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Newsletter

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What's inside?

Hong Kong is making headway in having the widest reciprocal enforcement arrangement with the Mainland

Joseph Kwan and Andy Lam

On 22 April 2022, the Hong Kong Government gazetted the Mainland Judgments in Civil and Commercial Matters (Reciprocal Enforcement) Bill (Bill), three years after the Government and the Supreme People's Court entered into 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" (REJ Arrangement).

The Bill has now been introduced into the Legislative Council. Upon its enactment, the Government will make relevant rules for operation of the mechanisms. The REJ Arrangement will come into effect simultaneously in Hong Kong and the Mainland when the relevant implementation mechanisms are in place.

Instead of revisiting the REJ Arrangement (which we have covered in our earlier article), we will summarise here the actual mechanisms and practical implications when the same is brought to life under the long-awaited Bill.

Pro-enforcement mechanisms

The Bill provides two pro-enforcement mechanisms in relation to Mainland and Hong Kong judgments respectively.

The first is the mechanism for registration in Hong Kong of Mainland judgments. A judgment creditor may apply to the Court of First Instance (CFI) to have a Mainland judgment in a civil or commercial matter registered with the CFI on an *ex parte* basis. Subject to certain exceptions, the regime covers both monetary and non-monetary relief. Once registered, the Mainland judgment may be enforced in the same way as if it were a CFI judgment.

To set aside the registration, the person against whom such judgment may be enforced shall apply within the time limit and prove that any of the exhaustive grounds of refusal exists. The grounds upon which registration "must" be set aside include, for example, that the defendant was not summoned to appear in the original Mainland court according to the Mainland law, or the original proceedings were accepted by the Mainland court after proceedings of the same cause of action and same parties were started in the Hong Kong court. A discretionary ground is also available where the proceedings in the original Mainland court were contrary to a valid arbitration or jurisdiction agreement between the parties.

The second is the mechanism for the application of certified copies of and the issuance of certificates for Hong Kong judgments in civil or commercial matters, to facilitate parties in seeking recognition and enforcement of the judgments in the Mainland. Such Hong Kong judgments cover not only the ones handed down by the District Court and higher courts, but also the Competition Tribunal, Lands Tribunal, Labour Tribunal and Small Claims Tribunal.

Implications

The Bill is a big step towards a more comprehensive REJ regime, which is essential to the growing economic integration between Hong Kong and the Mainland. The existing regime under the Mainland Judgments (Reciprocal Enforcement) Ordinance (Cap. 597) (MJREO) has limited application, as it covers only monetary judgments and contracts which provide for the exclusive jurisdiction of the courts in Hong Kong or the Mainland. The passing of the Bill will mean that Hong Kong is the only place that has such a wide REJ arrangement with the Mainland. This should encourage parties, especially foreign parties that are used to the common law system, to choose Hong Kong as a venue for dispute resolution.

Some Mainland judgments are expressly excluded for registration in the Bill, such as corporate insolvency, debt restructuring and personal insolvency, succession of the estate of a deceased person, and excluded matrimonial or family matters. That said, there are complementary mutual legal assistance arrangements in aid of the disgruntled parties to the proceedings, among which include the Matrimonial and Family Cases (Reciprocal Recognition and Enforcement) Ordinance (Cap. 639), which just came into force early this year.

Whilst the Bill embodies a more uniform approach for judgment creditors or debtors to pursue or resist enforcement of Mainland judgments in Hong Kong, dissimilar language has been used in the Bill as compared to the Foreign Judgments (Reciprocal Enforcement) Ordinance (Cap. 319) or MJREO. This means that previous case law on the MJREO will not apply directly to the interpretation of the new legislation. The ambit and meaning of the new provisions will be subject to interpretation by the courts once the Bill has been enacted.

Further development in Hong Kong-Mainland cross border insolvency

Richard Hudson and Judy Wu

Since the signing of a record of meeting concerning mutual recognition of and assistance to insolvency proceedings between the courts of Mainland China and Hong Kong in May 2021, there have been a number applications for letters of request to be issued by the Hong Kong Court to the Bankruptcy Court of the Shenzhen Intermediate People's Court. The recent case of *Re Hong Kong Fresh Water International Group Limited (In Liquidation)* [2022] HKCFI 924 featured another application for recognition and assistance by Hong Kong liquidators in Mainland China, but this was the first application for a letter of request to be issued to the Shanghai No. 3 Intermediate People's Court (Shanghai Court).

The Cooperation Mechanism provides a procedure for mutual recognition of insolvency processes and office holders by the High Court of Hong Kong and the Intermediate People's Courts in three pilot cities: Shenzhen, Shanghai and Xiamen.

The two important documents under the Cooperation Mechanism are (i) the Record of Meeting of the Supreme People's Court and the Government of the Hong Kong Special Administrative Region and Mutual Recognition of and Assistance to Bankruptcy (Insolvency) Proceedings between the Court of the Mainland and the Hong Kong Special Administrative Region" (Record of Meeting), and (ii) the Supreme People's Court's "Opinion on taking forward a pilot measure in relation to Recognition and Assistance to Bankruptcy (Insolvency) Proceedings in the Hong Kong Special Administrative Region" (SPC Opinion). Our article, Hong Kong's first application for recognition of and assistance to liquidators in Mainland China, set out details of the application requirements and procedures.

Background

Hong Kong Fresh Water International Group Limited (Company) was incorporated in Hong Kong. It is part of a group headed by Ozner Water International Holding Limited (Parent), which is incorporated in Cayman and listed in Hong Kong. The Company's main assets in the Mainland are its shareholding in subsidiaries incorporated in Shanghai. Both the Parent and the Company are in liquidation in Hong Kong.

The same parties were appointed as liquidators of the Parent on 16 April 2021, and as liquidators of the Company on 27 July 2021 by the Hong Kong Court. There was a pressing need for the liquidators to control the Shanghai subsidiaries, as investigations showed that the management of the Shanghai subsidiaries had apparently diverted the Shanghai subsidiaries' business and continued to use the association with the Parent as a listed entity, whilst ignoring the liquidators' requests for information. The liquidators had to obtain recognition and assistance in the Mainland in order to deal with the Company's substantial assets in the Mainland, especially the Shanghai subsidiaries.

Application for a letter of request

The Honourable Justice Harris referred to his decision in *Re Samson Paper Co Ltd (in Creditors' Voluntary Liquidation)* [2021] HKCFI 2151), which set out the principles governing the grant of a letter of request and the procedure for recognition specified in the SPC Opinion, and held that the granting of a letter of request in the present case was consistent with the principles in the Record of Meeting and the SPC Opinion. In particular, although the Company was not incorporated in Hong Kong, Hong Kong is the centre of main interests of the Company, where the Parent was listed. Further, the Court held that the centre of main interests of the Company had been in Hong Kong for more than 6 months prior to the application being made.

Comments

This is yet another case in which a letter of request has been issued to a Mainland court for Hong Kong liquidators to obtain recognition and assistance in the Mainland. We anticipate that, as parties grow used to the procedure, there will be more applications for letters of request to the Shanghai Court, and eventually the system will be opened up to courts beyond the three pilot cities.

Court orders insider dealers to pay HK$12.9 million to 63 investors in civil proceedings commenced by the SFC under s.213 of SFO

Peter So and Victor Wong

On 9 November 2021, the Court of First Instance declared that three individuals committed the offence of insider dealing in the shares of TeleEye Holdings Limited (8051.HK) (currently known as CircuTech International Holdings Limited) (TeleEye) involving a total profit of close to HK$13 million (Profit), which was paid into Court in full before trial pursuant to an undertaking given by the 2nd and 3rd Defendants.

On 14 February 2022, the Court ordered that the Profit be paid to 63 investors who sold TeleEye's shares to the 2nd and 3rd Defendants from 29 February 2016 to 12 April 2016 (Relevant Period) via the court-appointed administrators.

Background

On 14 April 2016, TeleEye announced a takeover by Foxconn (Far East) Ltd. (Foxconn), a wholly owned subsidiary of a Taiwan listed company, Hon Hai Precision Industry Co Ltd., which acquired a 50.07% stake in TeleEye (Takeover). The Takeover also involved an unconditional cash offer at HK$0.55. Upon resumption of trading on 15 April 2016, the share price surged 71%, to close at HK$0.99 from the pre-suspension close.

The 1st Defendant was TeleEye's representative in the discussion with Foxconn's representatives on the intended Takeover. Amongst others, the 1st Defendant had knowledge of the terms of the sale and purchase agreement, the joint announcement and the closing timetable to the Takeover. The 2nd Defendant is the niece of the 1st Defendant. The 2nd and 3rd Defendants got married before the relevant events. All defendants were close to each other.

During the Relevant Period, the 1st Defendant bought TeleEye shares through the 2nd and 3rd Defendants' brokerage accounts. The 1st Defendant was authorised to operate and control these accounts. The 3rd Defendant also acquired some TeleEye shares through his trading account during the Relevant Period. A total of 22.72 million shares, at an average cost of HK$0.4295 per share, were eventually acquired through these accounts.

Between the resumption of trading on 15 April and 20 May 2016, a total of 15.65 million shares at an average cost of HK$1.259 per share were sold resulting in the Profit.

The Securities and Futures Commission (SFC) commenced its investigation in April 2016 and commenced these civil proceedings in September 2016 against the trio under s.213 of the Securities and Futures Ordinance (SFO).

The nature of s.213 proceedings

As held in *SFC v Tiger Asia Management LLC and others* (2013) 16 HKCRAFR 324, s.213 of the SFO provides remedies for the benefit of parties involved in the impugned transactions, including orders that would restore all parties to the transactions to their respective former positions. In such proceedings, the SFC acts not as a prosecutor in the general public interest but as protector of the collective interests of the persons dealing in the market who have been injured by market misconduct. The relief under s.213 of the SFO is entirely free-standing. While the standard of proof is the civil standard, where serious wrongdoing is involved, the inferences must be compelling and the Court should refrain from drawing inferences on a bare or mere balance of probabilities.

The offence of insider dealing under ss.270(1)(a)(i) and 291(1)(a) of the SFO

The essential elements are as follows: (1) a person is connected with a listed corporation (Connection Element); (2) the person has information which he knows is inside information in relation to the listed corporation (Information Element and Knowledge Element); and (3) the person deals in the listed stocks of (a) the listed corporation or their derivatives; or (b) a related corporation of the corporation or their derivatives (Dealing Element).

As regards the Connection Element, the Court clarified that the test of assessing whether a person occupies a position which may reasonably be expected to give him access to inside information under s.247(1)(c) of SFO is an objective one.

As regards the Information Element, the Court reiterated that "specific information", as referred in s.245(1) of SFO, is information which possesses sufficient particularity to be capable of being identified, defined and unequivocally expressed. It is to be contrasted with mere rumour, with vague hopes and worries or with unsubstantiated conjecture. However, what begins as a vague hope or worry may over time acquire sufficient substance and particularity to be properly defined as specific information. Whether and when such a transformation takes place is a question of fact. Further, the fact that details of a proposed transaction (including price) were still under negotiation would not make the information fall outside the meaning of "specific information", if the proposed transaction went beyond the exploratory stage of "testing the waters", mere rumour or "fishing expedition".

Besides, as regards the materiality of the impact on price of listed securities, as referred in s.245(1)(b) of SFO, the Court stated that the test is a hypothetical one. The Court must ask itself whether, had the information been generally known to the investing public on the day the insider traded, it would have been likely to have had a material impact on the company's share price. In this regard, evidence on how investors reacted once the information became public knowledge often provides the answer. However, care must be taken to ascertain whether the investors' response was attributable to the information released, or whether it was attributable to other extraneous events or considerations. The test is applied with reference to the ordinary reasonable investor.

As regards the Knowledge Element, the Court stated that actual knowledge at the time the insider traded is required. It is well established, that actual knowledge includes "blind eye knowledge" or "wilful blindness", which requires a suspicion or belief that the relevant facts do exist (which must be firmly grounded and targeted on specific facts), *and* a deliberate decision to avoid confirmation of the facts in whose existence there is good reason to believe. The test of knowledge is a subjective one. It is established by admission or inference. One has to examine the surrounding circumstances and consider what events occurred before and after the material time to see if they throw any light on what the insider truly knew.

The tipping off offence under s.270(1)(e)(i)

The elements of the tipping off offence are as follows: (1) the person (tippee) has information which he knows is inside information in relation to the listed corporation; (2) the person received the information, directly or indirectly, from a person (tipper) whom he knows is connected with the listed corporation; (3) the tippee knows or has reasonable cause to believe that the tipper held the information as a result of being connected with the listed corporation; and (4) the tippee deals in the listed securities of (a) the corporation or their derivatives, or (b) a related corporation of the corporation or their derivatives.

In the context of the insider dealing, the first and second elements can be inferred from circumstantial evidence, which may include factors such as (1) the tippee's background or previous share trading, (2) his access to information, (3) his relationship with the tipper, (4) timing of contact between the tipper and the tippee, (5) timing of the trades, (6) pattern of the trades; and (7) attempts to conceal either the trades or the relationship between the tipper and the tippee.

Application

The court accepted the SFC's contention that the 1st Defendant was a connected person within the meaning of s.247(1)(d) of the SFO because (1) the 1st Defendant had access to inside information in relation to TeleEye by virtue of her position as a director of Chinese Energy, which is a the holding company of First Top. TeleEye's shares were charged as security for a loan advanced by First Top to TeleEye's former majority shareholder; and (2) the inside information related to a transaction involving both TeleEye and First Top.

The Court found that the 1st Defendant had direct access to all inside information relating to the Takeover, which remained confidential to the parties and not available to the public. Further, on the date when trading of shares in TeleEye shares resumed, its share price rose by 70.7%, while the GEM market only rose by 0.2%. The turnover of TeleEye shares was 138 times the average turnover for the period in question. The above evidence shows that the subject information, if generally known to the relevant investors during the Relevant Period, would have a material impact on TeleEye's share price. There was also evidence showing that the 1st Defendant knew that she could not buy any TeleEye shares through her own securities account. While the trades were put through the 2nd and 3rd Defendants' securities accounts, the 1st Defendant placed almost all buy orders and placed all the sell orders herself. The Court declared that the 1st Defendant committed an offence of insider dealing under ss.270(1)(a)(i) and 291(1)(a) of the SFO.

Insofar as the 2nd and 3rd Defendants are concerned, the Court found that the only reasonable inference drawn was that they were told by the 1st Defendant about the subject information and that they knew that the 1st Defendant was a person connected with TeleEye. Further, the fact that the TeleEye shares were purchased through the 2nd and 3rd Defendants' accounts constituted dealing in TeleEye share. The Court declared that the 2nd and 3rd Defendants committed offences of insider dealing under ss.270(1)(e)(i) and s.291(5)(a) of the SFO.

The Court also declared that all defendants are persons within s.213 of the SFO.

Relief

The Court held that a claim brought by the SFC under s.213 based on insider dealing, in contravention of ss.270 and 291 of the SFO, is a claim founded in tort. Having said that, the Court clarified that the relief which may be granted by the Court is not limited by common law principles governing a claim founded in tort. The Court granted a restoration order, requiring that the Profit together with interest accrued thereon, less remuneration and costs of the administrators, be distributed *pro rata* to 63 investors who sold a total of 22.72 million TeleEye shares to the 2nd or 3rd Defendants during the Relevant Period, to be distributed by the administrators, notwithstanding that the 63 investors had no means of detecting who they were dealing with at the time of selling their shares.

Implications

This case once again demonstrates the judicial attitude and the SFC's approach in ensuring that the consequences of wrongdoing should be met by the wrongdoers and not be borne by innocent investors or the market. S.213 of SFO is a powerful tool for the SFC to protect collective interests of persons dealing in the market who have been injured by market misconduct. It also illustrates that the Court may appoint administrators to facilitate the distribution of wrongdoers' windfalls to innocent third parties.

Key takeaways on the Rental Moratorium under the Temporary Protection Measures for Business Tenants (COVID-19 Pandemic) Ordinance

Carmen Ng and Michelle Wan

The Temporary Protection Measures for Business Tenants (COVID-19 Pandemic) Ordinance (Cap.644) (Ordinance) was passed by the Legislative Council in Hong Kong on 28 April 2022. Its commencement date was 1 May 2022.

The Ordinance aims to provide temporary protection measures for business tenants adversely affected by the COVID-19 pandemic with a rental moratorium for three months starting from 1 May 2022, which prohibits landlords from taking certain actions against tenants of certain premises for failure to pay rent during the period from 1 January 2022 to 31 July 2022.

Key Takeaways

(1) **Effective date**: 1 May 2022.

(2) **Protection Period**: 1 May 2022 to 31 July 2022.

(3) **Relevant Rental Period**: 1 January 2022 to 31 July 2022, see 5 below.

(4) **Premises covered**: Premises used wholly or primarily as "Specified Premises" at the beginning of the protection period (i.e. 1 May 2022).

"Specified Premises" are listed in Part 2 of the Schedule to the Ordinance (as may be amended from time to time), including scheduled premises under the Prevention and Control of Disease (Requirements and Directions) (Business and Premises) Regulation (Cap.599F), such as:

(a) food related business including catering and food business, caterers for schools, dishware washing businesses, fresh food wholesale business;
(b) child care and education including child care centre, kindergarten, private primary day school and private secondary day school, tutorial school, hobby classes;
(c) retail shop including supermarkets;
(d) travel related business including travel agencies, cruise ship businesses;
(e) art and culture including Pop concert organisers, performing arts;
(f) employment agency.

(5) **Prohibited Actions**: Landlords are barred from taking or continuing to take the following actions against tenants of the covered premises for their failure to pay rent during the period from 1 January 2022 to 31 July 2022:

In relation to the recovery of arrears:

(a) deducting outstanding rent from deposit held by the landlord;
(b) demanding the tenant to pay any shortfall in deposit deducted before the protection period in respect of rent due during the relevant rental period;
(c) recovering interest or surcharge on rent arrears.

In relation to enjoyment of the premises:

(d) suspending utility services or other services in relation to the premises;
(e) terminating the tenancy;
(f) exercising right of re-entry or forfeiture.

In relation to the commencement of legal actions:

(g) presenting bankruptcy or winding-up petition against the tenant;
(h) commencing arbitral proceedings against the tenant;
(i) commencing or leving an execution, distress or other legal proceedings against the tenant's property;
(j) making an application under section 670 of the Companies Ordinance (Cap. 622) for a meeting of creditors to be summoned to agree to a compromise or an arrangement in relation to the tenant; and
(k) appointing a receiver or manager over the tenant's property.

(6) **Permitted actions**: Landlords may take action or continue to take action against tenants on a ground other than failure to pay rent during the protection period.

(7) **Rental moratorium ceases to apply in the following situations**:

(a) a written agreement entered into during the protection period in respect of a tenancy with an agreed forbearance in respect of the amount of rent or the time when any rent is payable;
(b) the tenancy is terminated on a ground other than the tenant's failure to pay rent;
(c) the tenancy expires or otherwise comes to an end without a renewal;
(d) the premises are no longer used wholly or primarily as specified premises.

(8) **Relief to landlords**: The Ordinance also protects landlords from certain actions by their lenders for failing to repay loans secured by any covered premises.

8.1. The landlord needs to establish that the rent moratorium is the sole or significant reason for his default in repaying loans.

8.2. The court will take into consideration the nature and magnitude of the tenant's default and overall financial condition of the landlord.

8.3. Subject to the above, the lender is barred from taking or continue to take the following actions against the landlord for his default, during the affected period:

(a) enforcing security;
(b) suing for repayment of default sums;

(c) recovering interest or surcharge on default;
(d) bringing action in court or commencing arbitration against the landlord;
(e) presenting bankruptcy or winding up petition against the landlord.

8.4. The Ordinance ceases to apply if a written agreement is entered into during the protection period in respect of a loan and with an agreed forbearance in respect of the repayment schedule or the amount of any repayment.

(9) **Stay of pending actions**: All prohibited actions commenced before 1 May 2022 will be stayed, and landlords or lenders will have to put such actions on hold until the end of the protection period.

(10) **Consequences of non-compliance**

(a) A landlord or lender, who takes or continues to take any prohibited action in contravention of the Ordinance during the protection period, commits a criminal offence.
(b) An offending landlord is liable to a fine that is equal to twice the amount of rent claimed, and in any event not less than $50,000.
(c) An offending lender will be liable to a fine that is twice the amount of the repayment default claimed, and in any event not less than HK$50,000.

Practical Tips

The following are some practical tips to avoid any contravention of the Ordinance and related criminal liability:

(1) **Contract Out.** The relevant parties may contract out of this rental moratorium by entering into a written agreement during the protection period with an agreed alternative forbearance arrangement. So, an affected landlord or lender may try to discuss and agree on an alternative arrangement with his counterparty.

(2) **Demand Letter.** It appears that an affected landlord or lender may still issue a demand letter for outstanding rent or loan repayment, but no interest or surcharge may be "recovered" (追討), during the protection period.

(3) **Uncertainties.** If there are any uncertainties, such as (i) whether the premises are used wholly or primarily as "Specified Premises" or (ii) in case there is any breach of the tenancy agreement other than or in addition to default in payment of rent, an affected landlord may wish to err on the side of caution and withhold any action in respect of the tenant's failure to pay rent during the protection period.

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