Disputes highlights briefing – Hong Kong

2019

A look back at the Year of the Dog

Introduction

Over the past 12 months, the courts of Hong Kong have made a number of interesting decisions, many of which we have written about, and which are likely to prove instructive for lawyers in 2019 and beyond.

We summarise below some of the cases and legal developments from 2018 which are particularly noteworthy, as guidance on the Hong Kong courts' current approach to various legal issues.

We have identified five broad themes:

Early dismissal of claims

Regulatory disputes

Interplay between Hong Kong and foreign or mainland jurisdictions

Shareholder activism

Costs

Any comments or queries?

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Early dismissal of claims

In 2018 the Hong Kong courts displayed a noticeable trend of taking a more pro-active role in dismissing defective claims at an early stage. Some of the claims which were struck-out alleged negligence by professional advisors.

1. Company barred from recovering same loss as subsidiaries

In a cautionary tale, a group company and its current liquidators had their claim against the group company's former liquidators struck out under the "no reflective loss" principle. The strike-out was granted on the basis that the group company's subsidiaries had a closer nexus to the relevant loss than the group company. The group company appealed, arguing that it would be unjust to prevent it from making its own claim in the event that its subsidiaries' claim failed. This was rejected.

As a mere shareholder of the wronged company, the group company was not entitled to bring proceedings in its own name against the alleged wrongdoer. The appeal judgment follows other recent case law (see 4. below) which demonstrates that the courts are prepared to dismiss defective claims against professional advisers without trial.

(*Re Wah Nam Group Ltd, HCA 960/2015; Re Wah Nam Group Ltd* [2018] HKCA 687)

2. Mis-selling claim dismissed

The Court of First Instance in *Shine Grace Investment Limited v Citibank NA* confirmed the conventional thinking that a relationship between a bank and a customer does not of itself give rise to a duty of care to advise on the bank's part.

The court dismissed the claimant investor's mis-selling claim against the bank on the basis that neither the terms of the relevant contracts entered into with the bank, nor the circumstances of the case, suggested that there had been any assumption of a duty to advise by the bank. The court also observed that even if the bank had (contrary to the court's finding) assumed a duty to advise and been in breach, the claim would have failed because the sole controlling director of the investor company was a strong-minded individual who would have proceeded with her investment decisions regardless of the bank's advice.

(*Shine Grace Investment Limited v Citibank NA* [2018] HKCFI 1737)

3. More dismissal of "dormant" claims

Defendants should welcome the judgment in *Fiscalink International Ltd v Yiu Yu Sum Alex*, in which the court struck out the plaintiffs' claims against a majority of the defendants on the basis that the lack of progress over many years was an abuse of process warranting the entire action against those defendants to be dismissed. The court's judgment is another first instance example of the court pragmatically applying the relevant principles concerning dismissal for abuse of process – those principles are set out in Court of Final Appeal judgment (*Wing Fai Construction Co Ltd v Yip Kwong Robert* (2011) 14 HKCFAR 935) and their application (in practice) leaves much to the discretion of the case-managing courts.

(*Fiscalink International Ltd v Yiu Yu Sum Alex* [2018] HKCFI 1293, HCA 5913/1997)

4. Flawed claim against solicitors struck out

In defending themselves against a claim for professional negligence brought by a former client, two law firms and the individual solicitor successfully applied to strike out the entire claim against them, with costs awarded on a more generous ("indemnity") basis.

The two related judgments are a salutary reminder of the need for plaintiffs to plead all material particulars, failing which there is a real prospect that their claim could be struck out as plainly defective. A plaintiff in these circumstances (as happened in this case) should not expect a court to allow amendments to cure an inherent defect in a claim. The two judgments, while both first instance, caught the attention of the legal profession in Hong Kong and sent a clear message that flawed claims against professional advisers are liable to early challenge and dismissal without trial.

(*Jim Chiu Yuen v CL Chow & Mackison Chan (a firm)* [2018] HKCFI 154, and *Jim Chiu Yuen v CL Chow & Mackison Chan (a firm)* [2018] HKCFI 215)

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Regulatory disputes

The Securities and Futures Commission (SFC) has been particularly aggressive over the past 12 months in prosecuting potential wrongdoers. The first case discussed below also shows that the SFC will actively pursue investigations into alleged transgressions even if they only have a limited connection to Hong Kong.

1. Lead regulator wins landmark civil lawsuit

The SFC has been using section 213 of the Securities and Futures Ordinance (Cap 571) for some time to secure (among other things) compensation on behalf of counterparty investors to impugned transactions. In a landmark judgment, the Court of Final Appeal confirmed that the SFC's remit under section 213 extends not only to insider dealing involving locally listed securities and regulated trades, but also to contraventions of section 300 – namely, transactions involving shares listed overseas carried out through means of fraud or deception.

(*Securities and Futures Commission v Lee & Ors* [2018] HKCFA 45)

2. Moody's appeal against SFC

In October, the Court of Final Appeal dismissed the credit agency Moody's appeal against the SFC's decision to sanction it for its "Red Flags" report.

The SFC had launched disciplinary action against Moody's in relation to a special comment report which Moody's had published in 2011, entitled "Red Flags for Emerging-Market Companies: A Focus on China". Apparently, more than half of the Mainland companies targeted by Moody's report experienced substantial falls in their share price the day after its publication. In its original decision the SFC concluded that the report contained a number of misleading statements. It fined Moody's HK$23 million and issued a public reprimand. Moody's appealed this decision, arguing that the publication of market reports did not fall within the performance its regulated activity, namely the provision of credit rating services. However, the SFC successfully argued that the publication of market reports did relate to its regulated activity for the purposes of section 193(1)(d) of the Securities and Futures Ordinance (Cap. 571).

Parties should be aware of how broadly the courts will interpret an act as "relating to" a regulated activity. Credit rating agencies should also recognise the high standards of accuracy expected from them before publishing reports to the market.

(*Securities and Futures Commission v Moody's Investors Service Hong Kong Ltd* [2018] HKCFA 42, FACV 6/2018)

3. SFC collective redress: reliance on misstatement in a real but not ideal world

As highlighted in 1. above, the SFC in Hong Kong has been active in using civil proceedings under section 213 of the Securities and Futures Ordinance to seek redress for investors. The recent judgment in *Securities and Futures Commission v Qunxing Paper Holdings Co Ltd* confirmed that the SFC can seek restorative orders not only against parties to impugned transactions, but also against individuals who aid or abet or who are otherwise involved. The High Court judgment is pragmatic and reasoned, and considers a novel issue affecting section 213 restorative orders – common law "reliance" on misstatement and the proportionality of relief for individual investors. This should encourage investors that the SFC will take steps to recover any assets misappropriated through improper transactions.

(*Securities and Futures Commission v Qunxing Paper Holdings Co Ltd* [2018] HKCFI 271)

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Interplay between Hong Kong and foreign or mainland jurisdictions

Hong Kong is a dispute resolution hub of global significance. As such, the approach its courts take to judgments and orders made in other jurisdictions are of keen interest to international observers.

1. Reciprocal enforcement of Mainland and Hong Kong civil judgments

In 2018, the Hong Kong government issued a consultation paper, seeking views from members of the public and interested stakeholders, on a proposed arrangement between Hong Kong and Mainland China for the reciprocal recognition and enforcement of judgments in civil and commercial matters (the proposed arrangement). The proposed arrangement seeks to widen the existing limited scope for the enforcement of Hong Kong court civil judgments in Mainland China and vice versa. The proposals have broad support in principle and reflect the realities of increased commercial interaction between the two jurisdictions within "One Country, Two Systems".

Postscript: On 18 January 2019 the "Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region" was signed between the Supreme People's Court and the HKSAR government.

For the Arrangement to come into force in Hong Kong, local legislation will need to be enacted and (at the time of writing) this is expected to be passed in 2019.

(Consultation Paper on the "Proposed Arrangement between Hong Kong and the Mainland on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters")

2. Cross-border insolvency regime – past and future

In the absence of a statutory corporate rescue procedure, the Hong Kong courts have continued to refine their use of inherent powers to assist cross-border insolvencies.

The United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-border Insolvency is not formally recognised in Hong Kong (unlike in Singapore, which adopted it in 2017). There are similarly no statutory provisions empowering the Hong Kong courts to provide assistance and recognition to foreign insolvency office holders.

The courts, therefore, rely on their inherent power (where appropriate) under the common law principle of "modified universalism" to provide such assistance. Although the application of this principle is not without problems, in recent years the courts have shown some willingness to assist the effective implementation of cross-border insolvency and restructuring regimes. This has given rise to the development of common law recognition and assistance in Hong Kong for cross-border insolvencies.

Some difficulties were illustrated in *Re CW Advanced Technologies Limited* – a case in which the companies judge, for the first time, considered the possibility of recognising and giving assistance in support of the new Singapore insolvency regime in Hong Kong proceedings.

The Proposed Arrangement for reciprocal enforcement between Hong Kong and the Mainland (see 1. above) does not cover corporate insolvency and restructuring or bankruptcy. Therefore, there is no statutory regime for the courts of either jurisdiction to recognise the other's insolvency or bankruptcy proceedings. This is a major hurdle to the recovery of assets across the border between the two jurisdictions.

While the government is planning to introduce legislation to provide for a corporate rescue procedure for Hong Kong, the legislative timetable is uncertain. It is understood that the government is considering conducting a standalone consultation on reciprocal enforcement for cross-border insolvency matters between Hong Kong and the Mainland.

(*Re CW Advanced Technologies Limited* [2018] HKCFI 1705; also see, more recently, *Re China Fishery Group Ltd* [2018] HKCFI 2622)

3. Court allows extra time to resist enforcement of foreign arbitral award

In the long-running Astro v Lippo saga, the Court of Final Appeal granted an application for time to resist the enforcement in Hong Kong of a "New York Convention" arbitral award made in Singapore. This was despite the appellant appearing to have consciously chosen not to resist enforcement of the award in Hong Kong initially, and when the appellant did so, it was over a year late.

This case does not diminish Hong Kong's pro-arbitration credentials. The CFA held that something fundamentally wrong had happened during the arbitration proceedings in Singapore, which meant that it would have been plainly wrong to refuse the appellant more time to apply to set aside the arbitral award. It was also reasonable for the appellant to have chosen to resist enforcement in Hong Kong, rather than to actively try to set aside the award at the seat in Singapore. This indicates that Hong Kong courts will take a holistic approach to requests for extra time, rather than a mechanistic one.

(*Astro Nusantara International B V v PT Ayunda Prima Mitra* [2018] HKCFA 12)

4. Court clarifies admissibility of Mainland court judgment

In *Capital Century Textile Co Ltd v Li Dianxiao*, in determining the admissibility of parts of an earlier judgment of a court in Beijing arising out of criminal proceedings, the High Court analysed the rationale behind the common law principle in *Hollington v F Hewthorn & Co Ltd*. The court clarified that, under Hong Kong common law, the Hollington principle did not prevent the courts from admitting factual evidence (as opposed to judicial findings) referred to in an earlier judgment of another court or tribunal, provided that it is relevant to the civil proceedings in Hong Kong.

(*Capital Century Textile Co Ltd v Li Dianxiao* [2018] HKCFI 729)

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Shareholder activism

Two 2018 court decisions in particular have served to clarify and extend shareholders' rights in disputes. Both should cause investors to take some heart.

1. Qualifying shareholders' access to company records

The decision of the High Court in *Ninotre Investment Ltd v L & A International Holdings Ltd* is an example of the court agreeing to grant a qualifying shareholder access to and inspection of company records using its statutory powers.

Section 740 of the Companies Ordinance (Cap 622) has become an established mechanism for aggrieved shareholders, with legitimate complaints in their capacity as shareholders, to obtain access to and inspection of company records. The outcome in the case is encouraging in respect of the likely consequences for minority shareholder protection and corporate governance generally.

(*Ninotre Investment Ltd v L & A International Holdings Ltd* [2018] HKCFI 2555)

2. Shareholders of a party granted access to pleadings

In *Elliott International LP v Bank of East Asia (No. 2)*, the High Court granted access to pleadings in the case to shareholders of the respondent public company.

The court held that the principle of open justice allowed it to diverge from the default position that third parties should not normally have access to pleadings. Although this was a private dispute, the 1st respondent was a public company and the dispute was of interest to its shareholders generally. Publishing the pleadings would allow the shareholders to better comprehend the details of the dispute without any significant negative effect. Hedge funds (as the plaintiffs were in this case) and other investment funds, particularly activist shareholders, should take note of this decision.

(*Elliott International LP v Bank of East Asia (No 2)* [2018] 4 HKLRD 427)

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Costs

Costs remain an important strategic consideration for any party to a civil claim. In 2018, the Hong Kong courts have clarified their interpretation of some of the existing rules on costs. One of the most significant developments was the introduction of third-party funding for arbitrations (see 2. below).

1. Top court rules on protective costs orders

The Court of Final Appeal in *Designing Hong Kong Ltd v Town Planning Board* confirms that, in deciding whether it is fair and just to grant a protective costs order in public interest litigation, the courts should be apprised of an applicant's financial position.

In the case of a corporate applicant, it is proper to inquire not only into the assets belonging to the company, but also other sources of funding to which it has access. Depending on the circumstances, these could include the financial resources of the directors, shareholders or other supporters of the company. In this case, the Court of Final Appeal dismissed the applicant's appeal of the lower courts' refusal to grant a protective costs order in its favour. Although perhaps of limited comfort to the applicant, the case is the first in Hong Kong in which the courts have extensively set out the relevant legal principles in this regard.

(*Designing Hong Kong Ltd v Town Planning Board* [2018] HKCFA 16)

2. Code for third party funding of arbitrations

The Hong Kong Government issued its Code of Practice for Third party Funding of Arbitration in Hong Kong, in December 2018. This follows on from the relevant legislation which was enacted in June 2017. As a result, from 1 February 2019 arbitrations in Hong Kong can be funded by qualifying third party funders.

3. Court of Appeal clarifies reviews of taxed costs

In *Lam and Lai (Solicitors) v Ho Chun Yan Albert* the Court of Appeal clarified the lower courts' role when reviewing disputes over taxed costs. In doing so, the Court of Appeal appears to have come to a sensible compromise in allowing some costs that had been approved by the taxing master but disallowed by the judge on review.

(*Lam and Lai (Solicitors) v Ho Chun Yan Albert* [2018] HKCA 83, CACV 172/2017)

4. New rates for recoverable costs

The long-awaited increase in the guideline solicitors' hourly rates adopted for party and party taxation in civil proceedings was announced towards the end of 2017. The new rates came into effect on January 1 2018 with the goal of narrowing the gap between the costs incurred by successful litigants and recoverable costs.

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