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ALTERNATIVE DISPUTE RESOLUTION OF SHAREHOLDER DISPUTES IN HONG KONG:  
INSTITUTIONALIZING ITS EFFECTIVE USE

By  
David Huehnergarth\*

I. INTRODUCTION

Dr. Ida Kwan Lun Mak<sup>1</sup> wrote *Alternative Dispute Resolution of Shareholder Disputes in Hong Kong: Institutionalizing Its Effective Use*<sup>2</sup> to analyze the institutional status of alternative dispute resolution (“ADR”) methods within Hong Kong economic, social and legal systems, and to suggest mechanisms to advance the institutionalization process.<sup>3</sup> Hong Kong is a blossoming global financial hub, and its laws governing ADR are written specifically to foster more international business.<sup>4</sup> However, the largest strata of Hong Kong’s economy is still comprised of small private limited companies, whose shareholder disputes are not well suited for resolution via litigation or dominant arbitral regimes.<sup>5</sup> Dr. Mak’s goal in writing this book is to assert a theoretical framework by which to measure the efficacy of Hong Kong’s current legislation governing shareholder dispute resolution via legal and private means.<sup>6</sup> The author guides the reader through her research by truncating the book into three sections: the developmental history of ADR in Hong Kong shareholder disputes, the institutional acceptance and legitimacy of ADR, and her suggested future legislative adaptations to regulations governing ADR in shareholder disputes.<sup>7</sup> Dr. Mak concludes that ADR systems employed in Hong Kong shareholder disputes are almost fully institutionalized, before proposing policy options to expedite the process and improve the standing of ADR as a potential solution to shareholder disputes.<sup>8</sup>

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<sup>1</sup> Dr. Ida Kwan Lun Mak is employed at the University of Hong Kong Department of Law as research assistant. Her research is specialized in empirical studies of the company laws, alternative dispute resolution methods, and sociolegal studies employed in Hong Kong. This book is an adaptation of her doctoral thesis, of which the underlying research was supervised by Katherine Lynch. (IDA KWAN LUN MAK, *Alternative Dispute Resolution of Shareholder Disputes in Hong Kong: Institutionalizing Its Effective Use* xi-xiii (2017)).

<sup>2</sup> DR. IDA KWAN LUN MAK, *ALTERNATIVE DISPUTE RESOLUTION OF SHAREHOLDER DISPUTES IN HONG KONG: INSTITUTIONALIZING ITS EFFECTIVE USE*, CAMBRIDGE UNIVERSITY PRESS (2017).

<sup>3</sup> *Id.* at 16.

<sup>4</sup> *Id.* at 3, 32.

<sup>5</sup> *Id.* at 3-10.

<sup>6</sup> *Id.* at 18.

<sup>7</sup> Mak, *supra* note 2, at vii-viii.

<sup>8</sup> *Id.* at 220-232.

Dr. Mak uses this book to analyze the progression of institutionalization and to present findings into what is preventing further progression,<sup>9</sup> yet she does not properly consider the most fundamental element of all types of adjudication; parties and lawyers are self-interested, seeking outcomes that are as favorable to them as possible.<sup>10</sup> For example, Dr. Mak explains that parties in Hong Kong shareholder disputes are often personally affiliated, and are primarily motivated by personal desires for money and power.<sup>11</sup> Dr. Mak then fails to recognize such motivations as potential reasons for clients to refuse to employ ADR on judicial or professional advice.<sup>12</sup> Similarly, Dr. Mak states that Hong Kong lawyers have monopolized their profession to preserve the level of their social status and financial compensation,<sup>13</sup> then fails to consider the obvious when questioning why those same lawyers are less likely to utilize or encourage less expensive, more expedient ADR systems to resolve their client's shareholder disputes.<sup>14</sup> Despite such flaws, *Alternative Dispute Resolution of Shareholder Disputes in Hong Kong: Institutionalizing Its Effective Use* is still a thorough study that offers compelling legislative options to advance ADR. Though the ideas presented are incredibly complicated, that depth offers substantial weight to Dr. Mak's array of programs and reforms tailored to advance the institutional progress of ADR in Hong Kong shareholder disputes. Overall, the book is an insightful and informative foray into Hong Kong shareholder dispute resolution, but the flaws in both its constructive and argumentative structure chip away at any persuasive weight it may hold.

## II. OVERVIEW

Expressed through eight chapters spanning three main sections,<sup>15</sup> this book's overarching argument is that ADR is more institutionalized in Hong Kong due to its growing usage by parties and lawyers and also because of mandates made by the Hong Kong legislature and judiciary to encourage parties to solve their disputes through ADR.<sup>16</sup> The Hong Kong legal system enshrines an imbalance of power between the city's historically powerful industrial lobbies and the general public interest.<sup>17</sup> This imbalance is highlighted by a constitutional right to the freedom to contract

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<sup>9</sup> Mak, *supra* note 2, at 216.

<sup>10</sup> *Id.* at 132, 158.

<sup>11</sup> *Id.* at 132.

<sup>12</sup> *Id.* at 137, 145.

<sup>13</sup> *Id.* at 158.

<sup>14</sup> Mak, *supra* note 2, at 169.

<sup>15</sup> *Id.* at 28.

<sup>16</sup> *Id.* at 226.

<sup>17</sup> *See, e.g., id.* at 125 (“[b]ig business enterprises and professional groups in Hong Kong have exerted their political influences in formulating and implementing the corporate law for safeguarding the free operation of business.”)

and the public's guaranteed access to courts<sup>18</sup>; even though people are guaranteed a chance to plead their case, the fundamental purpose of the Hong Kong legal system is to maximize and maintain economic growth.<sup>19</sup> The recent surge in the use of ADR in shareholder disputes is paralleled by a dearth of legislation and judicial guidance governing ADR, subsequently pressuring the government to introduce new policies that promote ADR while maintaining the balance between business and civilian interests.<sup>20</sup> Dr. Mak discusses the facets of this legislative gap in the three sections of this book.

First, Dr. Mak addresses how dispute resolution methods in Hong Kong dramatically shifted as the city ascended into a global financial hub; as Hong Kong bloomed, so too did the number of suits filed in its courts, leading to extensive docket backlogs and a coequal pressure to clear them.<sup>21</sup> One such means is the legislative endorsement of ADR, and chapter three identifies and develops methodologies to study the current ADR policy, and its reception in the Hong Kong legal community.<sup>22</sup> Comprising chapters four, five and six, part II explains the socio-legal and empirical analysis of how ADR processes can further consolidate institutional legitimacy in the law, court rules, and directives, and in the eyes of the Hong Kong legal community.<sup>23</sup> Part III is a singular, forward-looking chapter, which probes the potential for new law governing company composition and shareholder actions by analyzing similar international schemes for whatever teachings they can provide on the proper implementation of a court-based ADR system.<sup>24</sup> Finally, Dr. Mak uses a conclusory chapter to summarize her findings from each part and emphasizes the need for more mechanisms to study Hong Kong dispute resolution only grows as the system changes.<sup>25</sup> If ADR is ever to achieve full institutionalization, the Hong Kong government and judiciary need clear and objective guidelines, not endless empirical studies, before they can adopt ADR into comprehensive legislation.<sup>26</sup>

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<sup>18</sup> Xianggang Jiben Fa art. 35, § 1, art. 109 §1, art. 110 (H.K.).

<sup>19</sup> Mak, *supra* note 2, at 32 (Dr. Mak cites Articles 35, 109, and 110 of the Hong Kong Basic Law, which state, respectively, that the right to a court date is unfettered, that the Hong Kong government shall act to maintain the city's status as an international financial center, and that the law must safeguard the free operation of business. Xianggang Jiben Fa art. 35, § 1, art. 109 §1, art. 110 (H.K.)).

<sup>20</sup> *Id.* at 72-73.

<sup>21</sup> *Id.* at 32, 217. (the author ties the origin of the shift towards ADR to the construction industry, specifically the Hong Kong Airport Core Programme, which successfully showed the benefits of mediation and other ADR methods).

<sup>22</sup> *Id.* at 45-67.

<sup>23</sup> *Id.* at 32.

<sup>24</sup> Mak, *supra* note 2 at 181-215.

<sup>25</sup> *Id.* at 216-31.

<sup>26</sup> *Id.* at 230 (Dr. Mak cites her definition of meta-analysis to Jeremy A. Blumenthal, 'Meta Analysis: A Primer for Legal Scholars,' TEMPLE LAW REVIEW, 80 (2007), 201-244 at 202).

While the three-pronged organizational structure of the book is clear, the topical presentation and interrelations between each chapter seem frenetic and unclear. Mak introduces new concepts without explanation, including arcane sociolegal academic theories, and others are asserted as fact without any establishing citations.<sup>27</sup> The reader is frequently left to thumb between pages to ascertain what the author is referring to when Mak may or may not have addressed the topic. Chapter one closes with a list of limitations on the present study, including the lack of substantive case law analysis on the development of Hong Kong law, yet the author constantly refers to case law for guidance.<sup>28</sup> A study into a developing legal issue would undoubtedly benefit from a substantive case law analysis, especially when the role of the court is so important to the topic, that the book dedicates all of chapter four to discussing it. While a consistent and clear organizational structure could readily fix these problems, the reader will always be disappointed and confused by the lack depth afforded to the clear and obvious issues surrounding the allocation of power between parties, and the self-interested motivations that can arise when business partners oppose each other in court.

### III. INTRODUCTORY CHAPTER

Chapter one introduces the book and provides the foundational factual background behind unfair prejudice proceedings in Hong Kong shareholder disputes, an explanation of what institutionalization is, and a summarized catalog of the book's remaining content.<sup>29</sup>

Dr. Mak first provides the background on Hong Kong shareholder disputes and the derivative concerns associated with allowing their resolution by extrajudicial procedures. Hong Kong is a global financial hub governed by fundamental free-market principles designed to encourage capitalism and economic growth,<sup>30</sup> but sixty percent of the population is employed by small family businesses, not the giant corporations that dominate the economy.<sup>31</sup> These small businesses are often structured by informal agreements created at the formation of the owner's partnership.<sup>32</sup> However, because Hong Kong law dictates that all businesses are governed

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<sup>27</sup> See, e.g., Mak, *supra* note 2, at 92 (suggesting a winding-up order would be an ineffective and unreasonable remedy if the parties could find another solution, an order last mentioned without explanation on page six); see also, *id.* at 104 (citing the equitable considerations at stake in unfair prejudice proceedings to *Ebrahimi v. Westbourne Galleries, Ltd.* [1973] AC 360 at 379, a case last mentioned once on page seven).

<sup>28</sup> See, e.g., *id.* at 157 (discussing historical Hong Kong judicial animus for mediation agreements, as consistent with *Hyundai Engineering and Construction Co. Ltd. v. Vigour Ltd.*, [2005] HKLRD 723 at 734-735); see also, MAK, *supra* note 2, at 57 (“the study of relevant case law . . . should not be ignored, as [cases] can serve as a benchmark for comparison with the existing case law developments. . .”).

<sup>29</sup> *Id.* at 1-32.

<sup>30</sup> See, *id.* at 38, 76. (Article 110 of the Hong Kong Basic Law provides that the Hong Kong government must safeguard the free operation of financial business and financial markets. Additionally, Article 109 requires the government to act to ensure that Hong Kong remains an international financial center).

<sup>31</sup> *Id.* at 3.

<sup>32</sup> Mak, *supra* note 2, at 3.

exclusively by the majority shareholder, a combination that lends towards disputes when personal tensions flare.<sup>33</sup> When the majority shareholder of a company takes an action which unfairly prejudices and harms the minority's interest, the minority can file an unfair prejudice proceeding with the court seeking a remedy.<sup>34</sup> The endless variety of familial and business disagreements shape derivative shareholder disputes, and therefore whether the majority's action is sufficient to justify a legal remedy requires an objective reasonability analysis, judged against established equitable principles.<sup>35</sup> Thus Hong Kong courts are effective forums for unfair prejudice proceedings because the law provides them with the requisite discretionary flexibility to properly address the specific needs of each case.<sup>36</sup> However, as mentioned previously, the rapid economic growth of Hong Kong inundated the courts with costly, lengthy, unfair prejudice proceedings, thus, fostering an ADR industry in the court's stead, designed to be completely adaptable, less time consuming, and expensive than judicial alternatives.<sup>37</sup> Starting with the Civil Justice Reform of 2009, the Hong Kong government has sought to make ADR the primary method to resolve shareholder disputes.<sup>38</sup>

Despite legal incentives, ADR institutionalization in Hong Kong is not yet complete. Institutionalization is a "process by which certain practices . . . have acquired legitimacy through their link to broader cultural framework of beliefs or norms that most people support and will therefore endorse[,]" and the institutionalization status of a practice is defined as being pre, semi, or fully institutionalized.<sup>39</sup> Mak identifies three types of legitimacy: pragmatic, moral, and cultural-cognitive.<sup>40</sup> To properly analyze the institutional progress of ADR, Dr. Mak next explains its risks and the legitimacy it has and has not yet acquired under Hong Kong law. She assesses a semi-institutional status to ADR in Hong Kong shareholder disputes because the public and legal professionals retain doubts about its fairness and efficacy.<sup>41</sup>

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<sup>33</sup> Mak, *supra* note 2, at 3; *see also id.* at 108 n. 21 (stating majority shareholders sometimes opt to align business interests with their personal interests, in defiance of the firm's best interest. William R. Scott, *Financial Accounting Theory*, 3rd ed. (Toronto Practice Hall, 2003), 273-279).

<sup>34</sup> *Id.* at 4-8.

<sup>35</sup> *Id.* at 5, 12-13 (Dr. Mak identifies three objective classifications of disputes: dissension, oppression, and deadlock).

<sup>36</sup> *Id.* at 6 (the author states this is because unfair prejudice proceedings are derived from a law designed to protect minority shareholders, because the 2014 Companies Ordinance Cap. 622 expanded a courts discretion in granting relief, and because unfair prejudice proceedings are cheaper and more flexible than other statutory alternatives).

<sup>37</sup> *Id.* at 6-29. (the author identifies seven basic dispute resolution methods: negotiations, facilitative mediation, collaboration, mini-trials, expert determination, arbitration, and court adjudication).

<sup>38</sup> Practice Direction 3.3, paras 8-11 (Hong Kong courts now compel or recommend the parties undertake some form of ADR before the court proceeding can continue towards a court verdict).

<sup>39</sup> Mak, *supra* note 2, at 16.

<sup>40</sup> *Id.* at 17.

<sup>41</sup> *Id.* at 17, 19, 79 (the Basic Law of Hong Kong "originate[s] from the free-market ideology, which is in accord with shared beliefs among the powerful group of elite businessmen . . . [,]" and, under the right to a court hearing,

Finally, the chapter ends by outlining a theoretical framework to measure the institutionalization of ADR in Hong Kong shareholder disputes by the progression of its societal legitimacy.<sup>42</sup> Indicative of similar issues to come, the organizational structure of the introduction is inconsistent within itself and the rest of the book, possibly confusing the reader.<sup>43</sup> There is a lack of any proper foray into the problem of self-interested parties and lawyers, even though chapter one provides the basis of this criticism as a fundamental concern affecting the topic.<sup>44</sup> Though the introduction establishes all the of the foundational background built on later, the inconsistent amount of explanation proffered for later chapters could confuse the reader.<sup>45</sup> If the introduction were retooled to reflect the remainder of the book better, it would properly build on itself to introduce the remaining topics rather than providing some sort of crash course in Hong Kong litigation and sociological theory. Lastly, despite being a necessary inclusion, the string of self-imposed limitations on the present study seem both excessively harsh and arbitrary and may cause the reader to question the merits of the remainder of the book.<sup>46</sup>

#### IV. DEVELOPMENT AND GROWTH OF ADR FOR SHAREHOLDER DISPUTES IN HONG KONG AN OVERVIEW

To properly introduce the factual context of the following theoretical and empirical analysis, chapter two restates the origin of the use of ADR in Hong Kong and how it came to become the industry standard for shareholder disputes.<sup>47</sup> The primary point established in chapter two is that ADR and court-based shareholder proceedings are complementary and compatible with each other, though the author concludes the court's future is to promote the benefits of ADR to skeptical legal professionals, while ADR will become the primary dispute resolution method.<sup>48</sup>

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treats ADR as a completely voluntary process, for which agreement is determined solely by the decision of the majority shareholder. The non-binding nature of ADR means the practice is relegated to an extra step in litigation).

<sup>42</sup>Mak, *supra* note 2, at 16-32.

<sup>43</sup> *Id.* at 18, 28 (within the chapter, the three organizational themes are listed to imply there is nothing after the chapter six analysis of legal professional's opinions on ADR. The introduction also refers to itself in a manner that implies there is another introductory chapter, and that the current chapter is not chapter one).

<sup>44</sup> *Id.* at 16 n. 69.

<sup>45</sup> *See, e.g., id.* at 17-25 (the author includes the definition of each type of institutionalization but reserves the coequally important definitions for the types of legitimacy to be established in two later chapters. Similarly, the author reserves explaining how institutionalization could improve for the final chapter, before proceeding to frame how the book will argue the point six chapters before the topic is discussed).

<sup>46</sup> *Id.* at 29 (the author opted only to survey lawyers for their opinions on ADR, despite rehashing, in this chapter and most others, the role judicial discretion plays in both remedying unfair prejudice in shareholder disputes, as well as when to stay proceedings to recommend parties proceed to ADR).

<sup>47</sup> Mak, *supra* note 2 at 30.

<sup>48</sup> *Id.* at 31.

Dr. Mak first explains the deeper history of ADR in Hong Kong, tying the commonality of the practice to the specific litigative needs of an international financial hub; international companies prefer ADR for its flexibility and confidentiality.<sup>49</sup> Since arbitration is a preferred resolution medium for international commercial disputes, to remain an international financial hub, Hong Kong must remain the international arbitral hub of Asia to comply with Article 109 of the Basic Law.<sup>50</sup> In time, courts realized that recommending parties to an unfair prejudice proceeding to first use ADR before seeking court adjudication was actually a proper use of a judge's discretion to manage cases because a court-affiliated ADR system was not a lesser procedure but a supplementary practice that could improve the court system.<sup>51</sup> In dereliction of the precedential disdain for the process, and in the wake of the success of arbitration, as a means to mitigate the costs and duration of court-based shareholder proceedings, Hong Kong law began to encourage ADR to resolve shareholder disputes.<sup>52</sup>

Chapter two does not provide much new information for the reader and serves to represent the organizational flaws common throughout the book. To the reader, this chapter seems needlessly redundant, offering no argumentative insight into the topic and only introduces the details of the Hong Kong arbitral industry already discussed in chapter one.<sup>53</sup> However, that information on arbitration is almost irrelevant to the remainder of the book, as “[m]ediation is now recognized as the primary ADR process used for the reform of the law and procedures relating to unfair prejudice proceedings.”<sup>54</sup> The reader would likely not be confused if chapter one had already incorporated this chapter, nor would the reader be troubled should this chapter have been expanded to address other elements important to the topic but fall beyond the scope of the book, like other ADR processes or notable landmark cases.

## V. KEY METHODS FOR EVALUATION OF POLICY DEVELOPMENT ON ADR IN SHAREHOLDER DISPUTES

To analyze the legitimacy level achieved by ADR in shareholder disputes, Dr. Mak needed to create her own research methodology to properly quantify any objective factors weighed in the decision to promote or discourage ADR from a subjective survey of Hong Kong legal

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<sup>49</sup> See e.g. Mak, *supra* note 2, at 31.

<sup>50</sup> *Id.* at 34-36 (the Hong Kong arbitration industry was promoted by modernizing its law to meet international standards, by funding its own arbitral institution, and by innovating new practices and freedoms for parties to employ).

<sup>51</sup> *Id.* at 38-44 (the right to access court under Basic Law Article 35 meant courts could order parties to undergo ADR, absent their mutual agreement not to, if either party could still petition for the hearing to resume upon completion of the ADR method).

<sup>52</sup> *Id.* at 39.

<sup>53</sup> *Id.* at 8-15.

<sup>54</sup> Mak, *supra* note 2 at 15 (citing Rimsky Yuen, ‘HK a Perfect Partner in Mediation’, Conference on Asia Pacific International Mediation Summit (India, 15, February 2015)).



professionals, and she uses chapter three to explain it.<sup>55</sup> Dr. Mak explains that a realistic evaluation method is optimal because it incorporates the context, mechanisms, and potential outcomes of a dispute and allows the use of preexisting theories and knowledge in conjunction with data when constructing a methodology.<sup>56</sup> To assess the context in which ADR has acquired legitimacy requires reviewing the differences between the current era of shareholder disputes which have legitimized ADR, and the established culture of unfair prejudice settlements that had preceded the 2009 reforms; Dr. Mak identified reformed company law, the court's encouragement of ADR, and reformed court rules as contextual factors to study.<sup>57</sup> Dr. Mak next specifies three mechanisms that improve the understanding and awareness of ADR in shareholder disputes: coercive, normative, and mimetic mechanisms that could have institutionalized the use of ADR in shareholder disputes.<sup>58</sup> Lastly, legitimization corresponds to their respective stage of institutionalization: pragmatic, moral, and cognitive.<sup>59</sup>

Dr. Mak also assesses the merits of a pluralist methodology, whereby multiple methods are mixed to achieve a broader understanding of the legal and non-legal factors driving institutionalization.<sup>60</sup> Lastly, traditional legal study methods, comparative study methods, and empirical legal research comprise the author's preferred research method.<sup>61</sup> The traditional method involves a case law review and understands the law as a set of social beliefs and practices, including those of judges, and thus cases should include some of the social beliefs which drove the decision.<sup>62</sup> Comparative study here meant comparing foreign ADR practices with those of Hong Kong, and the findings suggest that incorporating and imitating foreign practices is highly effective at driving legitimacy.<sup>63</sup> Lastly, the empirical method was used to identify the underlying

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<sup>55</sup> Mak, *supra* note 2, at 45-67.

<sup>56</sup> *Id.* at 45-48 (Dr. Mak cites the "context, mechanisms, outcome" pattern to Pawson and Tilley, 'Realistic Evaluation,' 83-88. She chose this method because it best accommodates small data sets comprised of anecdotal evidence of variable subjects).

<sup>57</sup> *Id.* at 51-53.

<sup>58</sup> *Id.* (coercive mechanisms are rules established by a controlling authority, and which must be followed at risk of punishment. Normative mechanisms stem from beliefs, habits, and values which are taken for granted, like using something different because you believe it to be the new norm. Mimetic mechanisms originate in the need to cope with uncertainty by copying established legitimate models).

<sup>59</sup> *Id.* at 54-55 (pragmatic legitimacy arises from a self-interested calculation to determine the best direction. Moral legitimacy arises when authority figures provide a moral blessing to an action. Cultural-cognitive legitimacy is achieved when a norm is considered as indispensable, and abidance carries similar status to a rule or law).

<sup>60</sup> Mak, *supra* note 2 at 58.

<sup>61</sup> *Id.* at 56.

<sup>62</sup> *Id.* at 57-59.

<sup>63</sup> *Id.* at 60.

factors affecting lawyer's positions on ADR and helps to understand the motivations and actual opinions expressed by legal practitioners.<sup>64</sup>

Given the niche size of the research topic, Dr. Mak was forced to tailor the appropriate sample to only 120 subjects, with three nonresponses, a risk which she defends by stating she sufficiently controlled her population to produce a representative sample despite the small size, though it does not preclude other factors from driving the findings.<sup>65</sup> However, she does admit the potential for her data collection method, a five answer multiple-choice survey used to measure subjective opinions, to produce inaccurate results based on disparities in each subject.<sup>66</sup>

Having fully outlined the methodology for her empirical review of lawyerly opinions on ADR, the author resigns the section three full chapters from its implementation,<sup>67</sup> another example of the disorganization that a reader could readily find confusing. The author also put the overall conclusion of the chapter, her usage of a pluralist research methodology, in the middle of the chapter, after speaking about the context, mechanisms, outcome model as if it was going to be employed.<sup>68</sup> Given the nuance and esoteric nature associated with the field research methodologies of socio-legal theory, the lack of initial direction from the author means the reader could easily be confused about which method the author was choosing. Further, that detail and understanding will be three chapters stale when the reader reaches its implementation, further risking confusion.

Among concerns with the methodology itself, the author's limitation, the preclusion of any case law analysis seems indefensible after the author also stated that analyzing case law before the passage of the ADR legislation was necessary to ascertain the socio-legal factors that motivated judicial decision making.<sup>69</sup> The author admits the risks associated with the method and presents the statistical analysis undertaken as a defense against accusations of bias.<sup>70</sup> However, the author never explains what those statistical mechanisms do, or how they adapt the findings around bias, a manner any reader without an advanced understanding of predictive statistics could understand. The chapter should be closer to the actual study results, and it needs to organize and explain the specific numerical methods to be employed.

## VI. THE ROLE OF THE COURT: SECURING THE LEGITIMACY OF COURT-CONNECTED ADR INITIATIVES FOR SHAREHOLDER DISPUTES

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<sup>64</sup> Mak, *supra* note 2 at 62.

<sup>65</sup> *Id.* at 63-65, 177.

<sup>66</sup> *Id.* at 177.

<sup>67</sup> *Id.* at 66 n. 101, n. 102, n. 103, n. 104 (all of these footnotes say to see chapter 6 for the discussion of the study).

<sup>68</sup> *Id.* at 51-60.

<sup>69</sup> Mak, *supra* note 2 at 60.

<sup>70</sup> *See, e.g., id.* at 166 (“[i]n further attempt [sic] to assess model fit, the author computed the Hosmer-Lemeshow goodness-of-fit test statistics. The Hosmer-Lemeshow goodness-of-fit test put observations into groups based on estimated probabilities then computes a Pearson Chi-square statistic based on the observed and estimated frequencies in the groups, and thus a lack of model fit.”)

Chapter four opens by assigning the courts the role of mitigating the dangers of self-interest in an adversarial system; the length and cost of shareholder disputes is the product of “unscrupulous litigants or lawyers” abusing the court rules to delay proceedings and starve the opponent’s resources.<sup>71</sup> However, merely changing courtroom procedural rules is unlikely to affect change, and thus the author uses chapter four to analyze how a combination of ADR and the bench’s power to manage its cases can improve the cost and quality concerns associated with all shareholder disputes.<sup>72</sup> The cooperative role between the two resolution practices is derived from the court’s power to encourage litigants to partake in ADR under its own oversight, affecting the ADR method with its own cultural-cognitive legitimacy under the rules and economic values under Hong Kong Basic Law.<sup>73</sup>

For cost and quality to improve in a court-connected ADR proceeding, the parties cannot act unscrupulously, both by using mediation as a litigative ploy and for personal gain, and this is not a guarantee.<sup>74</sup> The first argument is subject to a glaring required assumption, one that is validated by the author both earlier and later in the book, and one that could cause a reader to question the credibility of the proposal. Some studies have already shown ADR to be just as lengthy and as expensive as litigation.<sup>75</sup> The Basic Law’s guaranteed right to court compounds this problem, because regardless of the finality of an ADR agreement, either party can still move to litigation, thus relegating court-connected ADR to another step in the litigation process.<sup>76</sup>

Next, the author suggests that courts may legitimize connected shareholder ADR proceedings by emphasizing the commonality between the policy objectives of court-connected ADR and the economic motivations within the Hong Kong Basic Law.<sup>77</sup> By providing a more cost-effective dispute resolution method that enhances efficiency while increasing corporate autonomy, the author argues court-connected ADR is aligned with the tenets of the Basic Law and thus will be granted the cultural-cognitive legitimacy the Basic Law provides.

Upon analysis of judicial opinion to determine the accuracy of that statement, the book presents the second most glaring issue with an argument for greater institutionalization of ADR.<sup>78</sup>

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<sup>71</sup> Mak, *supra* note 2, at 71.

<sup>72</sup> *Id.* at 72 (the quality of the ADR is defined as a measure of party autonomy and control over the proceeding).

<sup>73</sup> *Id.* at 73-74 (the author emphasizes this point by explaining that a court which applies to an ADR case, a system of rules that lacks the force of laws, the local community will subsequently treat those rules with a higher degree of legitimacy).

<sup>74</sup> *See, e.g., id.* at 16 (majority shareholders will sometimes attend ADR sessions with no intention to work towards an amicable settlement because the law favors them in court, and there is no prescribed minimum level of participation necessary for ADR).

<sup>75</sup> *Id.* at 169 (citing Thomas O. Main, *ADR: The New Equity*, UNIVERSITY OF CINCINNATI LAW REVIEW, 74 (2005), 329-404 at 396-397).

<sup>76</sup> *See, e.g., Mak, supra* note 2, at 139.

<sup>77</sup> *Id.* at 81.

<sup>78</sup> *Id.* at 82.

Court-ordered ADR fails to properly resolve disputes because it punishes parties for exercising their right to seek a trial under the Basic Law.<sup>79</sup> In an effort to expedite ADR proceedings and to ensure the parties take them seriously, Hong Kong courts are entitled to assess costs on parties who refuse to go to ADR.<sup>80</sup> Given parties in Hong Kong shareholder disputes tend to be poorer, so much so they generally need financial aid to afford any shareholder dispute proceedings,<sup>81</sup> the threat of cost sanctions could be considered coercion, so much so that lawyers have taken to simply advising their clients to go to ADR in bad faith rather than absorb the sanction.<sup>82</sup> Even if the party were to return to court after ADR, making ADR a step in the litigation game, the process still takes time and money, opposite the intended purpose of the law. This flaw supports the argument that self-interested motivations and an imbalanced remedy structure mars the Hong Kong shareholder ADR system. The stronger party can more likely absorb the additional legal costs of either pointless ADR proceedings or cost sanctions, rendering the entire ADR proceeding into a farce meant to drain the weaker party's resources. A reader could interpret this as a failure to facilitate greater access to dispute resolution, a gaping hole in the author's argument in favor of court-based ADR. Additionally, the reader could see this as a byproduct of a continuing oversight in the author's theory favoring ADR for unfair prejudice proceedings, one that prevents the practice from ascending the rungs of institutionalization and legitimacy.

The final argument presented in chapter four, that courts better address the proportionality concerns of minority shareholders, supports the self-interest argument against court-ordered ADR; the book states that courts will strike down an unfair prejudice petition upon notice that the respondent has made a reasonable offer to buy out the petitioner.<sup>83</sup> Winding-up-order based remedies<sup>84</sup> prevent those unscrupulous litigators from harassing the other party with unfair buyout offers, while also preventing those similarly devious parties from using court-ordered arbitration as an evidentiary fishing expedition.<sup>85</sup> ADR would have created numerous new opportunities for the majority party to decimate the weaker party's resources. The author comes unbelievably close to admitting this problem is still prevalent by citing to new law which prevents the disclosure of

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<sup>79</sup> Mak, *supra* note 2, at 82.

<sup>80</sup> Practice Direction 31, paras. 4 and 5 (though there are no enumerated minimum participation levels in Practice Direction 31, examples are included in Appendix C, footnote 4).

<sup>81</sup> Mak, *supra* note 2, at 83-89.

<sup>82</sup> *Id.* at 89.

<sup>83</sup> *Id.* at 93.

<sup>84</sup> A winding up order refers to a court order mandating shareholders to facilitate the sale of one shareholder's stock in a company to the other shareholder(s), where generally the complaining party at court is the selling shareholder. It is essentially a court ordered selloff meant to ensure that a fair price and deal is offered to a party seeking to leave a company.

<sup>85</sup> Mak, *supra* note 2, at 95.

mediation communications,<sup>86</sup> however this does not address concerns associated with a majority party pressuring the weaker party into an unfair buyout agreement.

## VII. REFORMS OF COMPANY LAW: LEGITIMIZING THE USE OF INFORMAL PROCESSES IN CONJUNCTION WITH COURT BASED SHAREHOLDER PROCEEDINGS

The recently passed Section 727 of the Companies Ordinance enables the Hong Kong Chief Justice to promulgate rules regulating unfair prejudice proceedings. This chapter is Dr. Mak's effort to examine how the new rulemaking structure will coincide with extrajudicial and court-based unfair prejudice proceedings, specifically how the court may now create rules that require parties to consider or undergo ADR processes in unfair prejudice proceedings.<sup>87</sup> Again the author addresses the symptoms of self-interested litigants, and again fails to extrapolate how the issue could affect mandatory ADR processes, instead asserting, without citation, that it the effect such a situation will have on minority shareholder rights is uncertain.<sup>88</sup> Instead, the author uses chapter five to assert that the corporate policy conventions under the new rules balance the flexibility of ADR proceedings with the need to protect minority shareholders from intrinsic procedural imbalances. The author does this by acknowledging that corporate legal structures which enable total internal control over shareholder disputes can result in abuse by the majority shareholders, albeit a rare occurrence.<sup>89</sup>

The argument states a strong legal framework paired with an efficient court enforcement system is a prerequisite to protect minority shareholders from controlling shareholders, and that available, efficient dispute resolution systems are perquisites for an efficient court and economic system.<sup>90</sup> Thus, the author concludes, incorporating ADR further into statutory unfair prejudice practices will open access to resolution structures, which enables a potent enforcement system, which thus protects the minority shareholders from controlling majority interests by providing a wider selection of remedies to a breach of their rights.<sup>91</sup>

Any reader will notice that the author is precluding the ability of the minority shareholder to adequately acquire remedies for the breach of their rights by the majority. Rather, the author asserts that a wider pool of remedial choices constitutes sufficient protections for the minority interest simply because it offers more party choices, and also because private ADR remedies

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<sup>86</sup> Mak, *supra* note 2, at 96, citing Section 8(2) of the Mediation Ordinance (Cap. 620).

<sup>87</sup> *Id.* at 104.

<sup>88</sup> *Id.* at 89 n. 93, 106, 107. (forced ADR only serves to increase the time commitment and costs of an unfair prejudice proceeding by functioning as an extra step in the litigation game); Hazel Genn et al., *Twisting Arms: Court Referred and Court Linked Mediation Under Judicial Pressure* Ministry of Justice Research Series, Series 1/07 (2007) at 15.

<sup>89</sup> *Id.* at 107. (citing William R. Scott, *Financial Accounting Theory*, 3rd ed. (Toronto Practice Hall, 2003), 273-279).

<sup>90</sup> *Id.* at 110, 111.

<sup>91</sup> Mak, *supra* note 2, at 112.

cannot achieve the guaranteed efficiency and fairness associated with a court-ordered winding-up proceeding as mentioned above.<sup>92</sup>

Next, the author presents the pitfall in caseloads in American civil courts as evidence that people consider ADR as an adjudicative process that is compatible with the goals and purposes of the courts, and again fails to present an explanation for how the imbalance of power between majority and minority shareholders can derogate the rights of the minority.<sup>93</sup> Dr. Mak attempts to show a lack of coercion present when arbitration proceedings are forced by law or by court order by stating that civilians must uphold their legal commitments or else risk damaging the legitimacy of them.<sup>94</sup> Any reader would note that this argument fails even to assert a lack of coercion; that a person is obligated to honor their legal commitments when they involve tolerating a loss of a fundamental right just because the rulemaking body depends on acquiescence to survive, cannot be considered an exercise of choice. This argumentative weakness is highlighted by the author's later references to the uncertainty of the future as a justification against enforcement of consensual mediation agreements.<sup>95</sup> The conclusion to chapter five, that ADR and court proceedings are compatible and complementary programs that also offer intrinsic benefits in unfair prejudice disputes, is so predicated on logical fallacies that it has the potential to destroy any credibility the reader still holds for the author's arguments. Properly addressing the vulnerability to majority abuse in Hong Kong's shareholder ADR system would have properly fixed chapter five.

#### VIII. DIFFUSION OF PROCEDURAL INNOVATIONS: AN EMPIRICAL ANALYSIS OF HONG KONG LAWYER'S ATTITUDES ABOUT THE USE OF ADR FOR SHAREHOLDER DISPUTES

Chapter six is the empirical analysis meant to reinforce the author's numerous hypothesis and preexisting arguments about the status of institutionalization of ADR as applied in shareholder disputes.<sup>96</sup> Dr. Mak suggests that ADR needs the acceptance of legal professionals and their professional organizations to achieve full institutionalization because the status requires changing the fundamental "dichotomous win-lose" nature of the adversarial courtroom so that lawyers can help their clients pursue consensual settlement solutions through ADR.<sup>97</sup> Immediately, a diligent reader could notice the author has again overlooked self-interested motivations for this type of lawyering, instead arguing the culture of the trial structure needs to be changed to accommodate ADR.<sup>98</sup> Moreover, the author assumes that lawyers do not want the current type of court

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<sup>92</sup> Mak, *supra* note 2, at 113-116.

<sup>93</sup> *Id.* at 116.

<sup>94</sup> *Id.* (citing Richard W. Scott, *Institutions and Organizations*, 2nd ed. 51-58 (Thousand Oaks, CA: SAGE, 2001.)).

<sup>95</sup> *Id.* at 157.

<sup>96</sup> *Id.* at 136.

<sup>97</sup> Mak, *supra* note 2, at 136.

<sup>98</sup> *Id.* at 137-145.

proceedings to continue over the alternative dispute resolution options, even though the author's position requires admitting that lawyers would risk sacrificing their financial and social status to change the system.<sup>99</sup> In response, the author suggests that lawyers would take this risk because it presents an opportunity to raise their own social status by being one of the few who provide low-cost ADR representation.<sup>100</sup>

Next Dr. Mak explains how she extracted the factors which dictate lawyer's opinions on ADR, generating six factors: compatibility, advantages, barriers, familiarity, network association and legal culture.<sup>101</sup> Using the method outlined in chapter three, Dr. Mak consolidated the answers from her survey into broader categories, then performed a series of statistic calculations to yield factor loading coefficient values, which indicate the best combination of factors explain any variance from her hypothesized answers.<sup>102</sup>

Addressing the findings on each factor, Dr. Mak first addresses compatibility, or a perceived degree of compatibility between court-based unfair prejudice proceedings and ADR, and found the factor produced a positive correlation supporting ADR adoption by survey respondents.<sup>103</sup>

Next, Dr. Mak highlights her findings of an inverse correlation between a Hong Kong lawyer's awareness of the advantages ADR offers over formal court-based remedies and methods and the likelihood that Hong Kong lawyer will recommend or employ ADR in his career.<sup>104</sup> Dr. Mak suggested the deep-rooted cultural implications of winner-take-all lawyering derives this correlation,<sup>105</sup> however, this could also be explained by lawyer's self-interested desire not to sacrifice a more lucrative line of work in exchange for a change of structure. There is a possibility that lawyers who are aware of the benefits of ADR are also aware of the risk of sham mediation as permitted under the current legal hierarchy. Lawyers, either adversarial or ameliorative, seek to achieve a beneficial outcome for their client, and entering into mediation when it carries the risk of being a waste of the client's time and money may explain such hostility to the practice.

Barriers, or inhibitions associated with ADR that are not associated with court-based shareholder proceedings, generated an unexpectedly positive correlation, suggesting the presence of issues like enforceability of the mediation agreement, and the risk parties will use the ADR hearings to trawl for discovery or delay proceedings, causes lawyers to recommend ADR.<sup>106</sup> The

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<sup>99</sup> Mak, *supra* note 2, at 137-148, 158 (Dr. Mak first acknowledges that the legal profession is monopolized by lawyers, who establish high barriers to entry into the field, then use their monopoly to create normative legitimacy based on the singular status of their own promulgated rules and practices. The exclusivity of the profession was then used to justify high social status and financial compensation for its members).

<sup>100</sup> *Id.* at 147.

<sup>101</sup> *Id.* at 151.

<sup>102</sup> *Id.* at 151, table 6.1.

<sup>103</sup> *Id.* at 168-69

<sup>104</sup> Mak, *supra* note 2, at 169.

<sup>105</sup> *Id.*

author suggests the court's case-by-case case management powers may offer a more consistent means to enforce mediated agreements.<sup>107</sup>

Lawyers familiar with the ADR process are more likely to employ ADR to help their clients, with a significant margin of support associated with the mitigated inequality imposed on the smaller party when their attorney was familiar with ADR processes.<sup>108</sup>

Professional network affiliation with ADR presented inconclusive evidence towards or against individual practitioners utilizing ADR, and the author could not conclusively determine whether Hong Kong lawyers were capable or incapable of acting in accordance with the friendlier notions of ADR proceedings.<sup>109</sup>

Lastly, a legal certainty that minority shareholders will receive judicial relief does not affect legal professional's opinions of ADR and if they would be more or less likely to employ it as a result.<sup>110</sup>

#### IX. INNOVATIVE APPROACHES TO THE FUTURE CODIFICATION OF ADR FOR SHAREHOLDER DISPUTES IN HONG KONG: BORROWING MODELS FROM THE UNITED KINGDOM, NEW ZEALAND, AND SOUTH AFRICA.

The penultimate chapter of the book harkens back to mimetic legitimacy<sup>111</sup> to fill the lack of research into how to use policy to institutionalize ADR in shareholder dispute resolution further. Dr. Mak does this by analyzing the legal treatment affected on ADR by three other common law countries, the United Kingdom, Singapore, and South Africa. The analysis creates three policy suggestions, derived respectively from one per country: 1) a company law rule that permits the parties to include an arbitration clause in the articles of association of the company, thereby assuring all shareholder disputes are subject binding arbitration, 2) mandatory ADR provisions included in the national company law, and 3) issuing a voluntary company law which recommends companies use ADR to resolve shareholder disputes and requires disclosure of how the company addressed said disputes.<sup>112</sup>

The author adapted these findings to accommodate the purely voluntary nature of Hong Kong ADR proceedings and suggested that future studies could seek out more law, or potentially original suggestions as well.<sup>113</sup> The same was done as it pertains to subject matter inarbitrability,

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<sup>106</sup> Mak, *supra* note 2, at 171.

<sup>107</sup> *Id.* at 171, 172.

<sup>108</sup> *Id.* at 173.

<sup>109</sup> *Id.* at 174.

<sup>110</sup> *Id.* at 175.

<sup>111</sup> Mak, *supra* note 57, at 51-53.

<sup>112</sup> *Id.* at 182.

<sup>113</sup> *Id.*



which the author determined would be a non-issue as an expression of contract freedom in Hong Kong.<sup>114</sup>

## X. CONCLUSION

Dr. Mak wrote *Alternative Dispute Resolution of Shareholder Disputes in Hong Kong: Institutionalizing its Effective Use*, to examine and offer potential means to legitimize ADR in unfair prejudice proceedings.<sup>115</sup> The book offers a comprehensive history of the use of ADR in Hong Kong business, an introduction and explanation for numerous sociological examination methods and standards, and finally concludes that there is no current consensus surrounding the use of ADR in shareholder disputes. In offering her theories surrounding the lack of consensus, Dr. Mak considers and discusses numerous possible explanations, but consistently fails to measure the possible influence self-interest, both on the part of the lawyer and the client, may have on the pre-institutionalized status of ADR. Regardless, she still offers numerous and valid mechanisms to advance the use of ADR, each of which she designs to suit the unique nature of the Hong Kong economy properly. Her final conclusion is that the judiciary, legislature, and the professional legal sphere must all work to encourage the use of ADR before the practices gain more legitimacy, and she invites future studies to better explain the best means to achieve that end.

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<sup>114</sup> Mak, *supra* note 2, at 182.

<sup>115</sup> *Id.* at 216.