



**CASE NOTE // LAM KIN CHUNG V
SOKA GAKKAI INTERNATIONAL
OF HONG KONG LIMITED [2022]
HKCA 480**

Rede Chambers

15.06.2022



Mr KC Lam, a member of Soka Gakkai International of Hong Kong Limited, a charitable company incorporated by guarantee formed to promote Buddhism, sought leave (pursuant to ss 732 and 733 of the Companies Ordinance Cap. 622) to bring a statutory derivative action against its former directors for negligent mismanagement of the company's affairs during the time they were in office. The leave application was opposed by Soka, most of whose members took the view that the former directors had acted in good faith and should not be sued even if they have been negligent as alleged.

Ordinarily, a member seeking leave to bring a statutory derivative action would only need to show (i) a serious issue to be tried and (ii) it appeared to be in the company's interest that it be tried. But here there was a preliminary question: in light of the fact that Soka was not a private company but a charity whose members have no right to any of its surplus assets upon its dissolution, and whose affairs are subject to supervision by the courts at the instance of the Secretary for Justice as *parens patriae* (protector of charities), did Mr Lam have standing to bring a statutory derivative action in the first place? This was the main question before Harris J. On behalf of Soka it was argued that a derivative action, whether common law or statutory, was a procedural device which offers protection to a member of a company who has personally suffered an economic loss (albeit reflective of the loss to the company). However, this presumes that the member had a private or proprietary interest to protect. Whilst this may be so in the case of regular private companies, it was not so in the case of charitable companies who hold their assets for the benefit of their charitable objects in a manner analogous to a trust. Given Mr Lam's status as a member of a charitable company, Soka argued that he could not invoke the court's jurisdiction under ss 732 and 733 of Cap. 622, and must apply instead to the SJ for her fiat to bring a relator action in her name.

Harris J rejected this argument. He held that members of charitable companies who join such companies for a range of activities had an interest in those activities to the extent that any wrongs done to the company which inhibits its proper functioning and condoned by its directors ought to be rectified by way of a common law derivative action. He further held that, in any event, when faced with an application for leave to commence a statutory derivative action, the court would only be concerned with whether the statutory criteria under s 733 of Cap. 622 had been satisfied and, if so, whether it was a proper case for the court to exercise its discretion. He did hold, however, that the fact that the company was a charity might be relevant to the exercise of the court's discretion, in that it may not be interest of the charity to commence a statutory derivative action.

On the SJ's position, he held that the fact that the SJ was *parens patriae* did not mean that a derivative action could not be brought. Whilst there is a public interest in the protection of charities, it did not follow that a member did not have an interest in the proper administration of the company arising from his membership, which was distinct from the public interest in the proper administration of charities generally.

Soka appealed to the Court of Appeal. Yuen JA, giving the leading judgment (with which Kwan VP and Barma JA agreed), placed the argument in the context of a statutory derivative action, and held that although it was true that members of commercial trading companies generally have a private or proprietary interest to protect, there was no ground to "presume" as a condition for all companies that a member applying for leave must have a private or proprietary interest in addition to the conditions set out in the statute. Yuen JA also agreed with Harris J on his reasons on why the SJ's role did not preclude the bringing of a statutory derivative action, but added that the inadequacy of the protection by resorting to the SJ as *parens patriae* rendered it wrong to preclude the protection afforded to members under the statutory regime altogether.

Once Mr Lam was cleared to bring a statutory derivative action, the next question was whether he could obtain leave to do so. Prior to the hearing before Harris J, Soka had called an extraordinary general meeting before its members to ratify all acts of alleged misconduct, the result of which was that an overwhelming majority of members voted not to pursue Mr Lam's claims. However, Harris J held that members were not properly informed of the nature of the claims before the vote, and accordingly held that the ratification carried little to no weight. He therefore gave Mr Lam leave to pursue some (but not all) of the claims of alleged misconduct against Soka's former directors.

To strengthen its position on appeal, Soka called another EGM and managed successfully to obtain leave to adduce fresh evidence before the Court of Appeal to show that an overwhelming majority of members had once again voted not to pursue Mr Lam's claims notwithstanding Harris J's decision. However, the Court of Appeal held, once again, that Soka had not properly informed its members of the true position and the purported ratification was marred by deficiency.

A key part of the court's reasoning centred on the proposition that, following the United Kingdom Supreme Court's decision in *Children's Investment Fund Foundation (UK) v AG and ors* [2022] AC 155, members of charitable companies limited by guarantee owe fiduciary duties in relation to its charitable objects, and that accordingly Soka's members were to vote in the best interests of the company. Apart from the fact that this was not drawn to members' attention, the Court of Appeal held that the way members could exercise their

voting rights consistently with their duty owed to Soka's charitable objects was to focus on the financial considerations of pursuing Mr Lam's claims and that other, non-financial considerations could not override those considerations. Further, although the court held that it would not normally intervene absent a breach of duty or the circumstances of the case had reached a level of seriousness and exceptionality, it was nevertheless its view that the EGM was so deficient that nothing would be served by remitting the matter back to the first instance judge for reconsideration and proceeded to dismiss the appeal.

This [litigation](#) has brought up a number of important issues concerning the interrelation between companies and charities law. These issues have never been examined before in this jurisdiction and would benefit from the insight and clarification of the highest court. A further appeal has been lodged and is pending a decision and updates are to follow. [Ambrose Ho SC](#), leading [Michael Yin](#) and [Justin Ismail](#), acted for Soka in the Court of First Instance and the Court of Appeal and continue to act for them in the further appeal.