN and QIU Parties respectively would own shares in East Crown. Initially East Crown was to hold 100% of the shares in Best Nation. Best Nation was to hold 100% of the shares in ZG.
- [9] Mr JIN B and Mr Qiu decided upon this structure because they planned to take the new group public in the United States of America, through a reverse takeover.
- [10] Immediately before the transactions in issue JIN Parties held 55.34% of the registered shares in East Crown, and the QIU Parties held 44.66%. In respect of the JIN Parties’ holding, Mr JIN B held 36.74% and JIN X’s (now ex-) wife, Ms WEN Liming, held 18.60%. After Mr JIN B passed away, his shareholding eventually devolved to his widow, Madam MA and Mr JIN X. Mr JIN X also eventually took over his ex-wife’s 18.60%. So, despite these changes the JIN Parties’ 55.34% remained the same. In respect of the QIU Parties, Mr QIU himself held 21.98%, with the remainder of the QIU Parties holding the balance. We will need to consider these facts further.

- [11] The situation with Best Nation was more fluid, and it is that which has given rise to this claim.
- [12] East Crown was initially the holder of a single issued ordinary share in Best Nation. That was at 27 June 2003. Mr JIN B and Mr QIU found an outside investor, which can for convenience be simply referred to as Dragonlink. Two Dragonlink connected entities, Winsummit and PanAsia respectively, would each receive 10,000 ordinary shares in Best Nation. At the same time, Best Nation would issue a further 29,999 shares and transfer these to East Crown, bringing East Crown's holding in Best Nation to 30,000. The effect of that was to give East Crown 60% of the ordinary issued share capital of Best Nation, and Winsummit/PanAsia 40%. This took place between July and December 2004.
- [13] The composition of the Board of Directors of Best Nation is highly relevant to this dispute. Initially, on 27 June 2003, the Board comprised only Mr QIU and Mr JIN X. On 7 September 2004 Mr JIN B replaced Mr JIN X, and three other directors were added. Two of these were Dragonlink nominees. The third, Ms LIN Hui, is one of the QIU Parties. Upon Mr JIN B's passing on 14 July 2009 he clearly ceased to be a director. Best Nation's Register of Directors records that the Dragonlink nominees resigned on 19 September 2010, to be replaced by Mr ZHU Ya Qing (the Second Defendant) and Mr GONG Yuda (the Fourth Defendant). Both Mr ZHU and Mr GONG are QIU Parties. Thus upon Mr JIN B's passing, and following the departure of Dragonlink nominated directors, the Board of Best Nation was entirely controlled by QIU Parties.
- [14] Mr JIN X, however, contends that he was elected as a Director of Bent Nation at a meeting of members and Directors held on 24 July 2009. The QIU Parties say he was not. Whilst a minute of the meeting exists, there is a dispute over whether or not a resolution was passed to appoint Mr JIN X. Counsel for the Defendants argued that it could not be a resolution for a number of reasons. First, to constitute a valid resolution of the members, there would have to be evidence that East Crown, as Best Nation's majority holding member, had voted for it. That was because the minute was not executed by representatives of Winsummit/PanAsia in their capacity as members. Mr JIN X suggested

that he had obtained Mr QIU's oral agreement to the matters resolved at the meeting, thus that he, Mr JIN X, was entitled to sign the minute on behalf of East Crown. There was however no other evidence of such agreement between Mr JIN X and Mr QIU, and Mr QIU denied it. I am not persuaded on a balance of probabilities that Mr QIU had given such oral agreement. He may have done, but I cannot tell whose evidence in this regard is more reliable, and so the balance of probabilities does not tip in Mr JIN X's favour on this point. I am thus not satisfied that this minute constituted a resolution of members. As a potential resolution of directors it suffered from other uncertainties. Mr QIU did not sign that document. He says that he had no notice of the meeting. If he received any notice it is likely to have been oral. There is no evidence of any written notices, and Mr JIN X's evidence was that he had spoken to Mr QIU by telephone. At least three days' notice in writing was required, pursuant to Article 10.1 and 10.4 of the company's Articles of Association. There was also a dispute over the meaning of what the minute recorded. Mr QIU suggested that it was only a draft. That is unlikely, in my respectful view. The minute was signed by the other attendees, which they would have had no reason to do if it was only a draft. Mr QIU gave evidence that those attending the meeting had not been in agreement with each other. He had not attended however, and the translation prepared by the Court Appointed Interpreter showed no doubt about the existence of an agreement. Nonetheless, given the apparent, or at least arguable, defects as a resolution of either the members or of the Board, I consider it is not safe to treat it as a resolution. The result is that contentions by the Claimants that the QIU Party Directors of Best Nation improperly exercised their powers by excluding Mr JIN X in their deliberations fall away.

- [15] On 26 May 2011 Madam MA and Mr JIN X were appointed as the administrators of the estate of the late Mr JIN B and shortly afterwards took over Mr JIN B's shareholding in East Crown. Now able to vote Mr JIN B's shares in East Crown, the JIN Parties caused East Crown to resolve on 6 September 2012 to appoint five additional directors of Best Nation, thereby securing majority control over the Board of Best Nation. That is how it has since remained. By the same resolution the JIN Parties had East Crown change Best Nation's Registered Agent and Registered Office. They then procured that the new Registered Agent produce a new Register of Directors, showing not just these changes but

also Mr JIN X as having been appointed a Director on 24 July 2009. That entry will have to be reversed.

- [16] The JIN Parties contend that Mr QIU and his QIU Parties seized upon the hiatus left by Mr JIN B's passing to obtain a majority and controlling shareholding in ZG. The JIN Parties, through the Claimants, say it happened like this.

The First Series of Transactions

- [17] ZG started its existence as a PRC domestic enterprise. On 30 July 2004 it became a wholly foreign owned enterprise ("WFOE") and a wholly owned subsidiary of Best Nation. On 5 May 2009, that is, a couple of months prior to Mr JIN B's passing, 40% of the shares in ZG were transferred by Best Nation to a company called Xinchang Guobang which can conveniently be referred to as "XG". XG was controlled by the First to Fourth Defendants, i.e. the same QIU Party individuals who the QIU Parties maintain comprised the Board of Best Nation following the passing of Mr JIN B and Dragonlink's exit. Thus ZG was controlled as to 60% by Best Nation and 40% by the QIU Parties through XG.
- [18] At this point (5 May 2009) the QIU Parties also had a 44.66% stake in East Crown, which held a 60% stake in Best Nation. It should also be said that the individual shareholdings were not all directly owned, but that some shareholders were holding shares on behalf of other persons. Mr JIN X, for example, at some point held shares on behalf of Mr JIN B. The registered shareholding did not necessarily reflect the underlying beneficial ownership.
- [19] The parties appear to have given considerable thought to what the equity percentage stake of the various individuals was. The QIU Parties point to a document entitled "Memorandum", dated 8 November 2004. In this, it is recorded, *inter alia*, that Mr JIN B originally had a 52.18% stake in ZG, and Mr QIU 26.08%, and that all the "shareholders appoint [Mr JIN X] and [Mr QIU] to contribute 68.29% and 31.71% in East Crown respectively". Mr JIN X challenges his ostensible signature to that document, but accepts that his father's signature "looks more or less correct". Counsel for the Defendant

submitted that Mr JIN X sought to disavow his signature to that document as it showed that the parties were conducting themselves in accordance with beneficial entitlements, which were different from the registered shareholdings, that Mr JIN X now says should be used as the appropriate ownership percentages.

- [20] The QIU Parties also point to a document dated 22 February 2005 entitled “Confirmation of Equity and Percentage of Shareholding” as evincing the equity position as at that date, and that it shows that the JIN Parties did not have an entrenched majority interest in ZG. That document records that before ZG was changed to a WFOE Mr JIN B held a 52.16% indirect equity stake in ZG, Mr QIU 26.08% and various QIU Parties the balance. It then recorded the introduction of Dragonlink, and a negotiation between “*all the shareholders*”, which resulted in the following “equity” and “shareholding” percentages in ZG: Mr JIN B 33.20%, Mr QIU 13.19%, Dragonlink 40%, and the balance of 13.61% held by various QIU Parties. Under this arrangement the QIU Parties had a 26.8% indirect equity share in ZG. That document was signed by various individuals, including Mr JIN B and Mr QIU. The QIU Parties say this formed the basis upon which the parties dealt with each other. On 19 December 2006 the registered shareholdings in East Crown were changed. This reduced the JIN Parties’ shareholding in East Crown from 68.29% to 55.34%. The QIU Parties say that this reflected with mathematical precision the JIN Parties’ 33.20% indirect equity stake in ZG, and demonstrates that it was never intended that the JIN Parties should have a controlling interest in ZG. Further, as ZG was the operating company, and Best Nation and East Crown were only holding companies, it was a mere accident that the JIN Parties should have a majority 55.34% shareholding in East Crown. The Claimants disagree, because they say the Defendants’ position erroneously equates an indirect interest in underlying assets with a direct interest. The difference, explain the Claimants, is that an indirectly interested party is interested in what happens to an underlying asset, but is not interested in the asset itself. Shareholders of a company have no proprietary interest in the assets of the company¹.

¹ **Macaura v Northern Assurance Co Ltd** [1925] AC 619; **Lonrho Ltd v Shell Petroleum Co Ltd** [1980] 1 WLR 627; **Prest v Petrodel Resources Limited et al.** [2013] UKSC 34

- [21] On 13 February 2004 East Crown, Best Nation and Dragonlink entered into a “Framework Agreement” for investment by Dragonlink of RMB32million. The plan was that Dragonlink would put in capital, and the parties would promote a public listing for the group. Best Nation would issue new shares to Dragonlink and East Crown, to establish East Crown as a 60% shareholder in Best Nation and Dragonlink a 40% shareholder. Dragonlink would pay RMB32 million to acquire those shares. If the group would not be listed publicly within two years, Best Nation and East Crown would repurchase Dragonlink’s 40% shareholding in Best Nation at a price linked to the original purchase price, together with interest.
- [22] This was followed by the Memorandum dated 8 November 2004 mentioned above. Apart from recording equity percentages, it also provided that if public listing were to fail, the original shareholders would return Dragonlink’s capital contribution in a certain ratio.
- [23] Shortly afterwards it was decided that Hangzhou Aida but not ZG would be publicly listed. Hangzhou Aida was hived off into parallel structure.
- [24] On 24 April 2009 Best Nation, East Crown and Dragonlink entered into another “Framework Agreement”. ZG was also a party to this. The purpose of this agreement was to provide for the withdrawal of Dragonlink’s investment. It was agreed that following Dragonlink’s withdrawal Best Nation would hold 60% equity in ZG, XG would hold 40% in ZG and East Crown would revert to being the sole shareholder in Best Nation. The mechanism for Dragonlink’s withdrawal was to be that Best Nation would sell 40% of its 100% shareholding in ZG at a price of RMB32.32 million to a third party (which was to be XG) and then Best Nation would use that money to redeem the 40% of its issued share capital held by Winsummit and PanAsia for Dragonlink. This agreement was signed by both Mr JIN B and Mr Qiu.
- [25] This agreement was partially put into effect. XG, which was owned and/or controlled by all or some of the QIU Parties, duly purchased a 40% stake in ZG from Best Nation on 5 May 2009.

- [26] Some two months later, on 14 July 2009 Mr JIN B passed away. He had been the sole signatory of Best Nation's bank account. No payment was made as planned from Best Nation to Dragonlink.
- [27] A combined meeting of shareholders and directors of Best Nation was convened ten days later on 24 July 2009. There was at least discussion of the situation at that meeting, and also concerning having Mr JIN X appointed as a signatory and a Director. Mr JIN X's evidence is that he would have had to have been appointed as a Director in order to become a signatory to Best Nation's bank account. He maintains he was appointed as a Director. The QIU Parties, who completely controlled the Board of Best Nation upon Mr JIN B's passing, hotly deny it. Mr JIN X also stated in his evidence that he was not appointed as a signatory to the bank account. For some reason Mr JIN X made no effort to establish through correspondence that he should be treated as a Director, nor appointed as the bank account signatory, until he eventually caused Best Nation and East Crown to file this suit. He claims that Mr QIU and the QIU Parties prevented him from becoming a signatory.
- [28] Mr QIU denies this. Rather, he alleges that Mr JIN X had been using this pause to attempt to negotiate an agreement with PanAsia/Winsummit which would see him receive their 40% block of shares. It is the case that on 30 November 2009 Dragonlink through its connected company Pan Asia entered into a framework agreement with Mr JIN X. The latter gave evidence that PanAsia had prepared this document and, although it did not specify on whose behalf Mr JIN X entered into this agreement, it had been Best Nation. It is not clear in what capacity Mr JIN X entered into that agreement, although he asserted in his oral evidence that he controlled Best Nation at that point. In that agreement it is recorded that the parties undertook to execute with integrity and good faith the Dragonlink exit framework agreement of 24 April 2009, together with minutes of the Best Nation members' and Directors' meeting on 24 July 2009. It further provided that Dragonlink would transfer its 40% stake in Best Nation to an "assignee" represented by Mr JIN X, with the "assignee" then paying Dragonlink a total of Hong Kong \$36,650,000. The Defendants point out that it was rather odd that the agreement should be expressed as being with Mr

JIN X personally, and not Best Nation, and that it referred to transfer of the shares to an “assignee”, and not Best Nation, because elsewhere in the document Best Nation was referred to precisely. I do not need to make any findings whether this is likely to have been what Mr JIN X had been doing.

- [29] The Dragonlink exit however did not happen this way. On 11 June 2010 PanAsia and Winsummit entered into an equity transfer agreement with a company called Tore Biotechnology Co. Ltd. (“Tore”). This provided for the sale of Dragonlink’s 40% stake in Best Nation to Tore for RMB32.32million. Mr JIN X’s evidence is that Tore is owned by a close associate of Mr QIU, Mr GE. Neither Tore, nor its legal owners, are parties to these proceedings. Mr QIU did not deny association with Mr GE, but sought, rather unconvincingly, to portray Tore as independent of Mr QIU’s influence.
- [30] Two days later, on 13 June 2010, the QIU Parties agreed to form the Fifth Defendant (“Antow”) to purchase the former Dragonlink 40% stake in Best Nation. This is hardly a coincidence and is strongly suggestive of collusion between Mr QIU and Mr GE. On 28 June 2010 Tore and Antow entered into an equity transfer agreement. This provided that Tore would transfer the 40% stake in Best Nation to Antow for a consideration of RMB32.32million. Mr JIN X considers that Mr QIU had been stalling on having Best Nation pay off PanAsia/Winsummit, to enable Mr QIU to try to get that 40% block of shares for himself, through Antow. Whether or not Mr QIU had been stalling is not immediately relevant. What is relevant is that Antow, controlled by Mr QIU, obtained that shareholding.
- [31] As a result, the structure of group became as follows. ZG was formally owned as to 40% by XG and 60% by Best Nation. Best Nation was owned as to 60% by East Crown and 40% by Antow. The shareholdings in East Crown had not changed, although Mr JIN B had already passed away. His estate would remain unrepresented until his widow, Madam MA, and Mr JIN X received letters of administration on 1 April 2011 (subsequently amended on 26 May 2011).

- [32] On 28 April 2011 the QIU Party directors of Best Nation, that is, Mr QIU, Mr GONG Yuda, Mr ZHU Yaqing and Ms LIN Hui, produced a Board resolution. This recorded that as at that date Best Nation's assets comprised only of its 60% shareholding in ZG and Hong Kong \$36,720,964.38 and that it did not have any other assets and liabilities. Further, that with the passing away of Mr JIN B, described as the leader and Executive Director of Best Nation, the initial purpose of the cooperation of the shareholders of Best Nation could not be achieved. It recorded that pursuant to a request of Antow, it was unanimously agreed that the 40% shareholding in Best Nation held by Antow would be "withdrawn", in exchange for a payment of Hong Kong \$14,688,385.75, being 40% of Best Nation's cash, and that after these changes Best Nation would become the wholly owned subsidiary of East Crown. There was also to be a transfer of 24% of Best Nation's shareholding in ZG to Antow. Mr GONG Yuda was elected as the new Executive Director of Best Nation.
- [33] Mr JIN X, through the Claimants, submits that the logic behind this arrangement seems to have been that because Antow held 40% of Best Nation, and Best Nation held 60% of ZG, 24% (being 40% x 60%) of Best Nation's shares in ZG should be transferred to Antow, together with 40% of Best Nation's cash.
- [34] Mr JIN X, through the Claimants, impugns this resolution on a number of grounds. They remark that the resolution does not show that any discussion concerning the best interests of Best Nation took place, and there was no declaration of interest by any of the Directors. The latter contravened section 124 of the Business Companies Act, 2004, as amended, asserts Mr JIN X through the Claimants, rendering the transaction voidable at the instance of the company pursuant to section 125.
- [35] Mr JIN X alleges that those Directors of Best Nation were also the underlying beneficial owners of Antow. Consequently, contends Mr JIN X, there was a clear conflict of interest. Such conflict of interest breached the directors' duty of honesty and good faith under section 120(1) of the Business Companies Act, 2004, as amended, and the proper purpose duty under section 121. It also infringed the statutory duty of care of directors imposed by section 122.

- [36] Mr JIN X, through the Claimant, further alleges that this resolution contravened the company's Articles of Association, Regulation 9.2, which provided that each director should act honestly and in good faith in what the director believes to be the best interests of the company.
- [37] Mr JIN X points out also that the resolution should have, but did not, contain a statement that in the opinion of the directors, the company would, immediately after the distribution envisaged, satisfy the solvency test, pursuant to section 57(2) of the Business Companies Act 2004, as amended, and Regulation 3.2 of the Articles of Association. As will be seen, the Claimants point out similar defects in subsequent resolutions. However, the resolutions did mention, when it materially mattered, that the company had sufficient assets and no liabilities so as to be able to make the transfers envisaged. That was broadly to the same effect as a declaration of solvency, although not all the rubrics of solvency would be covered thereby. I need not decide whether those statements were sufficient, as the claim turns on other principles.
- [38] In sum, Mr JIN X, through the Claimants, contends that the resolution was wrongful. He says the reason it was done was that QIU Parties had fallen out with Mr JIN X and wanted to gain control.
- [39] This resolution was implemented. The first step in doing so was for the same Directors of Best Nation to pass a written resolution, on 10 May 2011, to redeem Antow's shareholding in Best Nation, at their par value of US\$1 per share. The resolution described this as "their fair value".
- [40] Mr JIN X says that this resolution suffered from the same defects of lack of any declaration of interest or solvency. He further claims this resolution was mendacious, in that Antow was getting approximately Hong Kong \$14million in exchange for its shares, and not US\$20,000.

- [41] The next step undertaken was for Best Nation, by Mr GONG Yuda, to enter into a shareholding transfer agreement with Antow, by Mr ZHU Mingxing, on 17 June 2011. This records that Best Nation would transfer 24% of its shareholding in ZG to Antow at a consideration of RMB33,312,000. Mr JIN X says that this consideration was fictitious, as Antow paid no money for this shareholding in ZG. The only benefit Best Nation received was redemption of 40% of its issued share capital from Antow.
- [42] Mr JIN X submits that the effect of this series of transactions, as a whole, was to reduce Best Nation's shareholding in ZG from 60% to 36%, thereby losing its valuable majority shareholding in ZG and, with Antow now directly holding 24% of the shares in ZG, and XG already holding 40% of the shares in ZG, the QIU Parties now held a total of 64% of the shares in ZG. Mr JIN X contends this was contrary to the Framework Agreement dated 24 April 2009, under which the shares in ZG would be held by Best Nation as to 60% and XG as to 40%. At the same time, the issued share capital of Best Nation was reduced from US\$50,000 to US\$30,000. Another result was that East Crown was returned to being the 100% shareholder of Best Nation.
- [43] Mr JIN X, through the Claimants, alleges that this series of transactions had no commercial benefit to Best Nation and, on the contrary, was seriously detrimental to its interests. Specifically, it says its shareholding in ZG was reduced from 60% to 36% and the purported consideration was not paid, and in any event expressed at an under value. Also, Best Nation's cash was depleted by approximately Hong Kong \$14.7million, to Antow's benefit.
- [44] The Defendants contend, however, that the Claimants' arguments are misplaced. First, the exchanges conducted were balance sheet neutral for Best Nation. Secondly Antow was not party to the Framework Agreement dated 24 April 2009, thus not bound by it. Thirdly, the object of the Framework Agreement dated 24 April 2009 was achieved in that East Crown was returned by being the 100% shareholder of Best Nation.

- [45] Around the same time, on 1 April 2011, Madam MA and Mr JIN X were appointed as administrators of the estate of Mr JIN B in the TVI. On 16 July 2011 this Court, by Bannister J, ordered that Mr JIN X and Madam MA be registered as holders of Mr JIN B's share in East Crown. This was effected on 19 July 2011. Mr JIN X claims that Mr QIU knew this was happening, and when he had been asked if he consented to the registration, Mr QIU prevaricated and postulated that pre-emption rights might apply. Mr QIU on the other hand claimed not to have opposed such registration at all.
- [46] Two days later, on 21 July 2011, using their newly acquired majority voting power, Mr JIN X, Madam Ma and Mr JIN X's ex-wife Ms WEN Liming, together holding 55.34% of the issued share capital of East Crown, passed an ordinary resolution appointing Madam MA as a Director of East Crown, and changed the registered agent.
- [47] As a result, the Board of East Crown now comprised Mr JIN X, Madam MA and Mr QIU.

The Second Series of Transactions

- [48] On 15 March 2012 Best Nation, acting by Mr GONG Yuda, Antow and a group of eight individuals headed by Mr QIU ("the Group of Eight") entered into what they referred to as a "Shareholder Restructuring Agreement". The Group of Eight was described in the preamble to the agreement as the legally registered shareholders of East Crown. They did not there include Ms WEN, Madam MA or Mr JIN X, but in another part recognized that they held a 55.34% stake, whereas the Group of Eight together held 44.66%. East Crown was not a party to this agreement. Nor were Mr JIN X, Madam MA and Ms WEN.
- [49] In this agreement, Best Nation purportedly agreed to transfer 13,398 shares out of its remaining 30,000 issued shares, and what was referred to as its corresponding 16.078% shareholding in ZG, to Antow, together with a cash sum of Hong Kong \$907,749.62.
- [50] It should be recalled that as at 15 March 2012 East Crown owned 100% of the remaining issued share capital of Best Nation. Mr JIN X, through the Claimants, accuses the QIU

Parties of theft, as it was not within Best Nation's power to take shares away from East Crown and transfer them to another. Mr JIN X similarly alleges that the notion of indirect ownership (whereby the QIU Parties were treating the 13,398 shares in Best Nation as representing a 16.078% stake in ZG) is a concept not recognized in law.

- [51] The agreement then relates that by way of consideration payable by Antow to Best Nation for the transfer (by whom is unstated) of the 13,398 shares to Antow, the Group of Eight agreed to "give up" their respective shares in East Crown. As the document recited: "*i.e. the redemption by the East Crown of [the Group of Eight's] shares therein shall be proceeded at nil consideration, so as to set off against the consideration for the transfer payable by [Antow] to [Best Nation]*".
- [52] The document then recited that the situation of the shareholders after completing the agreement would be as follows. The JIN Parties would own all the issued shares in East Crown, which would own 100% of the shares in Best Nation, "*fully hold the 19.922% shareholding in [ZG]*" and "*fully hold*" the remaining cash in Best Nation of Hong Kong \$12,192,829.01. It concluded that "*[t]herefore, the shareholders' interests of WEN Liming and the late JIN Biao (MA Guomei and JIN X as the administrators of his estate) before and after the restructure would be the same*".
- [53] This agreement was followed by a confirmation of the Group of Eight that they unanimously agreed to exchange their shares in East Crown, with East Crown redeeming them. Neither East Crown nor the JIN Parties executed this document. Mr JIN X, through the Claimants, says this document creates a pretence of formality, in furtherance of the QIU Parties' fraud.
- [54] This agreement was also followed, on 16 March 2012, by a resolution passed by the QIU Party Directors of Best Nation unanimously approving this second series of transactions.
- [55] The reason for the transaction was stated nebulously as "*According to International Acts Series and the need of operation and development of [Best Nation], this Company*

convened a board meeting on 16/3/2012 in Hangzhou, at which all the resolutions were approved unanimously by the board of directors,...”.

- [56] Mr JIN X, through the Claimants, argues that Best Nation is unable to implement such resolutions as it is legally impossible for Best Nation to take shares away from East Crown and give them to Antow. As with the earlier resolutions, Mr JIN X, through the Claimants, observes that this resolution contained no declaration of interests, no record of any consideration of the best interests of Best Nation, and no declaration of solvency after the intended redemption.
- [57] The same directors passed a resolution of Best Nation on 16 March 2012 purporting to cancel the share certificate for East Crown’s shareholding in Best Nation. This resolution purported to annex a copy of an instrument of transfer dated 16 March 2012, wherein East Crown transferred to Antow those 13,398 shares, for a stated consideration of \$13,398. This instrument was signed on behalf of East Crown by Mr QIU. Mr JIN X contends that Mr QIU had no authority to sign such an instrument on behalf of East Crown, as East Crown had no executive directors, and Mr QIU was not the sole director, and the Board of East Crown had not authorized Mr QIU to do so. Mr JIN X gave evidence that he was not informed of these transactions by Mr QIU, and only discovered them later, in 2012. Mr QIU gave evidence that the Directors had sought advice from lawyers in the People’s Republic of China, and they had interpreted TVI law as permitting a transfer by Best Nation of its own issued shares, and for him as a Director of East Crown to authorize such a transfer without the agreement of the other Directors. Mr QIU claimed that he had not been able to reach Mr JIN X to obtain his agreement, the transaction had to be done, and so he signed off on them as something had to be done to progress the transaction. The Claimants, through their Counsel, submitted that this was not true, and that Mr QIU had tried to steal a march on Mr JIN X by deliberately not informing the JIN Parties of what he was machinating.
- [58] The envisaged transaction proceeded in accordance with the QIU Parties’ intentions.

- [59] The effect of this was to constitute Antow as a 44.56% shareholder in Best Nation, and East Crown a 55.34% shareholder in Best Nation.
- [60] On 20 March 2012 the QIU Party Directors of Best Nation resolved to redeem the 13,398 shares held by Antow at par value of US\$13,398, described as being their fair value. Mr JIN X observes that again this resolution contained none of the requisite declarations. He also points out that the consideration stated was not true – it had been Best Nation's 16.078% stake in ZG together with Hong Kong \$907,749.62.
- [61] On 31 March 2012 Best Nation by Mr GONG Yuda entered into a shareholding transfer agreement with Antow for transfer of 16.078% of Best Nation's shareholding in ZG to Antow for a consideration of RMB22,316, 264. Mr JIN X, through the Claimants, says that this transfer was a sham, in that no money would pass by way of consideration for the transfer. Instead, it had been intended that the purported redemption of the Group of Eight's shares in East Crown would justify the transfer by East Crown to Antow of the 13,398 shares in Best Nation, and that the purported redemption of those shares by Best Nation would in turn justify the transfer of the 16.078% shareholding in ZG by Best Nation to Antow.
- [62] The end result was that Best Nation's shareholding in ZG was reduced from 36% to 19.922%, and Antow became a 40.078% shareholder in ZG. As the remaining shares in ZG were held as to 40% by XG, this gave the QIU Parties an 80.078 stake in ZG. The Defendants remark that immediately before the first transfer on 23 June 2011 the JIN Parties' indirect interest in ZG was 19.99% ($55.54\% \times 60\% \times 60\%$), and immediately after the second transfer on 10 April 2012 it was 19.922%, thus, overall, the net effect of the two transfers was to maintain the JIN Parties' indirect interest in ZG almost exactly. The JIN Parties thus have no good grounds for complaint, say the Defendants.
- [63] On 24 July 2014 Mr JIN X, Madam MA and Ms WEN, as shareholders holding a majority of shares in East Crown, passed a resolution of East Crown condemning Mr QIU's acts in relation to the second set of impugned transactions and resolving to authorize

commencement of legal proceedings to have them set aside or annulled and to seek compensation and/or damages and/or other relief.

- [64] On 8 December 2014 Mr JIN X became the registered holder of 1860 shares in East Crown previously held by Ms WEN.
- [65] Mr QIU gave evidence at trial that what had motivated the Directors of Best Nation in making the transfers was that Mr JIN X was a disruptive influence over the smooth management of ZG. ZG was a company with some one thousand three hundred employees. Mr JIN X's inconsistency created a climate of fear and uncertainty. In order to re-assure, incentivize and reward the management and staff of ZG the QIU Parties therefore decided to restructure the group so that the indirect interests would be converted into direct interests. One of the purposes, but not the only purpose, was to give shareholder control over ZG to ZG's management, to further the purpose of establishing a more stable and rewarding environment. Mr QIU accepted that one of the consequences was to remove the power to control ZG of the JIN Parties' stake in East Crown and give it to Mr QIU and his associates. The overall purpose was proper, however, and it worked, because ZG's business has improved considerably, benefiting all the shareholders.

Discussion

- [66] I will concentrate here on those issues which are determinative of this matter in my view.

The First Series of Transactions

- [67] Section 120(1) of the Business Companies Act, 2004, as amended, provides:

"120. (1) Subject to this section, a director of a company, in exercising his powers or performing his duties, shall act honestly and in good faith and in what the director believes to be in the best interests of the company."

Section 121 provides:

"121. A director shall exercise his powers as a director for a proper purpose and shall not act, or agree to the company acting, in a manner that contravenes this Act or the memorandum or articles of the company."

The Articles of Association of the Claimant companies reflect these statutory provisions.

- [68] Both sides accept that the “interests of the company” referred to in section 120, and within the wider scheme of that section, include all a company’s shareholders, as well as the shareholders of its parent.
- [69] The requirements of sections 120 and 121 reflect separate concepts, but both constitute fiduciary duties of directors².
- [70] In considering whether there has been an abuse of powers by directors, it is well settled that *“the state of mind of those who acted, and the motive on which they acted are all important, and you may go into the question of what their intention was, collecting from the surrounding circumstances all the materials which genuinely throw light upon that question of the state of mind of the directors so as to show whether they were honestly acting in discharge of their powers in the interests of the company or were acting from some bye-motive, possibly of personal advantage, or for any other reason”*³.
- [71] This principle applies in particular when the issue is whether directors have exercised their powers for a proper purpose.
- [72] The question whether directors have acted honestly and in good faith and in what they believe to be in the best interests of the company involves a slightly different enquiry. There is a subjective element to this duty – to have acted honestly and in good faith and in

² **Howard Smith Ltd. v Ampol Petroleum Ltd.** [1974] AC 821 (PC)

³ **Hindle v John Cotton Ltd.** (1919) 56 ScLR 625, 630 – 631, per Viscount Finlay, as quoted in **Howard Smith Ltd. v Ampol Petroleum Ltd.**, *supra*

a belief that their acts are in the best interests of the company. There is also an objective element – the best interests of the company. The test to be applied was summarized by Pennycuick J in **Charterbridge Corporation Ltd v Lloyds Bank Ltd**⁴:

“...whether an intelligent and honest man in the position of a director of the company concerned, could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company.”

- [73] Counsel for the Claimants submitted that it was impossible to construe a reduction of Best Nation's shareholding in ZG from a controlling 60% shareholding to a 36% minority shareholding, with, further, a substantive payment of cash, as in the best interests of Best Nation. Control, he submitted, has value. With control, there would be prospects of being able to raise finance to leverage the underlying business. Without control, raising capital would be so much harder. Also, ZG would have to do very well indeed to give Best Nation the same income return with 36% as it had with 60%. So, in respect of the objective element, Counsel for the Claimants submits that the acts of the first four Defendants fail the test in section 120(1).
- [74] He submits that those defendants also fail the subjective test, in that they had given no regard to the best interests of Best Nation at all. They had only had regard to their own interests in creating a majority for the QIU Parties in ZG. They had not considered the interests of all the shareholders of Best Nation, just those of their own QIU Party block. They had done so by subterfuge, to steal a march on the JIN Parties without involving them whilst they had temporarily been deprived of a position on Best Nation's Board upon Mr JIN B's passing away, and therefore through dishonesty and bad faith.
- [75] When Mr QIU explained the Directors' motives and purpose he spoke only of the positive effects he sought to bring about in relation to ZG. That is understandable, as ZG is the operating company which generates the value. It would be erroneous to treat Best Nation as “only” a holding company. It is a corporate entity entitled to receive the income of its

⁴ [1970] 1 Ch 62 at 74

shareholding in ZG. Mr QIU did not mention Best Nation at all. It is clear that his goal was to gain control of ZG. It is clear to me that he and the other QIU Party Defendants did not have any regard to the best, nor indeed any, interests of Best Nation.

- [76] The flaw in the QIU Parties' position is that their motive was to further their own interests. That was their real purpose.
- [77] Having considered all the evidence I accept Counsel for the Claimants' submissions that the first four Defendants were in breach of section 120(1) with regard to the first series of transactions.
- [78] As the first four Defendants' motive behind the first series of transactions was the personal advantage of gaining control over ZG, they also fail the proper purpose test, and are thus in breach of section 121.
- [79] The first series of transactions should therefore be set aside.
- [80] As Mr QIU was the sole director of Antow, Antow was fixed with knowledge of the first four Defendants' improper motives and acts. Consequently Antow, as the Fifth Defendant, cannot retain the shareholding it gained in ZG and the cash it received from Best Nation.

The Second Series of Transactions

- [81] The second series of transactions was also flawed. The same factors vitiating the first series of transactions also apply. However there is a more fundamental flaw. Mr QIU had no authority to sign the instrument of transfer dated 16 March 2012, wherein East Crown purportedly transferred 13,398 shares in Best Nation to Antow. I cannot agree that his doing so should be excused on grounds that he could not obtain Mr JIN X's agreement and that the transaction had to be done. There was no compulsion to do that transaction, other than the wishes of the QIU Parties. It does not help Mr QIU to point to a decision of the QIU Party Directors of Best Nation to enter into such a transaction, as Best Nation had

no power of disposal over the issued share capital which was held by East Crown. It is also no reason for upholding the transaction to say that its net effect was to restore the JIN Parties as an almost 20% shareholder of ZG. Without the requisite authority in Mr QIU to sign an instrument of transfer on the part of East Crown the transaction must fail and be set aside.

- [82] He however submitted that the Claimants would need to show some independent ground for reversing the last part of that series of transactions, namely the delivery by Antow of the shares in Best Nation back to Best Nation in exchange for a further tranche of shares in ZG and cash. Counsel for the Claimants disagrees. He submitted that the pillar of the whole transaction had been the initial, unauthorized, transfer of the 13,398 shares from East Crown to Antow. If that pillar goes, the whole transaction falls. I agree. Had Antow delivered those shares back to East Crown, and not Best Nation, then I can see the Defendants might have a point. But that is not how the transaction worked. Best Nation ended up redeeming its own share capital, at the instigation of the first four Defendants and with the knowledge of Antow, in circumstances where it should have stayed with East Crown. Had it stayed with East Crown, there would have been no exchange by which a further tranche of shares in ZG was transferred from Best Nation to Antow, and no reduction in share capital to free up cash for payment to Antow, and no need to pay any cash at all to Antow. The entire transaction must therefore be reversed.
- [83] The Claimants have additionally sought compensation. They have produced no evidence of any loss if the transactions are reversed and the monies repaid. No order for additional compensation is appropriate therefore.
- [84] The Defendants raised a defence of *res iudicata*. I have delivered a separate reasoned oral ruling on that issue, which the Defendants also pressed as a free-standing application. For the reasons given there I find that there was no res iudicata, and therefore this defence fails.
- [85] The Order upon Judgment will therefore be as follows.

In respect of the First Series of Transactions:

1. The resolution dated 28 April 2011 of the Board of Directors of the First Claimant (Best Nation) is hereby set aside.
2. The redemption by the First Claimant (Best Nation) of 40% of its issued share capital from the Fifth Defendant (Antow) pursuant to the resolution dated 28 April 2011 and 10 May 2011 of the Board of Directors of Best Nation is hereby set aside, and the Register of Members of the First Claimant shall be amended accordingly.
3. The transfer of 24% of the First Claimant's shareholding in ZG to the Fifth Defendant pursuant to the resolution dated 28 April 2011 of the Board of Directors of Best Nation and/or the share transfer agreement dated 17 June 2011 is hereby set aside.
4. The Fifth Defendant shall procure re-transfer to the First Claimant of the said 24% percentage shareholding in ZG at nil consideration free from encumbrances at the Fifth Defendant's cost. The Fifth Defendant shall do all things within its power that the First Claimant may require for the First Claimant to re-constituted as the lawful holder of the said percentage shareholding.
5. Should such re-transfer ordered in the preceding paragraph be impossible in whole or part, the Defendants shall pay the First Claimant damages and/or equitable compensation in lieu, to be assessed. The burden of proving such impossibility shall be on the Fifth Defendant.
6. The Fifth Defendant shall repay to the First Claimant the sum of Hong Kong \$14,688,385.75.

In respect of the Second Series of Transactions:

7. The resolutions dated 16 March 2012 of the Board of Directors of the First Claimant approving of and resolving to implement transfer of 13,398 shares in the issued share capital of the First Claimant from the Second Claimant (East Crown) to the Fifth Defendant are hereby set aside.
8. The purported Instrument of Transfer of the said shares executed on behalf of the Second Claimant by the First Defendant in favour of the Fifth Defendant on 16 March 2012 is hereby declared to be invalid for want of authority and is hereby set aside.
9. The redemption by the First Claimant of 13,398 of its issued share capital from the Fifth Defendant pursuant to the resolution dated 20 March 2012 of the Board of Directors of the First Claimant is hereby set aside.
10. The First Claimant shall rectify its Register of Members to restore the Second Claimant as the registered shareholder of the said 13,398 shares.
11. The shareholding transfer agreement dated 31 March 2012 between the First Claimant and the Fifth Defendant for transfer of 16.078% of the First Claimant's shareholding in ZG to the Fifth Defendant is hereby set aside.
12. The Fifth Defendant shall procure re-transfer to the First Claimant of the said 16.078% of the First Claimant's shareholding in ZG at nil consideration free from encumbrances at the Fifth Defendant's cost.
13. Should such re-transfer ordered in the preceding paragraph be impossible in whole or part, the Defendants shall pay the First Claimant damages and/or equitable compensation in lieu, to be assessed. The burden of proving such impossibility shall be on the Fifth Defendant.
14. The Fifth Defendant shall repay to the First Claimant the sum of Hong Kong \$907,749.62.

15. To the extent that the Second Claimant redeemed the shares in its issued share capital of the Group of Eight referred to earlier in this Judgment the Second Claimant shall restore such shareholdings and amend its Register of Members accordingly.
16. It is declared that the 24% shareholding in ZG and the 16.078% shareholding in ZG and the sums of Hong Kong \$14,688,385.75 and Hong Kong \$907,749.62 have been and are held upon constructive trust by the Fifth Defendant for the First Claimant.
17. Without prejudice to the foregoing the Register of Members of the First Claimant shall be rectified to the effect that out of a total of 50,000 ordinary shares in the issued share capital of the First Claimant
 - a. 30,000 shares shall be registered in the name of the Second Claimant;
 - b. The remaining 20,000 shares shall be registered in the name of the Fifth Defendantat all times as from 10 May 2011.
18. The entry in the First Claimant's Register of Directors showing Mr JIN X as having been appointed a Director on 24 July 2009 shall be reversed.
19. The Defendants shall jointly and severally pay the costs of these proceedings to the Claimants, to be assessed if not agreed within 60 days.
20. All other claims stand dismissed.

[86] I thank Mr QIU and Mr JIN for having made the long journey to attend the trial in person, together with their PRC legal teams. I also thank Learned Counsel for their assistance. Lastly, but certainly not least, I thank and commend the Interpreter, Ms Lori Chen, for her indefatigable efficiency and professionalism throughout the trial.



Commercial Court Judge

28 March 2017