

Article

BVI shareholders disputes in the context of a feuding family

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The recent decision of the Judicial Committee of the Privy Council in *Kathryn Ma Wai Fong v Wong Kie Yik and Ors* (British Virgin Islands) illustrates the challenges that family owned businesses can face and offers lessons on ways in which family members can structure their affairs to prevent and minimise the effects of disagreements between them on a company's activities. The case involved an all too typical situation where a family owned business was suffering because in the judge's words "*two sides of the family are not getting along*".

The Judicial Committee of the Privy Council ordered one side of the family to buy the other side of the family's shares in the family business at a price to be determined by the court as it was "*highly unlikely that the two sides of the family would be able to work together*". The court concluded that it would be unfair for it to insist on them cooperating in running the business.

Unfortunately, cases in which family companies are subjected to unfair prejudice or winding-up petitions brought by feuding family members against other members of the family are not uncommon. In this article, we will summarise the key takeaways from the Privy Council decision in *Kathryn Ma* and explore ways to prevent and minimise the effects of disagreements between family members on a company's activities.

Brief background to the *Kathryn Ma* case

The appellant, Ms. Kathryn Ma, brought proceedings as the executrix and trustee of the estate of her late husband against his two brothers. Ms. Ma challenged the entitlement of the respondents to exercise their contractual right to convert a block of convertible preference shares in the family company. By exercising this right, the two respondents as majority shareholders would acquire effective voting control over a group of companies (the "**Conversion**").

Ms. Ma claimed, relying on equitable principles, that there should be a unanimous vote of all the shareholders in favour of the Conversion. It was therefore unfairly prejudicial for the two respondents to proceed with the Conversion when Ms. Ma opposed it. The judge at first instance did not agree with Ms. Ma and dismissed all aspects of her claim.

Ms. Ma appealed relying on two main grounds.

Was there a quasi-partnership between the family members?

Ms. Ma argued that the family business had been operated as a quasi-partnership between the shareholders founded on mutual trust and confidence. She claimed that this quasi-partnership gave rise to equitable constraints which meant that the majority should not instigate the Conversion without her consent even though they otherwise had a contractual right to do so. By ignoring her opposition to the Conversion, she claimed there had been an irretrievable breakdown of trust and confidence between the family members justifying the grant of unfair prejudice relief.

The Privy Council rejected Ms. Ma's argument. It emphasised that the mere fact that a company is a family business is not enough of itself to establish that all family shareholders can expect to be involved in the management. Even if there were such an expectation, there would be no presumption that such an expectation would pass to an heir. There would need to be clear evidence of an understanding that a family member's spouse, child, or other representative would step into the shoes of the deceased so as to become entitled to be involved in their stead.

Did the respondents breach their fiduciary duties as *de facto* directors?

Ms. Ma also alleged that the Conversion was instigated by the two respondents in their capacity as *de facto* directors of the family business. She claimed they breached their fiduciary duties, because the Conversion was carried out for an improper purpose. The Privy Council found that the respondents were acting as *de facto* directors but that they had not breached their duties. The family business genuinely required financing and the Conversion was the best way to achieve it.

How can this sort of unhappy saga be avoided?

1. Do not assume that family relationships and understandings will override contractual and company law requirements if there is a falling out between family members.
2. Do not assume that your heirs will naturally stand in your shoes and enjoy your rights and expectations as a member of a family company.
3. Although you may have thought that you and your family members have always operated the family company as if it were a partnership, do not assume that the court will necessarily see it the same way.
4. If you wish to ensure that you and your heirs will be fully involved in the management of the family business, consider putting in place a shareholders' agreement. It can be comprehensive or short depending on what you think is necessary to set out ground rules for your day-to-day relationships and to avoid misunderstandings and conflict.
5. A well drafted shareholders' agreement should serve as a practical guide to what should happen in various situations. Amongst other matters it can cover:
 - How shares can be transferred;
 - Whether they may not be transferred to certain parties;
 - How to resolve disputes from minor issues to matters which affect the commercial justification for continuing in business. Different methods can be specified depending on the seriousness of the dispute, for example, a mediator may be appointed to facilitate a settlement;
 - The voting requirements to approve different categories of business. The most significant matters may require a vote of all shareholders in favour of a resolution.
6. Directors should pay proper regard to their fiduciary duties.

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