

# THE CONVOY SAGA CONTINUES: CHAIRMAN'S WIDE POWER TO EXCLUDE VOTES IN A GENERAL MEETING CONFIRMED

The Hong Kong Court of Appeal (CA) and Court of First Instance (CFI) have recently handed down decisions confirming the wide power of a chairman in a general meeting to disallow a member's votes. In the CA decision<sup>1</sup>, the CA upheld the Companies Judge's decision that under the articles of Convoy Global Holdings Limited (**Convoy Global**), the Chairman's decision to exclude votes in a general meeting cannot be set aside by a Court other than for bad faith. In the CFI decision<sup>2</sup>, Coleman J dismissed the applicant member's application for an injunction to pre-emptively restrain Convoy Global from excluding the applicant's votes in an upcoming extraordinary general meeting (EGM).

It is not uncommon for the articles of association of listed companies in Hong Kong to provide for the power of the chairman of a general meeting to rule on a substantive objection to a registered member's voting right and make a final and conclusive decision to disallow his votes. The decisions provide helpful guidance to both individuals who are in the position of a chairman and also members who may be concerned about their rights.

## Background

Convoy Global is a Cayman Islands company, which shares are listed on the Main Board of the Hong Kong Stock Exchange<sup>3</sup>.

In May 2017, stock market activist David Webb published a blog post about the 'Enigma Network', which was a group of 50 Hong Kong listed companies including Convoy Global with significant overlapping ownership. It was alleged that these companies and their associated parties had acted in collusion to the detriment of other shareholders and the investing public.<sup>4</sup> In the following

month, the Securities and Futures Commission (SFC) conducted a raid on the offices of Convoy Global.

On 7 December 2017, trading of Convoy Global's shares was suspended.<sup>5</sup> The company announced on the next day that three of its executive directors (including its then Chairman) were arrested by the Independent Commission against Corruption. The current Chairman (the **Chairman**) Johnny Chen (**CHEN**) was appointed on 9 December 2017.

On 18 December 2017, Convoy Global and two other group companies commenced a claim against 41 defendants including Kwok Hiu Kwan (**KWOK**) that certain shares allotted in October 2015 were void or voidable (**Main Action**).<sup>6</sup>

It was alleged that over several years up to 2017, Roy Cho (**CHO**), who was a director of Convoy Global from March to August 2017, had wrongfully and illicitly acquired and maintained secret ownership in and control over Convoy Global via his associates. The allegation concerning **KWOK** was that, after the Enigma Network was exposed, in a scheme to whitewash the tainted origins of those shares concerned and allow **CHO** to cash out of his interests in Convoy Global, **KWOK** acquired an aggregate of 29.91% of the company shares from **CHO**'s associates, nominees, and/or agents by matching buy and sell orders in the open market in 2017. These shares that **KWOK** acquired were connected to the share allotment in 2015 which Convoy Global is challenging.

**CHO** was later indicted for conspiracy to defraud Convoy Global and publishing false statements in Convoy Global's

<sup>1</sup> Kwok Hiu Kwan v Johnny Chen and Others [2020] HKCA 972.

<sup>2</sup> Kwok Hiu Kwan and Convoy Global Holdings Limited [2020] HKCFI 2874.

<sup>3</sup> Its shares are currently suspended from trading.

<sup>4</sup> See the blog post by David Webb on 15 May 2017 [here](#).

<sup>5</sup> On 5 June 2020 the Listing Committee of the Stock Exchange announced its decision to delist Convoy Global's shares, which decision is currently subject to appeal before the Listing Review Committee.

<sup>6</sup> Convoy Global Holdings Ltd and Others v Cho Kwai Chee Roy and Others [2018] HKCFI 2111.

2016 annual report. He was recently acquitted on both counts on 30 November 2020<sup>7</sup>.

### Legal battle concerning KWOK's voting rights

As a registered owner of 29.91% shares in Convoy Global, KWOK has attempted to remove the incumbent board of directors including CHEN. In October 2017, he requisitioned an EGM (2017 EGM), which took place on 29 December 2017.

Shortly before the 2017 EGM, an individual shareholder issued an unfair prejudice petition at the High Court of Hong Kong repeating the allegations made by Convoy Global in the Main Action and seeking a declaration that KWOK and another shareholder be disallowed to vote their shares.

The 2017 EGM was chaired by CHEN, who came on board not too long ago. A member present at the meeting raised an objection that KWOK's shares were problematic as he might not own the voting rights. KWOK's lawyer who was also present, however, maintained that the controversy surrounding KWOK's shares should be left to the court to resolve. CHEN eventually decided to exclude KWOK's votes for the purposes of the resolutions proposed at the 2017 EGM by invoking article 74 of the articles of association of Convoy Global (the **Chairman's Decision**). Article 74 provided that:

*'If...any objection shall be raised to the qualification of any voter....Any objection...shall be referred to the chairman of the meeting and shall only vitiate the decision of the meeting on any resolution if the chairman decides that the same may have affected the decision of the meeting. The decision of the chairman on such matters shall be final and conclusive' (Article 74).*

As a result of the Chairman's Decision, KWOK's votes were not counted for the purpose of the resolutions to remove the incumbent board. The resolutions were not passed.

KWOK subsequently challenged that the Chairman's Decision was unlawful, void and/or of no legal effect. In the legal action commenced by him against Convoy Global and CHEN (2018 Action), KWOK sought, *inter alia*, a declaration that his resolutions to remove the incumbent board were duly passed. The 2018 Action was heard in two parts, and involved the Honourable Mr Justice Harris answering the following questions:

- (1) Did the Chairman (CHEN) have the power under Article 74 to determine the objection to KWOK's votes being counted?
- (2) If so, was the determination final and conclusive?
- (3) Was the Chairman's Decision challengeable on the ground that the decision was one which no reasonable chairman, properly directing himself as to his duties could have reached?
- (4) If the Chairman's Decision was only challengeable on the ground that it was made in bad faith, was bad faith established in this case?

Harris J decided against KWOK. The 2018 Action was dismissed<sup>8</sup> on the basis that (1) the Chairman did have power under Article 74 to determine the objection to KWOK's votes being counted at the EGM; (2) the Chairman's Decision was final and conclusive; (3) the Chairman's Decision was only challengeable on the ground of bad faith and not otherwise; and (4) bad faith was not established on the facts. KWOK then lodged an appeal against Harris J's decision (the **Appeal**).

After the first failed attempt to remove the board, KWOK requisitioned another EGM for the same purpose in 2020. On the same day of his requisition, KWOK commenced legal proceedings to seek a determination on the question of whether Convoy Global is entitled to disallow KWOK's votes if the court has not declared otherwise or has not made an order prohibiting him to vote his shares (2020 Action). Having not received a written confirmation from the board that his votes to be cast at the forthcoming EGM would be recognised, KWOK applied for an interim injunction effectively barring the Chairman of the EGM from disallowing his votes absent any court declaration or order against him (**Injunction Application**).

Both the 2018 Action and the 2020 Action and the ancillary applications made therein concerned the question as to the basis on which the Chairman's Decision could be subject to challenge and set aside.

### To what extent can the Chairman's Decision be challenged?

It is not disputed that a chairman's decision made pursuant to Article 74 of the articles of association could be set aside if made in bad faith. However, could it be challenged on other grounds?

<sup>7</sup> <https://www.thestandard.com.hk/breaking-news/section/2/159909/Cho-Kwai-chee-cleared-in-Convoy-related-fraud-charges>

<sup>8</sup> Kwok Hiu Kwan (郭曉群) v Johnny Chen (陳志宏) & Ors [2018] HKCFI 2112.

At the trial of the 2018 Action, Counsel for KWOK argued that the Chairman's Decision should be set aside as it was manifestly wrong or *Wednesbury* unreasonable (an administrative law concept) in the sense that the decision was one that no reasonable chairman could have reached if he properly directed himself as to his duties and had regard to all the facts he knew or should have known. He sought to bring an administrative law concept into play.

Harris J, however, held that any qualification to the finality of the Chairman's Decision to exclude votes had to be founded on established contractual or company law principles. Applying the well-established principles for implication of contractual terms - that a term should only be implied if (i) it is so obvious that it goes without saying; and/or (ii) it is necessary to give the contract business efficacy, Harris J held that neither of these were satisfied and therefore Article 74 should not be read as subject to the qualification that a chairman's decision could be challenged for being *Wednesbury* unreasonable. The proposed wholesale import of administrative law concepts to qualify Article 74 was therefore misconceived.

On appeal, the CA dismissed KWOK's appeal and endorsed much of Harris J's reasoning:

- (1) There is nothing inherently objectionable in a shareholder restricting the exercise of his rights as a shareholder or in the members, by the articles of association, agreeing to regulate how resolutions are passed. If members of a company have agreed to a particular method of regulating the business of the company, the court should give weight to the agreement contained in the articles of association in light of party autonomy.
- (2) Article 74 empowers a chairman at general meeting to decide whether a vote should or should not be counted for at a particular general meeting. The chairman does not determine any underlying dispute which has given rise to the objection to a member's voting rights.
- (3) It is not necessary to imply in the articles of association a right to challenge a chairman's decision under Article 74 on the ground that it is indisputably wrong or sufficiently bad because:

<sup>9</sup> The 2020 EGM has since taken place on 26 November 2020 but was adjourned shortly after proceedings began and before votes were cast. The adjourned EGM is yet to take place as of the date of this briefing.

<sup>10</sup> Where it is reasonably certain that what the defendant is threatening and intending to do will cause imminent and

- a. If the chairman's decision was indisputably wrong (i.e. an obvious and indisputable mistake was made), the chairman's decision only affects the particular meeting at which the decision was made. The error is open to correction by the chairman himself or at a future meeting;
  - b. Where there is a dispute as to whether a shareholder was entitled to vote, there would not be much difference in terms of bringing the dispute on to trial, between (1) an action on whether the registered shareholder was entitled to vote and (2) an action on whether the chairman's decision not to admit the shares for voting purposes was sufficiently bad, especially when the case is complex. Therefore, allowing a shareholder to challenge a chairman's decision under Article 74 for being sufficiently bad would not enable the dissatisfied shareholder to quickly overturn the erroneous decision.
- (4) It is desirable, especially in the case of a public company, that there is certainty and finality about the status of resolutions put to members, which militates against allowing an aggrieved shareholder to seek to overturn the chairman's decision for being erroneous.
  - (5) There is sufficient protection against abuse of power by a chairman in that a chairman's decision may be challenged on the ground of bad faith.

### Can a member pre-empt a decision to be made by a chairman under Article 74 by obtaining a *quia timet* injunction?

As mentioned above, KWOK commenced the 2020 Action and, as he failed to secure a written confirmation in advance of the 2020 EGM<sup>9</sup> that his votes would be counted, he sought a *quia timet* injunction<sup>10</sup> to pre-emptively restrain Convoy Global from disallowing his votes. The interim application was heard by the Honourable Mr Justice Coleman<sup>11</sup>.

In support of his application, KWOK raised arguments which are not dissimilar to those advanced in the 2018 Action, which have been decided by Harris J. In sum, KWOK argued that a decision by the chairman to reject a member's votes under Article 74 has the effect of interfering with the member's property right. As such, it

substantial harm to the plaintiff, the court may grant a *quia timet* injunction to restrain the defendant from conducting the act concerned.

<sup>11</sup> Kwok Hiu Kwan v Convoy Global Holdings Ltd [2020] HKCFI 2874.

should only be exercised in good faith, rationally and for a proper purpose, and not arbitrarily or capriciously or in breach of the principles of natural justice.

Notwithstanding that Harris J had already decided that the Chairman's decision could only be set aside on the ground of bad faith (thus nothing less than that), counsel for KWOK attempted to argue that that decision (which was binding at the hearing of the Injunction Application as the Appeal was yet to be heard) should only be confined to a chairman's decision *already* made, and not, as in the present case, *yet* to be made.

Coleman J rejected this argument. He held that the attempted distinction between a pre-emptive or quia timet application made in advance of an Article 74 decision and a challenge made after the event of such decision is an illogical distinction. Accordingly, if the chairman's decision once made, cannot be challenged on the grounds of Wednesbury unreasonableness, then equally the chairman's prospective exercise of power under Article 74 cannot be fettered or pre-emptively restrained.

In light of the then looming Appeal, Coleman J declined to differ from the findings and approach of Harris J, and he declined to grant the injunction sought by KWOK to pre-emptively restrain Convoy Global from disallowing KWOK's votes in the 2020 EGM. Even if he were to depart from Harris J's decision on the grounds for setting aside the chairman's decision to reject a member's votes, Coleman J considered that he could not have acceded to KWOK's application by declaring to the effect that the chairman at the 2020 EGM should make a decision that is "proper", not "capricious" or arbitrary as that would pre-suppose that the chairman will make a decision which is subject to legal challenge. Any decision that the 2020 EGM chairman might make is best reviewed *after* it has been taken.

### Takeaway

The recent CA and CFI decisions demonstrate that it is exceedingly difficult for a registered member to challenge a chairman's decision to disallow his votes at a general meeting, where the articles of association of the company provide for the power of the chairman to determine objections to a member's votes. In such circumstance, a chairman's decision can only be challenged on the ground of bad faith and not otherwise. The chairman's decision cannot be challenged even where the decision is Wednesbury unreasonable in the sense that no reasonable chairman, properly directing himself as to his duties, could have reached that decision.

Although it would still be open to a member to challenge a chairman's decision on the ground of bad faith, such legal challenge is inherently difficult as, given the serious nature of the allegation, it must be clearly proved. In the absence of direct evidence, it is necessary for an accuser of bad faith to prove facts and matters from which a *compelling* inference of bad faith can be drawn.

Seeking to pre-emptively restrain a company from disallowing votes in a yet to take place general meeting would also be extremely difficult. A court would unlikely grant such requests unless, in an extreme case, it can be proven in the context that, even in advance of knowing what will take place and how the chairman will act at the prospective general meeting, the chairman is bound to make a decision which is not proper. In this case, it is notable that the board did not respond to KWOK's request for a written confirmation that his votes be allowed at the forthcoming EGM, which could be seen as a wise decision in hindsight.

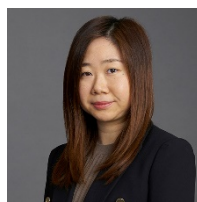
From the perspective of a chairman in general meeting, the CA and CFI decisions confirm that he has wide power in disallowing votes in a general meeting where the articles of association of the company confer such power. However, he should not abuse that power as his decision is still amenable to challenge on the ground of bad faith, which includes exercising his power for an improper purpose, such as that of entrenching the control of another faction of shareholders. A chairman should:

- a) Read in advance of a general meeting the articles of association to assess his powers in relation to adjudicating objections and disallowing votes, and seek legal advice where necessary to ascertain the meaning of particular provisions in the articles;
- b) Where it is anticipated that objections will be raised at a general meeting to a particular member voting, procure the presence of legal advisor at the general meeting, in order to seek legal advice instantaneously at the general meeting;
- c) Bear in mind his duty to make a decision in good faith, which includes not preferring the interests of a shareholder over another; and
- d) Record and document the reasoning of his/her decision for future reference and/or defend against subsequent challenge.

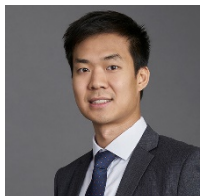
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