ONC Lawyers
柯伍陳律師事務所

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ONC Corporate Disputes and Insolvency Quarterly

Dear Clients and Friends,

This special newsletter aims to regularly update practitioners on important and noteworthy cases in the areas of corporate disputes and insolvency in Hong Kong, the UK and other common law jurisdictions. In this issue, we have highlighted:

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Our selection of cases and our analysis of them may not be exhaustive. Your comments and suggestions are always most welcome. Please feel free to contact me at ludwig.ng@onc.hk

Best regards,

Ludwig Ng
Partner, Solicitor Advocate
ONC Lawyers

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Corporate Insolvency Cases

1. A contributory (as opposed to a creditor) petitioning for the winding-up of a company should normally show a "tangible interest" in the assets of the company or a 'need for investigation', which entitles him to ask for the winding up of the company

Haw Par Pharmaceutical Holdings Pte. Ltd v Hua Han Health Industry Holdings Ltd [2019] 4 HKLRD 286

In the October issue of ONC Corporate Disputes and Insolvency Quarterly 2019, we discussed the Court of First Instance decision in *Cypress House Capital Ltd v Hua Han Health Industry Holdings Ltd* [2019] HKCFI 1826, in which Coleman J made order for the substitution of Haw Par Pharmaceutical Holdings Pte Ltd ("**Haw Par**") as the petitioner in a petition to wind up Hua Han Health Industry Holdings Ltd (the "**Company**") and the appointment of provisional liquidators for the Company. The Company applied for leave to appeal against the orders. Coleman J refused leave to appeal. The Company renewed its application before the Court of Appeal, arguing that, *inter alia*, the Judge erred in law in holding that the need for investigation alone was sufficient to justify a winding-up order, even on a contributory's (as opposed to a creditor's) petition.

A contributory petitioning for the winding-up of a company must show a "tangible interests" in the assets once the matter came to trial, which entitle him to ask for the winding up of the company. However, such tangible interest, the Court of Appeal (Lam VP and Kwan VP) held, are not limited to a surplus for distribution of assets amongst shareholders.

The Court of Appeal noted that this was the very preliminary stage of the winding-up proceedings and there was no reason why Haw Par would not be able to show clearly a tangible interest at trial. The Company's listed status was a valuable asset that could be realised on liquidation. The fact that the Company had no liquid funds to pay its debts did not mean there would be no surplus or no substantive benefit accruing to shareholders on liquidation: *Re Commercial and Industrial Insulations Ltd* [1986] BCLC 191; *Ng Yat Chi v Max Share Ltd* [2001] 1 HKLRD 561.

On the facts at the current stage, the Court of Appeal held that the present case is plainly not a case where the petitioner was required to produce sufficient evidence at the preliminary stage that the investigation of the Company's affairs was likely to produce a surplus. Nor was it one where the petitioning contributory had failed to demonstrate a tangible interest or could only rely on the need to investigate. The Court of Appeal refused leave to appeal.

2. Relevant factors that Court will take into account in giving retrospective sanction

Re Moulin Global Eyecare Trading Ltd (in liquidation) [2019] 4 HKLRD 643

The Company was wound up on 5 June 2006. On taxation of the liquidators' bill of costs dated 27 August 2013 of approximately HK$3.3 million, the Master taxed the bill on the basis that the liquidators' fees had not been approved by the COI nor paid out of the Company prior to the disbanding of the COI. As a result, the liquidators' bill was taxed down to approximately HK$1.16 million.

The liquidators then appointed Messrs. DLA Piper Hong Kong (the "Firm") to advise them and successfully applied to set aside the order nisi and 90% of the original sum was allowed. The Official Receiver refused the liquidators' application to uplift funds from the Company's liquidation account to settle the Firm's taxed bill of costs as the Firm's appointment had not been sanctioned by any COI or the Court. The liquidators then sought the Court's retrospective sanction of the appointment of the Firm.

It was held that the Court had power under section 200(3) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32) and its inherent jurisdiction, in a proper case, to give retrospective sanction to a liquidator's appointment of solicitors to assist him in the performance of his duties. Relevant factors which warrant the court's exercise of its discretion include whether the decision is for the benefit and in the best interests of the creditors and/or liquidation; whether the resultant expenditure was necessary and reasonable; and whether the relevant agent's fees would be subject to the court's scrutiny through the normal taxation of fees in liquidation.

On the facts, the Court granted the retrospective sanction of the Firm's appointment. The Official Receiver did not oppose the application.

3. The requisite intention to gift must be proved to establish transaction at undervalue on the basis of gift

Ho Man Kit v Sure Lead Ltd [2019] HKCFI 2914

On 3 May 2018, Mr Sonu Shailesh Mehta ("**Mr Sonu**"), the sole shareholder and director of Auragem Company Limited ("**Auragem**"), executed a written record of sole director to call an extraordinary general meeting to have Auragem wound up voluntarily. On 24 May 2018, Auragem was voluntarily wound-up pursuant to a special resolution passed by Mr Sonu and the First Creditors' Meeting. Ho Man Kit and Kong Sze Man Simone were appointed the joint and several liquidators of Auragem (the "**JSL**").

An examination of the bank statements and transfer advices of Auragem revealed that five days after the written record of sole director was executed, two transfers in the total sum of US$180,400 (the "**Money Transfers**") were paid to Sure Lead Limited ("**Sure Lead**") from Auragem's bank account.

Upon enquiry made by the JSL, Sure Lead provided an invoice and claimed that the Money Transfers were made to settle payments due to Sure Lead for the liquidation consulting services it had provided to Auragem (the "**Alleged Service**"). However, Sure Lead was not on the list of sundry creditors in the balance sheet provided by Mr Sonu and no record showed Auragem was indebted to Sure Lead at any material time.

The JSL thus took out an application, by way of originating summons, seeking a declaration that the Money Transfers constitute transactions at an undervalue within the meaning of sections 265D and 266B of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32) ("**CWUMPO**")) on the basis that the Alleged Service provided by Sure Lead did not exist and the Money Transfers should be considered as gifts from Auragem to Sure Lead. Alternatively, the JSL contended that as Auragem was insolvent at the material time, the Money Transfers were unfair preference given by Auragem to Sure Lead within the meaning of sections 266 and 266B of CWUMPO.

Transaction at Undervalue

Insofar as the transaction at undervalue claim is concerned, the JSL relied solely on the gift limb of section 265E of CWUMPO, i.e. that the Money Transfers were a gift to Sure Lead. The Judge held that where it is asserted that the transaction in question is a gift, it must be shown that the debtor intended to make a gift and, in the absence of such intention, it does not suffice that no consideration was received such that the transaction was effectively a gift: *Re Hampton Capital Ltd* [2016] 1 BCLC 374.

In order to constitute a gift, there must have been an intention by the donor to make an immediate present gift; and the gift must be perfected either by delivery of possession or by deed. It must be shown that the donor intends there and then to give the property to the donee: *Young Tin Kin Kenneth v Lau Lan Fong Nancy* (HCA 1545/2004, unreported, 6 September 2006). The JSL, however, did not seek to prove the requisite intention to gift. Thus, the Court held, the JSL's claim for transaction at an undervalue should be dismissed.

Nevertheless, the Court went on to consider whether the JSL could rely on the limb of a transaction on terms that provide for the company to receive no consideration. The Court accepted that there are sufficient materials for the Court to cast doubt on the genuineness of the services allegedly provided by Sure Lead to Auragem. However, without proper pleadings and cross-examination, the Court would not be able to determine the issue of fraud and/or sham transactions made for no consideration on paper. JSL's submission that the Money Transfers were a sham was therefore unsuccessful.

Unfair preferences

The Court accepted that as a matter of fact, the settlement of the invoices through the Money Transfers when Auragem was in fact insolvent means that assets of Auragem have been distributed to Sure Lead prior to Auragem's secured and other unsecured creditors, not in *pari passu* as would have been the case in the usual liquidation process. The Money Transfers hence had the effect of putting Sure Lead in a better position than it would have been in, had the Money Transfers not been made and Sure Lead had been paid in accordance with the statutory fixed priority during the liquidation process.

As to the requisite mental element, i.e. the desire to prefer, the Court found that other than the invoices, Sure Lead did not apply any pressure to secure a payment. In the absence of any credible explanations, the Court agreed that other than a desire to prefer, there is no other plausible explanation as to why only Sure Lead was paid in full and not any other creditors. The Court was satisfied that the Money Transfers were unfair preference and should be paid back to Auragem.

4. Petitioner ordered to pay costs on a common fund basis for failing to explain why a winding-up order was sought in the petition

Wong Wai Tung v Lam Chun Fung and Another [2019] HKCFI 3034

Upon the application of the respondents, the Court struck out the prayer for a winding up order in the Petition. There is no dispute that the petitioner should pay the respondents' costs. The only issue is whether the costs should be assessed on a higher than party and party basis.

Referring to his Lordship's own decision in *Re Sun Light Elastic Limited* [2013] 5 HKLRD 1, Harris J reiterated that "the court will only grant a winding-up order rather than relief under section 168A if there is good reason to do so. … if a winding-up order is to be sought, particularly in the alternative it should only be because the petitioner has a particular reason for doing so. … the petitioner must be able to point to particular matters he is concerned might make a winding-up order the appropriate or only practical relief."

The Petition did not contain any averments explaining why a winding-up order was sought. If a petitioner includes a prayer for a winding-up order, for which he is not able to provide a plausible explanation, and necessarily if the petitioner fails to give any reason at all, the claim for a winding-up order is an abuse and it is appropriate to award costs on a higher than normal basis. The Judge thus ordered the petitioner pay the respondents' costs on a common fund basis with a certificate for counsel.

5. Once privileged, always privileged - legal advice attaching to the documents subsisted notwithstanding the dissolution of the company

Addlesee v Dentons Europe LLP [2019] EWCA Civ 1600

The claimants, a large group of investors, invested in a scheme marketed by a Cypriot company. The scheme closed in 2010 leaving the majority of investors unpaid. The company was dissolved in Cyprus in 2016. As far as any rights relating to the documents had passed to the Crown as *bona vacantia* and the Crown had disclaimed all interest in them 'without either asserting or waiving any legal professional privilege.' The claimants asserted that the scheme was fraudulent and in May 2016 they commenced actions against the defendant solicitors, seeking, among other things, a declaration that the documents in client files held by the defendant solicitors in respect of the company were not protected by legal professional privilege, and an order for disclosure of those documents. At first instance, the master refused to order disclosure, holding that the legal advice attaching to the documents subsisted notwithstanding the dissolution of the company. The claimants appealed.

The English Court of Appeal held that the rationale underlying legal advice privilege was that a person had to be able to consult their lawyers in confidence, and that what was said in confidence would never be revealed without their consent: *R. v Derby Magistrates' Court Ex p. B* [1996] A.C. 487. Legal advice privilege attached to a communication because of the nature of the communication and the circumstances under which it was made. Once established, it remained absolute unless it was waived by the client or someone otherwise entitled to waive it, or was overridden by statute: *Three Rivers DC v Bank of England* [2004] UKHL 48. If an exception were to be made in the case of a dissolved corporation, one would have to consider what other exceptions have to be made. The recognition of exceptions would undermine the policy of certainty that underpinned legal advice privilege.

In the present case, if the right to waive privilege never passed to the Crown, then there was no one who could or would waive privilege. If, on the other hand, the right to waive privilege passed to the Crown, it was clear that the Crown had not waived it. The appeal was dismissed.

Cross-border Insolvency Cases

6. Indonesian bankruptcy proceedings recognized in Singapore

Heince Tombak Simanjuntak and others v Paulus Tannos and others [2019] SGHC 216

The case concerns the recognition of Indonesian bankruptcy proceedings in Singapore. Bankruptcy orders were made against the Respondents on 22 February 2017. The Applicants, who are the receivers and administrators appointed in Indonesia, successfully applied to the Singapore court for recognition of the Indonesian Bankruptcy Orders, and were empowered to administer, realize and distribute the Respondents' property in Singapore. The Respondents applied to set aside the orders granting recognition of and assistance to the Applicants.

Since the UNCITRAL Model Law on Cross-Border Insolvency as enacted in Singapore does not extend to personal bankruptcy orders, the Singapore High Court had to consider the recognition of the Indonesian Bankruptcy Orders on the basis of common law and cases prior to the Model Law's enactment (cases that essentially proceeded on the basis of the endorsement of the modified universalist approach endorsed in the Court of Appeal's decision in *Beluga Chartering GmbH (in liquidation) and others v Beluga Projects (Singapore) Pte Ltd (in liquidation) and another (deugro (Singapore) Pte Ltd, non-party)* [2014] 2 SLR 815).

The Singapore High Court held that recognition should be granted to a foreign bankruptcy order if the following requirements are met:

(a) First, the foreign bankruptcy order is made by a court of competent jurisdiction.

(b) Second, that court must have jurisdiction on the basis of:

  (i) the debtor's domicile or residence; or

  (ii) submission by the debtor to the jurisdiction of the court.

(c) Third, the foreign bankruptcy order must be final and conclusive.

(d) Fourth, no defences to recognition apply.

On the facts, the Court found that:-

(a) the Indonesian Court had jurisdiction on the basis of submission by the Respondents, which was borne out by the evidence which showed that the Respondents were present at various hearings and other sessions.

(b) The Indonesian Bankruptcy Orders were final and conclusive, as the Respondents had failed to show that there was a substantive appeal underway. In any event, an appeal would not necessarily render the Indonesian Bankruptcy Orders non-final, but might be grounds for modifying or staying any recognition order granted pending the resolution of the appeal: *Manharlal Trikamdas Mody and another v Sumikin Bussan International (HK) Ltd* [2014] 3 SLR 1161; *The Irini A (No 2)* [1999] 1 Lloyd's Rep 189.

(c) The Respondents had failed to prove their alleged defences against the recognition of the Indonesian Bankruptcy Orders.

In conclusion, the Singapore High Court granted the Applicants full recognition of the Indonesian Bankruptcy Orders. The Applicants were empowered to administer the Respondents' property in Singapore, save that leave of court should be obtained for transfers of real or immovable property and for the repatriation of any assets out of Singapore.

7. Limits of assistance – it is not open to the assisting court to appoint a different person as the foreign representative

Re Rooftop Group International Pte Ltd and another (Triumphant Gold Limited and another, non-parties) [2019] SGHC 280

The 1st Applicant, Rooftop Group International Pte Ltd is a Singapore incorporated company. It filed for Chapter 11 in the US Bankruptcy Court. The 2nd Applicant is its putative foreign representative. Despite the US worldwide moratorium, one of the 1st Applicant's creditors, Triumphant Gold Limited ("**TGL**") sought by way of originating summons No. 544 of 2019 ("**OS 544/2019**") to enforce a share charge it holds over 44 shares in the 1st Applicant.

The Applicants applied to seek the assistance of the Singapore Court under the UNCITRAL Model Law for:-

(a) Recognition of the US Chapter 11 proceedings as a foreign main proceeding, or alternatively as a foreign non-main proceedings;

(b) The recognition of the 2nd Applicant as the foreign representative of the 1st Applicant; and

(c) A stay of the proceedings against the 1st Applicant, including OS 544/2019.

TGL argued that the US Chapter 11 proceedings should only be recognized as foreign non-main proceedings, and that any assistance granted should not include a stay of OS 544/2019. Further, TGL objected to the 2nd Applicant being the foreign representative as he would not act impartially and would favour the shareholders' interest.

Under the UNCITRAL Model Law, the place of the debtor company's registered office is presumed to be its COMI (center of main interest). The presumption may be displaced if various factors which are ascertainable by third parties, particularly creditors and potential creditors of the debtor company, point to a different location as being its COMI: *Re Zetta Jet Pte Ltd and others (Asia Aviation Holdings Pte Ltd, Intervener)* [2019] 4 SLR 1343.

The Court found that although there were factors in support of the US being the COMI, such as that the 2nd Applicant, being the primary decision maker for the 1st Applicant, is a US citizen, they were not sufficient to displace the presumption in favor of Singapore, which is the place of incorporation. Consequently, the US proceedings are not foreign main proceedings for the purpose of the UNCITRAL Model Law. Assistance would be granted on the basis that the US proceedings were recognized as a foreign non-main proceedings.

Under article 20 of the UNCITRAL Model Law, a moratorium automatically operates upon recognition of a foreign main proceedings. But in respect of foreign non-main proceedings, stays and other orders are granted at the discretion of the court. The Singapore High Court

declined to exercise its discretion to grant a stay of OS 544/2019 which would result in TGL being prevented from enforcing its share charge over shares in the 1st Applicant. The Court found that the moratorium sought was intended to head off any change in control of the 1st Applicant. However, the point of assistance under the Model Law is to ensure the orderly and equitable distribution of assets and to facilitate the process of restructuring wherever possible. It is not intended to protect or preserve a party's position within the company, or to prevent a different view being taken about the direction of the restructuring, or whether restructuring efforts should even be maintained. Thus, the assistance in Singapore cannot be directed to prevent the transfer of shares in the 1st Applicant.

Lastly, in relation to the recognition of the 2nd Applicant as the foreign representative, the Court expressed serious concerns about the 2nd Applicant's fitness. However, the Court found that it is not open to it to appoint a different person as the foreign representative of the 1st Applicant. The appointment of a particular person as the foreign representative is a matter which falls to be determined by the foreign proceedings itself. The wording of the UNCITRAL Model Law suggested that a foreign representative could not be displaced, even if the court was of the view that the interests of local creditors might be better served by having some other person administer or realize the locally-based assets.

8. Hong Kong Court recognized and assisted Mainland liquidators for the first time

Re CEFC Shanghai International Group Limited [2020] HKCFI 167

CEFC Shanghai International Group Limited (the "**Company**") is in insolvent liquidation in the Mainland and has substantial assets in Hong Kong. Following their appointment, the Mainland Administrators discovered the following. The Company's assets in Hong Kong included a claim against its Hong Kong subsidiary, Shanghai Huaxin Group (Hong Kong) Limited ("**HK Subsidiary**"), amounting to some HK$7.2 billion ("**HK Receivable**"). However, prior to the Company's liquidation, one creditor of the Company had obtained a default judgment in Hong Kong and a garnishee order nisi in respect of the HK Receivable to enforce the default judgment. In order to prevent the creditor from obtaining a garnishee order absolute, the Mainland liquidators applied to the Hong Kong Court for recognition and assistance urgently.

It is now well-settled that the Hong Kong court will recognize foreign insolvency proceedings that are collective in nature and are commenced in the company's country of incorporation: *Re Joint Provisional Liquidators of China Lumena New Materials Corp* [2018] HKCFI 276; *Re Joint Liquidators of Supreme Tycoon Ltd* [2018] 1 HKLRD 1120. Provided these criteria are satisfied, the Court may recognize insolvency proceedings opened in a civil law jurisdiction: *Re Mr Kaoru Takamatsu* [2019] HKCFI 802.

Upon the foreign insolvency proceedings being recognised, the Court will grant assistance to the foreign officeholders by applying Hong Kong insolvency law. In the case of liquidators appointed in jurisdictions with similar insolvency regimes to Hong Kong, the assistance may extend to granting orders that give the foreign liquidators substantially similar powers: *Re Joint Liquidators of Supreme Tycoon Ltd* [2018] HKCFI 277.

Harris J was satisfied that the Company's Mainland liquidation is a collective insolvency proceeding, which is demonstrated by the fact that the liquidation proceeding encompasses all of the debtor's assets. Further, his Lordship considered that the powers sought by the Administrators are consistent with Mainland insolvency law and the standard recognition order as set out in *Re Joint and Several Liquidators of Pacific Andes Enterprises* (unrep, HCMP 3560/2016, 27 January 2017) and *Re Joint Provisional Liquidators of Hsin Chong Group Holdings Ltd* [2019] HKCFI 805.

Harris J thus granted the recognition and assistance sought by the Mainland Administrators and held that the garnishee proceedings ought to be stayed as it violated the *pari passu* principle and the principle of collectivity.

This is the first time where the Hong Kong Court recognized and assisted Mainland liquidations. As to the extent to which greater assistance should be provided to Mainland administrators in the future, Harris J commented – "*development of recognition is likely to be influenced by the extent to which the court is satisfied that the Mainland, like Hong Kong, promotes a unitary approach to transnational insolvencies.*"

9. English High Court held that a scheme of arrangement only affects the rights of the creditors of a scheme company in their capacity as creditors, not other rights they have, such as proprietary rights in property

Re Instant Cash Loans Limited [2019] EWHC 2795 (Ch)

Instant Cash Loans Limited (the "**Company**") applied for sanction of a scheme of arrangement between it and its creditors. The scheme contained a provision that would force the creditor landlords to accept a surrender of the Company's lease. The rent liabilities would be replaced with a right to damages for the landlord. The scheme was approved by overwhelming majorities of classes. The issue at the sanction hearing was whether the Court had jurisdiction to sanction a scheme that included a provision compelling creditor landlords to accept a surrender of leases.

The English High Court held that a scheme could not affect a creditor's proprietary rights: see *Discovery (Northampton) Ltd v Debenhams Retail Ltd* [2019] EWHC 2441 (Ch), and also see *Re Lehman Brothers International (Europe) (In Administration)* [2009] EWCA Civ 1161, where the Court of Appeal held that a scheme can only affect the rights of the creditors of a scheme company in their capacity as creditors, not other rights they have, such as proprietary rights in property. Here, the surrender of a lease affected the nature of the landlord's proprietary right, as it changed the landlord's interest in the freehold reversion from one encumbered by a lease to one that was not so encumbered.

In the circumstances, the Judge, relying on the modification provision in the scheme (which allows some provisions to be cut out if they would prevent the scheme from being sanctioned), ordered the relevant provisions be struck out of the scheme and sanctioned the scheme. The surrenders were then effected by separate agreement outside the scheme.

10. In considering whether a scheme of arrangement is propounded for a permissible purpose for the general benefit of the scheme creditors, the Court will take into account the rate of return to scheme creditors and the amount of the restructuring and liquidation expenses

Re Da Yu Financial Holdings Limited (formerly known as China Agrotech Holdings Ltd) (in liquidation) [2019] HKCFI 2531

Da Yu Financial Holdings Limited (formerly known as China Agrotech Holdings Limited) (in liquidation) (the "**Company**") is a Hong Kong listed company incorporated in the Cayman Islands. It has been in liquidation in Hong Kong since 9 February 2015.

Pursuant to leave granted by the Hong Kong court, the Company convened a Scheme Meeting on 5 July 2019 where an overwhelming majority of the Scheme Creditors voted in favour of the Hong Kong Scheme. On 16 July 2019, the Cayman Court sanctioned a parallel scheme of arrangement (the "**Cayman Scheme**"). The Company sought Court's sanction of the Hong Kong Scheme.

The only concern of the Court was the quantum of the liquidators' restructuring and liquidation costs as compared to the rate of return to the Scheme Creditors – save for that, the Court was satisfied to sanction the Scheme. In every case, the question to be asked by the Court is, taking into account all the circumstances of the case, including the rate of return to scheme creditors and the amount of the restructuring and liquidation expenses, whether the relevant scheme is propounded for a permissible purpose for the general benefit of the scheme creditors.

In the present case:

(1) HK$80 million is allocated for distribution to the Scheme Creditors — making a recovery rate of 4.28%;

(2) Restructuring expenses in the sum of approximately HK$49 million have been incurred and;

(3) Scheme costs in the sum of HK$5.87 million are expected to be incurred.

The Court further noted that there was insufficient information or meaningful disclosure for the Court and Scheme Creditors to assess the reasonableness of the restructuring costs and expense.

However, the Court also considered that it would not be just to withhold sanction of the Scheme as the failure of the Scheme would leave the Scheme Creditors with nil recovery. Accordingly, the Court sanctioned the Scheme on the condition that all of the restructuring

and other expenses will be subject to taxation. Any cost savings resulting from the taxation process should be distributed to the Scheme Creditors.

The Judge also expressed some reservation against the usual practice of Hong Kong listed companies using parallel schemes for debt restructuring and considered that such practice was outmoded. The Judge made reference to the Cayman Scheme judgment and echoed the remarks of Mr. Justice Segal on the need for cross-border coordination. The purpose of maintaining parallel schemes is to ensure that the scheme creditors cannot disrupt the smooth operation of the scheme by taking hostile action against the company in its place of incorporation even though Hong Kong is where the preponderance of the company's debts are located. Thus the Judge was of the view that requiring foreign office-holders to commence parallel proceedings is the very antithesis of cross-border insolvency cooperation as a crucial feature of cross-border insolvency cooperation is the recognition of foreign proceedings to avoid parallel proceedings: *Cambridge Gas Transportation Corpn v Official Committee of Unsecured Creditors of Navigator Holdings plc* [2007]1 AC 508 . The Judge concluded that a substantive recognition in the offshore jurisdictions of foreign schemes of arrangement would tie in with the advanced procedural coordination advocated by Mr Justice Segal and that progress in cross-border procedural coordination should march in lockstep with progress in cross-border substantive recognition.

11. Assessing the value of his shares is a proper purpose for a shareholder to seek inspection of the company's documents and accounts, particularly where a long-standing substantial shareholder is seeking to protect his economic interest as a shareholder

Selvaraj (Moorthy) v GMT Industrial Ltd [2019] 4 HKLRD 572

The plaintiff, Moorthy, has been a shareholder of the defendant company since April 1979 and presently holds 10% of the shareholding in GMT. GMT is a family-owned company incorporated to hold a business previously managed by the plaintiff's father, and on his demise by the eldest brother. After the eldest brother died, a dispute arose between the plaintiff and his other elder brother over the management of GMT. In March 2019, Moorthy requested confirmation that GMT's bank accounts had been reactivated and repayment of a HK$1.2 million shareholder's loan and payment of some salary. GMT initially indicated that the sums owing to Moorthy would be paid within four weeks after debts were paid to non-family creditors. However, upon being asked to see the bank statements, GMT denied that it was indebted to Moorthy.

Moorthy then applied under section 740 of the Companies Ordinance (Cap 622) for an order authorizing inspection of GMT's bank account statements from March 2019 in order to investigate what Morrthy described as a genuine belief that its operation of the accounts constituted mismanagement, and to ascertain GMT's cash position to assess the fair market price of his shares which he intended to sell.

There is no question that Moorthy has the necessary *locus standi* to make the application. The issue is whether the application is made in good faith and the inspection is for a proper purpose. The Court held that an application made by a substantial and longstanding shareholder may in and of itself discharge the burden of establishing good faith and proper purpose. Where an applicant seeks inspection to protect his economic interest in the company, this might *prima facie* satisfy the proper purpose requirement. It remained in principle a proper purpose for seeking inspection to enable an applicant to assess the value of his shares, particularly where the possibility of a disposal of that investment was a prospect.

On the evidence, the Court was satisfied that the plaintiff had demonstrated that he had the status to make the application, that it was made in good faith and that the inspection was for a proper purpose, not least because of his substantial and long-standing shareholding but also that he was seeking to protect his economic interest in GMT as a shareholder. Further, the Court took the view that the relatively narrow scope of the application and the limited

documents to which reference was made, identified the appropriate proportionality of the request.

12. Court of Appeal: those who alleged fraud should carry the burden of proof and the proper remedy for a forged transfer is to seek a rectification of the share register and the company is a necessary party to the claim

Ngan Pui Chi and Another v Bao Quan [2019] 4 HKLRD 135

The Defendant advanced two loans to the Plaintiffs on the security of some shares of the 1st Plaintiff in a company formerly called Wealth Blooming (Asia Pacific) Bullion Limited (the "**Company**"). For the purpose of the security, the 1st Plaintiff executed undated bought and sold notes in respect of the pledged shares. The Plaintiffs defaulted on the repayments and the shares were transferred to the Defendant. However, the 1st Plaintiff claimed that her signature on the instruments of transfer was forged. After trial, the Judge found in favor of the Plaintiffs, finding that the Defendant had not discharged the onus of proving the impugned documents. The Judge ordered, among other things, that the Defendant deliver up the shares back to the 1st Plaintiff. The Defendant appealed.

Allowing the appeal, the Court of Appeal held that the onus was on the Plaintiffs, rather than the Defendant, to prove the forgery. The Plaintiffs had not discharged that burden. Citing *Nina Kung v Wong Din Shin* (2005) 8 HKCFAR 387, the Court of Appeal emphasized that inference of fraud or forgery could not be reached by conjecture. Without a reasonable foundation for an inference to be drawn, one could not elevate the rejection of the defence's evidence or the defence's case or failure to dispel suspicious circumstances as proof of such serious allegations.

Further, the Court of Appeal held that even if forgery had been established, the prayer for relief in the form of a "return" or "delivery up" was not properly formulated. Shares were choses in action. A shareholder had a bundle of rights in the company and the company only recognised his status by reference to the share register. Upon a transfer, the company issued a new share certificate in favour of the new shareholder. Thus, the proper remedy for a forged transfer was to seek a rectification of the share register. The company was thus a necessary party to the claim: *Barton v London & NorthWestern Railway Co* (1888) 38 Ch D 144.

13. Singapore Court of Appeal: discount for lack of control would typically apply where the buyout of a minority shareholding was made pursuant to a consent order in the absence of any finding on the issue of minority oppression

Liew Kit Fah and others v Koh Keng Chew and others [2019] SGCA 78

In the July issue of ONC Corporate Disputes and Insolvency Quarterly 2019, we discussed the Singapore High Court decision in *Koh Keng Chew & Ors v Liew Kit Fah & Ors* [2018] SGHC 262. The minority shareholders of the Samwoh group of companies ("**Samwoh Group**") brought an unfair prejudice action under section 216 of the Singapore Companies Act against the majority shareholders. Prior to trial, the parties compromised and recorded a consent order (the "**Consent Order**") agreeing that the only issue to be determined at trial was whether the majority shareholders were to purchase the minority shareholders' shares in the Samwoh Group or vice versa. The Consent Order also recorded that the majority shareholders would not admit to liability for any of the alleged acts of oppression. The parties could not agree on whether the value of the minority shareholders' shares should be discounted. The Judge at first instance directed that discounts were not to be applied to the valuation of the minority shareholders' shares. The majority shareholders appealed.

The minority agreed that the Judge at first instance was wrong to treat the buy-out order as having been made under section 216(2). However, the minority did not agree that the circumstances of the case warranted an application of the discounts. Further, the minority considered that the precise jurisdiction of the court to make a buy-out order where an oppression action had been compromised under a consent order was not fully resolved and would have to be addressed in an appropriate future case.

The Court of Appeal, by a majority of two to one, allowed the appeal. It was held that the High Court was wrong to have proceeded on the basis that the minority shareholder respondents had successfully established a case of minority oppression against the appellants. This was incorrect because it was clear from the statutory text that the court's power to order a buy-out of shares under section 216(1) of the Singapore Companies Act arose only where oppression had been established. The Consent Order had recorded parties' agreement to dispense with the issue of liability for minority oppression and the Judge had accordingly not made any finding in that regard. There was therefore no proper legal basis to invoke the court's power to order a buy-out of shares under the statutory oppression regime.

Whether the relevant discounts (i.e. discounts for lack of control/marketability) ought to apply depend on whether the respondents could be treated as willing sellers of their shares in the Samwoh Group. For this purpose, the court will look at whether the minority shareholder's interests had been unfairly prejudiced by the majority's conduct, which thereby made it no

longer tolerable for him to retain his interest in the company. In light of the Consent Order as well as the absence of any finding on liability for minority oppression, the respondents were to be treated as willing sellers of their shares under the buy-out order for the purpose of ascertaining whether the relevant discounts ought to apply.

In relation to the discount for lack of control, the Court of Appeal noted that in the context of a buyout of a minority shareholding pursuant to a consent order where the seller was to be treated as akin to a willing seller, this discount would typically apply. The respondents argued that this discount should not apply because there was no question of lack of control given that the appellants had a majority of the shares and would after the purchase collectively own 100% of the shares. The Court of Appeal rejected this argument, holding that the respondents were not a monolithic majority shareholder which would vote in support of each other at all times, and instead comprised disparate individuals who held a majority of the shares and were majority shareholders only for the purpose of this case.

As to whether the discount for lack of marketability should be applied, the Court held that it was industry specific and was therefore a matter appropriately left for the valuer to determine according to his expertise.

Bankruptcy Cases

14. An application for a non-commencement order under the Bankruptcy Ordinance (Cap 6) should be made *inter-partes*

Re Cai Sui Xin [2019] HKCFI 2547

The trustees sought an order pursuant to section 30AB of the Bankruptcy Ordinance (Cap 6) for a non-commencement order. If approved, the relevant period of bankruptcy will be treated as not commencing to run until the bankrupt complies with the relevant terms specified by the Court in the non-commencement order. The Judge was satisfied that the substantive requirements of the Ordinance were met. However, there was a procedural irregularity in that the trustees, in the first instance, applied for such order *ex parte* by way of a report. Upon directions from the Court, the trustees filed an affirmation and summons for the purpose of the application, which however were more than 6 months after the date of the bankruptcy order as prescribed by section 30AB(2)(a).

G Lam J emphasized that an application for a non-commencement order should not, generally speaking, be made *ex parte*, as it has a serious impact on the length of the bankruptcy. However, his Lordship agreed that the incorrect manner in which the application was initially made within time (i.e. by a report filed *ex parte*) is a mere formal defect and irregularity which has not caused any substantial injustice to the bankruptcy or anyone else, and may be waived under section 124(1) of the Ordinance and rule 203 of the Bankruptcy Rules (Cap 6A): *Re Dias-Azedo* [2010] 5 HKLRD 474; *Ma Wing, Michael v Fong Sze-ming* [1988] 1 HKLR 354. The Judge thus granted the order sought.

15. Bankruptcy petition dismissed as the creditor failed to do all that was reasonable for the purpose of bringing the statutory demand to the debtor's attention and to cause personal service of the demand to be effected

Re Luo Xing Juan Angela [2019] HKCFI 2674

The debtor was a tenant of the creditor. As the debtor failed to pay rent, the creditor brought proceedings against her in the District Court, seeking among other things vacant possession. The creditor succeeded in the action and the debtor was ordered to pay costs of the creditor.

On 8 November 2017, the creditor issued a statutory demand to the debtor requiring payment of, *inter alia*, the taxed costs, together with taxing fee and interest on the taxed costs, totaling HK$182,214.56. On the same date, the creditors' solicitors attempted unsuccessfully to serve the statutory demand on the debtor personally at an address in Hung Hom (the "**Address**"). They also sent the statutory demand to the Address by ordinary post, but it was not stated in the affirmation of service whether this was returned or not. Other attempts were made, but the creditors' solicitors were not able to find the debtor at the Address.

On 21 January 2019, a Master gave leave for the creditor to file a petition against the debtor. The bankruptcy petition was issued on 11 March 2019 and served personally on the debtor on 19 March 2019. The debtor opposed the bankruptcy petition, contending, among other things, that the service of the statutory demand was irregular.

Under rule 46(2) of the Bankruptcy Rules (Cap 6A), a creditor has to do all that is reasonable for the purpose of bringing the statutory demand to the debtor's attention and if practicable in the particular circumstances, to cause personal service of the demand to be effected. If a creditor had not been able to serve the debtor at the address or addresses which he has in his records but has other information or other means available which might enable him to obtain an address for service, … he should make use of them, where it is reasonable to expect him to do so, with a view to bringing the statutory demand to the attention of the debtor: *Re Pang Mei Lan May* [2015] 1 HKC 319.

The Court found that there was a problem with the service of the statutory demand. The evidence indicated that the creditor should have known that the debtor had not been living at the Address for a very long time. Further, the Court found that the creditor had the debtor's mobile phone number. However, none of the affirmations of service referred to any telephone calls having been made or explained whether the telephone number had been used for the purpose of arranging service and, if not, why not. The Judge concluded that the creditor had not done all that was reasonable for the purpose of bringing the statutory demand to the debtor's attention and to cause personal service of the demand to be effected. There is no

evidence of any attempt to contact the debtor by telephone so as to obtain an address for service or make an appointment for service or otherwise to inform her of the statutory demand such as by sending a copy to her phone so as to bring it to her attention.

In view of the creditor's failure to serve the statutory demand in accordance with the statutory requirements, the Court dismissed the petition and ordered the creditor to pay the debtor her costs of the petition.

16. To prove a debtor has carried on business in Hong Kong, it is not enough to show that a person is running his company's business even though he is the sole beneficiary shareholder and in complete control. There must be some evidence activities on the part of the debtor over and above those attributable to the company to show that the debtor has carried on business of his own

Re Chen Mei Huan also known as Liu Chen Mei Huan also known as Liu Mei Huan Chen [2019] HKCFI 3028

Venetian Macau Ltd presented a bankruptcy petition against Madam Chen Mei Huan based on an outstanding judgment debt exceeding HK$117 million. The judgment debt was not disputed by Madam Chen. However, she contended, among other things, that the court has no jurisdiction under section 4 of the Bankruptcy Ordinance (Cap 6) to make a bankruptcy order against her.

Section 4 of the Ordinance sets out the conditions, in terms of the debtor's connection with Hong Kong, that must be satisfied for the court to have jurisdiction to entertain a bankruptcy petition against him or her. The only ground now relied upon by the petitioner is s.4(1)(c)(ii), namely, that the debtor, "at any time in the period of 3 years ending with [the day on which the petition was presented] — … (ii) has carried on business in Hong Kong".

It is well established that this condition is not satisfied by showing merely that a person is running his company's business even though he is the sole beneficiary shareholder and in complete control: *Re Kok Hiu Pan, ex parte Wing Lung Bank Ltd* [2002] 3 HKLRD 20. This follows from the fundamental doctrine of separate legal personality of a company. There must be some evidence activities on the part of the debtor over and above those attributable to the company to show that the debtor has carried on business of his own: *In re Clark, ex parte Pope & Owles* [1914] 3 KB 1095.

The Court found that Madam Chen has been, in a general sense, a businesswoman. She and her husband Mr. Ng each held one of two shares in Silver Faith Holdings Ltd, a Hong Kong company, which held a few subsidiaries that in turn held a number of properties in Hong Kong. The evidence, the Court found, when viewed in its totality, falls short of what would be needed to establish that Madam Chen had carried on business in Hong Kong during the relevant period, namely, the three years ending with 21 March 2019. There was little evidence of any activities that Madam Chen carried out that led to the various properties being acquired and held by the companies in question. The injection of funding for use by the company, whether as share capital or shareholder's loans, does not without more show that the individual is carrying on her own business.

In the circumstances, the Court concluded that the petitioner has failed to establish jurisdiction for making a bankruptcy order against Madam Chen and for that reason the petition should be dismissed.

17. Singapore High Court: an annulment of bankruptcy order is not conditional upon all debts being proven

Standard Chartered Bank, Singapore Branch v Chua Seng Kiat (Lim Peng Liang David Llewellyn, intervener) [2019] SGHC 240

At the petition of the plaintiff, Standard Chartered Bank (Singapore Brach), Mr. Chua Seng Kia (referred to herein as the "**respondent**") was made bankrupt. Two proofs of debts were filed by the appellant against the respondent (the "**Alleged Debts**"). The respondent subsequently filed an application to annul the said bankruptcy order on the basis that he had paid or secured all debts and expenses of the bankruptcy. He had settled all the respective debts with his creditors but the appellant's Alleged Debts, which the respondent disputed. Nevertheless, the respondent secured the Alleged Debts by furnishing the sum of the Alleged Debts to his solicitors. His solicitors then in turn provided an undertaking as security for the respondent to pay the appellant the owed sums in the event that a court decided that the said sums were respectively due and payable to the appellant.

The appellant objected to the annulment, contending that the bankruptcy order could not be annulled before the Alleged Debts had been proven. The Assistant Registrar dismissed the objection and annulled the bankruptcy order. The appellant appealed.

The Singapore High Court upheld the decision of the Assistant Registrar, dismissing the appeal. Under section 123(1)(b) of the Bankruptcy Act, the court may annul a bankruptcy order if, to the extent required, the debts and expenses of the bankruptcy have been paid or secured to the satisfaction of the court. Further, pursuant to rule 237A of the Bankruptcy Rules, where a debt is disputed, the bankrupt must give such security as to satisfy any sum that may be subsequently be proven due to the creditor. Security may be in the form of an undertaking by a solicitor, payment into count, or a bond with a surety.

Upon a proper interpretation of the statutory provisions, the High Court held that none of them require all debts to be proved before a bankruptcy order could be annulled. Rule 237A only requires the bankrupt to give the necessary security to satisfy the sum relating to the disputed debt. The Court found that the Alleged Debts had been "paid or secured" as required under section 123(1)(b). The Court thus allowed the annulment of the bankruptcy order. Specifically, the Court emphasized a "golden thread that runs through bankruptcy proceedings" – that it will not endeavor to maintain a bankruptcy order when the bankrupt has paid or secured all debts.

18. Court of Appeal warned against debtor's opportunistic attempts to invoke the *Lasmos* approach in the future to stay winding-up/bankruptcy petition by invoking arbitration agreement

Sit Kwong Lam v Petrolimex Singapore Pte. Ltd [2019] HKCA 1220

In the July issue of ONC Corporate Disputes and Insolvency Quarterly 2019, we discussed the Court of First Instance decision in *Re Sit Kwong Lam* [2019] HKCFI 920. In gist, Petrolimex Singapore Pte Ltd (the "**Petitioner**") presented a bankruptcy petition against the debtor Sit Kwong Lam (the "**Debtor**") in respect of a debt of over US$30 million (the "**Debt**"). A bankruptcy order was made against the Debtor by Ng J on 11 April 2019.

The Debtor appealed against the bankruptcy order, raising two broad issues, namely first whether the Debt is covered by an arbitration clause, and secondly, if there is at least a good *prima facie* or reasonably arguable case on the first issue, whether the judge should have exercised his discretion to stay or dismiss the petition on the basis that the Debt is not admitted. Before Ng J, the the Debtor had opposed the petition, and argued the court should exercise its discretion to dismiss and stay the petition, invoking the approach in insolvency liquidation in *Re Southwest Pacific Bauxite (HK) Ltd* [2018] 2 HKLRD 449 ("the ***Lasmos* case**") because the disputed debt ought to be resolved by arbitration.

In the *Lasmos* case, in which Harris J departed from previous authorities at first instance and held that save for exceptional cases, a creditor's petition to wind up a company should "generally be dismissed" where three requirements are met (at §31):

(1) if a company disputes the debt relied on by the petitioner;

(2) the contract under which the debt is alleged to arise contains an arbitration clause that covers any dispute relating to the debt; and

(3) the company takes the steps required under the arbitration clause to commence the contractually mandated dispute resolution process (which might include preliminary stages such as mediation) and files an affirmation in accordance with rule 32 of the Companies (Winding-Up) Rules, Cap 32H, demonstrating this.

The Court of Appeal agreed with Ng J's findings that the Debt is not covered by an arbitration clause. The discretion issue thus does not arise for consideration. Nevertheless, in view of the challenge mounted by the Debtor to the necessity of the third requirement of the *Lasmos* approach, the Court of Appeal made the following observations, to discourage debtors from making opportunistic attempts to invoke the *Lasmos* approach in future. The Court of Appeal noted that this was the second occasion within 2 months that the appeal court was asked to consider the correctness of the approach in the *Lasmos* case – see *But Ka Chon v*

Interactive Brokers LLC [2019] HKCA 873 which was discussed in the October issue of ONC Corporate Disputes and Insolvency Quarterly 2019.

The Court of Appeal considered that it is not necessary that arbitration has been commenced by the time the insolvency proceedings are heard. All that is required of the debtor is that he has taken the steps required under the arbitration clause to commence the process of arbitration, which may include preliminary stages such as mediation, and file an affirmation in accordance with rule 32 of the Companies (Winding-Up) Rules (Cap 32H), demonstrating this. This sensible requirement is to demonstrate to the court that the debtor has a genuine intention to arbitrate and could hardly be considered onerous.

Further, the fact that the debtor has no substantive claim against the creditor is immaterial. It is entirely possible for the debtor to refer the dispute to arbitration and seek a declaration of non-liability in respect of the debt alleged by the creditor.

On the evidence, the Court of Appeal did not consider that the third requirement of *Lasmos* approach is satisfied. The Court found that the Debtor was aware of the requirements in *Lasmos*, as this case was mentioned in the skeleton submissions he filed for the first hearing before the judge on 7 January 2019. However, no mention was made in the subsequent affirmation he filed of any steps taken to commence the process of arbitration. In the skeleton submissions filed for the substantive hearing of the petition on 4 April 2019, the Debtor challenged the need for the third requirement and contended that "all that should be required is that the arbitration clause remains operable and capable of being performed", and "if necessary, [the Debtor] can undertake to commence arbitration within a prescribed period since the arbitration clause is still operable". The Debtor had ample opportunity to take steps to commence the arbitration process. He did not suggest there was any obstacle in taking the necessary steps. The belated and conditional assertion in the skeleton submissions of his counsel can hardly be regarded as indicative of a genuine intention to arbitrate.

The Debtor's appeal was dismissed with costs.

19. Trustees in Bankruptcy found not in breach of their duties to act with reasonable care and skill, as they had limited funding available to them at the time

Lau Chun Ming v Deloitte Touche Tohmatsu (A Firm) [2019] HKCFI 2722

The Plaintiff was the major creditor of Ma Koon Sik ("**Ma**"). Upon the bankruptcy petition presented by the Plaintiff, a bankruptcy order was made against Ma on 30 October 2002. The Plaintiff then entered into a contract with the Defendant (the "**Contract**"), pursuant to which the Defendant agreed that it would arrange its partners Lai Kar Yan Derek ("**Lai**") and Darach E Haughey ("**Haughey**") (i) to seek appointment as the Joint and Several Trustees of the estate of Ma and (ii) to assist the Plaintiff to handle or otherwise deal with the properties of Ma charged to the Plaintiff.

At the 1st general meeting of creditors, with the support of the Plaintiff, Lai and Haughey were appointed Joint and Several Trustees of the estate of Ma ("**1st Trustees**"). The 1st Trustees acted as such from 21 November 2002 to 29 June 2009 when they were removed and replaced by 2nd Trustees. On 28 January 2010, the 1st Trustees successfully obtained an order for release under section 94 of the Bankruptcy Ordinance (Cap 6). Shortly afterwards, the 2nd Trustees were replaced by 3rd Trustees. In the following years, the 3rd Trustees brought 3 recovery actions, which were met with challenges on the ground that they were time-barred. The parties eventually came to a settlement and the Plaintiff received slightly over HK$500,000 from the settlement.

The Plaintiff claimed against the Defendant for breach of an implied term of the Contract for failing to ensure Lai and Haughey would act with reasonable skill and care in their position as the 1st Trustees. The Plaintiff contended that the recovery actions were discovered and/or proceeded with by the 3rd Trustees but were not discovered, followed up, investigated and/or procured with by the 1st Trustees during the nearly 7 years of their trusteeship.

In order for a term to be implied into a contract, the following conditions must be satisfied: *Kensland Realty Ltd v Whale View Investment Ltd & Another* (2001) 4 HKCFAR 381

(1) It must be reasonable and equitable.

(2) It must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it.

(3) It must be so obvious that it goes without saying.

(4) It must be capable of clear expression.

(5) It must not contradict any express term of the contract.

The Court held that the Plaintiff failed to demonstrate why the implied term is necessary to give business efficacy to the Contract or that it must be so obvious that it goes without saying. The Court found that the Bankruptcy Ordinance (Cap 6) already provides a scheme for the supervision and control of trustees in bankruptcy by the creditors and the court: see ss.17, 82, 83, 84 and 96. Having found that the Contract did not contain the implied term, the Court nevertheless went on to consider whether the 1st Trustees had failed to carry out their duties with reasonable care and skill.

The Court agreed with the Defendant that it is not sufficient to simply look at what the 3rd Trustees did years later, with different funding, and in different circumstances, and to assert that it is *self-evident* that those actions and the enquiries that led to them should have been undertaken by the 1st Trustees too. In particular, the Court noted that the 1st Trustees had limited funding available to them and the Plaintiff was unwilling to provide the additional funding requested by the 1st Trustees, while the 3rd Trustees were put in sufficient funds to pursue the recovery actions. The Court concluded that it is not satisfied the 1st Trustees had failed to carry out their duties with reasonable care and skill, as claimed by the Plaintiff. Lastly, the Court held that in any event, no liability, whether on contractual or tortious bases, should be imposed on the 1st Trustees after the Release: see section 94(3) of the Bankruptcy Ordinance (Cap 6) and *In re Munro* [1981] 1 WLR 1358.

The Plaintiff's claim against the Defendant was dismissed.

For enquiries, please contact our Litigation & Dispute Resolution Department:

E: enquiry_cdniq@onc.hk
W: www.onc.hk
T: (852) 2810 1212
F: (852) 2804 6311

19th Floor, Three Exchange Square, 8 Connaught Place, Central, Hong Kong