Insolvency & Restructuring

Green Light for Liquidators to Assign Equitable Interests in Debt Recovery Action to Litigation Funding and Recovery Agent

Introduction

It is not uncommon for liquidators to identify actionable claims when looking into the affairs of a winding-up company, however, it may not always be feasible to pursue such claims either because the winding-up company lacks sufficient funds or there are high uncertainty in the chance of successful recovery.

The inherent difficulties and limitations to pursue these claims were identified as business opportunities by litigation funding and recovery agent. While the liquidators lack the necessary funds to pursue a substantial claim, a third party who had no financial interest is prepared to step in and fund the potential claims in return for a share of the proceeds if the actions were successful. Such arrangements were previously known to amount to maintenance and champerty which were crimes in Hong Kong.

The position changed since the Court of First Instance ruling in Re Cyberworks Audio Video Technology Ltd. It confirmed that the assignment of a cause of action by liquidator was an exception to the prohibition on maintenance and champerty. In other words, liquidators are permitted to enter into an agreement with a third party for the latter to pursue the claims in return for a commercial gain on successful recovery. In this article, with reference to the recent court decision in Remedy Asia Limited v Yick Shing Contractors Limited, we shall discuss relevant principles for liquidators to assign equitable interests only in debt recovery action to litigation funding and recovery agent.

Remedy Asia Limited v Yick Shing Contractors Limited

Background

In the Remedy Asia case, True Light Civil Contractors Limited (“TL”) was wound up by court in 2006. The appointed liquidators (“Liquidators”) have decided to assign debts due to TL (the “Indebtedness”) under 2 contracts (“Contracts”) made with Yick Shing Contractors Ltd (“Yick Shing”) to Remedy Asia Limited (“Remedy Asia”). Remedy Asia is in the business of litigation funding and recovery. Leave was granted by the Court on 11 October 2011 for the

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1 HCCW 1113/2002
2 HCCT 4/2012
Liquidators to enter into a deed of assignment (“Deed”) with Remedy Asia. The Deed contains, *inter alia*, the following terms:

1. Remedy Asia may only settle the legal proceedings upon terms acceptable to TL;
2. Remedy Asia undertakes to bear all the costs and expenses of seeking recovery of the Indebtedness by legal proceedings, negotiations or settlement; and
3. Remedy Asia has to pay TL 55% of the net recovery from the proceedings and the balance of the recovered sum shall vest in Remedy Asia only after it has paid that 55% to TL.

Accordingly, Remedy Asia, the Plaintiff, commenced proceedings against Yick Shing, the Defendant, for a sum of around HK$40 million as the outstanding payments due under Contracts.

**First opposition from the Defendant**

The Defendant attempted to strike out the Plaintiff's claim by alleging that the Deed constituted champerty and/or maintenance and was accordingly void or unenforceable. Further, the legal owner of the debt was not a party to the action.

On 26 June 2014, the Court ruled that the Deed arrangement fell within “access to justice”, one of the established exceptions to the law of champerty and maintenance. Therefore, the arrangement was not prohibited. The Court further ruled that TL acting through the Liquidators shall be joined as a party to complete the title to sue and thus the action was stayed until TL was formally joined as a party.

**Second opposition from the Defendant**

In accordance to the previous judgement, the Plaintiff applied on 4 August 2014 to join TL as the proposed 2nd Plaintiff. The joinder was again opposed by the Defendant. The Defendant alleged, amongst other things, that since the Deed was not an absolute assignment, Remedy Asia has no legal nor equitable interest in the Indebtedness after the signing of the Deed. Further, Remedy Asia’s interest was only limited to 45% of the Indebtedness, which was contingent upon the recovery of the Indebtedness and the paying of 55% of the net recovery to TL.

The Court found that before making the required payment to the Liquidators, Remedy Asia has an equitable interest in the Indebtedness under the Deed. Further, in light of the Defendant’s defence and counterclaim, the parties’ claims cannot be determined unless TL as the holder of the legal interests was joined. As the Defendant’s other grounds for opposition against the joinder also failed, the application was granted.
Implications

Despite the fact that the Deed is not an absolute assignment, the Court has accepted that the arrangement under the Deed falls into the exception of the law of champerty and maintenance. Further, the Court has clarified that even though an assignment is contingent upon fulfilling several other conditions, the equitable interest in the debts is vested in the litigation funding and recovery agent. It transpires that an absolute assignment to the litigation funding and recovery agent is not a must. This would allow flexibilities for the liquidators to formulate their deals with the litigation funding and recovery agent.

Having said that, liquidators should also take note that if only equitable interest is assigned to the litigation funding and recovery agent, the winding-up company should also be joined as the Plaintiff in the claim. It is important to identify all the necessary plaintiffs in the claim to avoid wasting costs on further amendments and dealing with the oppositions from the defendants.

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Important: The law and procedure on this subject are very specialised and complicated. This article is just a very general outline for reference and cannot be relied upon as legal advice in any individual case. If any advice or assistance is needed, please contact our solicitors.

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