

A
B
C
D
E
F
G
H
I
J
K
L
M
N
O
P
Q
R
S
T
U
V

A
B
C
D
E
F
G
H
I
J
K
L
M
N
O
P
Q
R
S
T
U
V

HCCT 14/2022

[2022] HKCFI 3173

[amended and redacted copy]

**IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF FIRST INSTANCE
CONSTRUCTION AND ARBITRATION PROCEEDINGS
NO 14 OF 2022**

IN THE MATTER OF Section 87 of
the Arbitration Ordinance (Cap 609)

and

IN THE MATTER OF arbitration
awards obtained by A1 and A2 against
W1 and W2 in LCIA Arbitration Case
No. 153051 dated 12 March 2019 and
13 October 2021 respectively

BETWEEN

A1 1st Plaintiff

A2 2nd Plaintiff

and

W1 1st Defendant

W2 2nd Defendant

Before: Hon Mimmie Chan J in Chambers

Dates of Written Submissions: 8, 22 and 27 September 2022

Date of Decision: 17 October 2022

DECISION

Background

1. By their Originating Summons issued on 2 March 2022, the Plaintiffs in these proceedings applied for leave to enforce the partial award and the final award made by the Tribunal on 12 March 2019 and 13 October 2021 respectively (“**Awards**”) in two co-joined LCIA arbitrations against the Defendants (“**Arbitration**”). Under the Awards, the 2nd Defendant was ordered to pay to the 1st Plaintiff a sum of US\$142,943,168, and interest; and the Defendants were ordered to jointly and severally pay to the Plaintiffs their total fees and disbursements of US\$6,185,886.85, and arbitration costs of GBP 618,249.91. By an order of 9 March 2022, leave was granted on the Originating Summons (“**Enforcement Order**”).

2. On 17 May 2022, the Defendants applied to set aside the Enforcement Order, on the stated grounds that: (1) the Awards were not awards which the Hong Kong Court would enforce, as they are not commercial cases under the commercial reservation made by the People’s Republic of China (“**PRC**”) upon accession to the New York Convention, as applied to Hong Kong after 1997, and/or that the Awards are not Convention awards within the meaning of the Arbitration Ordinance (“**Ordinance**”) (“**Commercial Reservation Ground**”); (2) the Awards

were made in respect of a matter which is not capable of settlement by arbitration under the laws of Hong Kong, in that the Awards constituted direct or indirect enforcement of tax and/or revenue laws of the PRC (“**Arbitrability Ground**”); and (3) enforcement of the Awards would be contrary to public policy as it would infringe and/or be contrary to the laws of the PRC (“**Public Policy Ground**”).

3. The Defendants’ setting aside application has been scheduled for hearing in February 2023.

4. On 4 July 2022, the Plaintiffs applied for security to be provided by the Defendants, pending the hearing of the Defendants’ setting aside application, and in default of security, for the setting aside application to be dismissed. The Plaintiffs further seek security for their costs, on the ground that the Defendants are ordinarily out of the jurisdiction and that, on their purported case, they have no assets in Hong Kong.

5. The application for security was directed to be dealt with on the papers.

Applicable legal principles

6. The legal principles applicable to determination of an application for security are not disputed. They are as set out in *Soleh Boneh International Ltd v Government of the Republic of Uganda* [1993] 2 Lloyd’s Rep 208 at 212, applied in *Guo Shun Kai v Wing Shing Chemical Co Ltd* [2013] 3 HKLRD 484 and *Dana Shipping and Trading SA v Sino Channel Asia Ltd* [2017] 1 HKC 281, and will not be repeated here.

The strength of the argument that the Awards are invalid

7. The strength of the argument that the award is invalid, as perceived on a brief consideration by the court, is the first important factor to be considered on an application for security. As Staughton LJ explained in *Soleh Boneh*, if the award is manifestly invalid, there should be an adjournment and no order for security, and if it is manifestly valid, there should be either an order for immediate enforcement, or else an order for substantial security. In between where there are various degrees of plausibility in the argument for invalidity, the court must be guided by its preliminary conclusion on the point.

8. The merits of the Defendants' application are at this stage to be perceived on a brief consideration only. On such a brief consideration, I fail to see how it can be said that the Awards dealt with the Tribunal's determination of the tax liability of W2, the 2nd Defendant and Target Company which was the subject of the Stock Purchase Agreement ("SPA") made between the 1st Plaintiff as Seller, the 2nd Plaintiff as the Seller's Guarantor, the 1st Defendant as Buyer and X, the Buyer's Guarantor. The Arbitration related to the parties' dispute under the SPA, a commercial agreement made between the parties for the sale and purchase of the share capital of the 2nd Defendant. The Awards concern the Tribunal's determination of the rights and liabilities of the parties under their commercial relationship created under the SPA, and the decision made by the Tribunal as to the 1st Defendant's liability to make the payment to the Plaintiffs was based on the Tribunal's construction of the SPA, and of the indemnity under the relevant clauses of the SPA as to the responsibility of the Seller for any taxes of the Target Company attributable to the time prior to and including the Closing Date of the transaction, net any tax

benefit actually realized by the Buyer or the Target Company with respect to the taxes.

9. It was not disputed in the Arbitration that the 1st Plaintiff had made a payment of US\$193.8 million to the Mainland tax authority, on behalf of the Target Company, on a without prejudice basis, as agreed between the parties to the SPA. The tax paid had been determined by the relevant Mainland tax authority, and paid pursuant to the demands made by the tax authority on the Target Company. The relevant tax authority then confirmed in writing to the Target Company, at its request, that it had become entitled to reduced tax liabilities under PRC law. It was on such basis that the Tribunal found that a tax benefit had crystallized upon and as a result of the 1st Plaintiff's payment of the tax assessed, that the Target Company had received the benefit, and that there was a causal connection or relation between the tax payment made by the 1st Plaintiff on behalf of the Target Company and the receipt by the Target Company of the tax benefit. The Tribunal then proceeded to evaluate and assess the value of the tax benefit received and to be accountable and reimbursed by the Defendants to the Plaintiffs in accordance with the provisions of the SPA. This was done on the basis of the Tribunal's construction of the terms of the SPA, and in particular the Tribunal's construction of the 2nd Plaintiff's liability under the indemnity clause of the SPA for the amount of the tax of the Target Company up to the completion of the transaction, net of any tax benefit received by the Buyer/ 1st Defendant, or the Target Company/ 2nd Defendant, on the evidence and basis of what was notified and confirmed by the Mainland tax authority. There was, at the quantum hearing, expert evidence on the value of the tax benefit, on the basis of which the Tribunal ascertained and determined the value of the tax benefit

received by the Target Company, to rule on the restitutionary compensation to be made by the 2nd Defendant/ the Target Company to the 1st Plaintiff under the Final Award on quantum.

10. The PRC expert opinion cited the PRC law which provides that the tax authority has the right to make adjustments or reductions of taxable income and the taxes for which the Target Company and/or the 1st Plaintiff should be liable, and argued that in substance, the Tribunal had adjudicated on the question of whether or not the Target Company was entitled to the tax benefit, which is a PRC tax issue. I fail to see how it can be said that the Tribunal has deprived the relevant Mainland tax authority of its right to charge or rule on any tax payable, or to relieve a party from any liability for tax, by virtue simply of the Awards. The decision of the Tribunal on the tax benefit received, and what it was worth, was made by the Tribunal on the basis of the contractual provisions of the SPA which governed the rights and liabilities of the parties to the SPA *inter se*, and on the basis of the written confirmation issued by the relevant tax authority confirming the Target Company's entitlement. There is nothing to suggest that if the relevant tax authority considers, for any reason, that the Target Company is liable for additional tax, it is precluded by the Awards to look to the Target Company, or to the parties to the SPA, for any tax properly payable by either the Target Company, or by either the Plaintiffs or the Defendants. I can see no question of the Tribunal usurping the role of the Mainland tax authorities in adjudicating any tax payable or allocating any tax benefit.

11. Needless to say, the Court is not concerned with the correctness of the Tribunal's decision as to the value of the tax benefit,

its allocation amongst the parties to the SPA under the provisions of the SPA, or as to the tax payable by any party or any deductions applicable.

12. Hence, I am not satisfied that the Awards dealt directly or indirectly with foreign revenue, or with enforcement of foreign revenue law. Even if the Commercial Reservation was applicable, I am satisfied at this stage that the Awards dealt with the commercial relationship between the parties arising under their commercial agreement, the SPA. For that same reason, the Arbitrability Ground and the Public Policy Ground have no application.

The ease or difficulty of the enforcement of the Awards

13. In applying the relevant legal principles to the determination of whether to order security as a condition for adjourning the enforcement proceedings, the Court is to compare the position of the creditor under the award, if it was allowed to enforce the award immediately, and its position if enforcement was to be delayed as a result of an adjournment (*Soleh Boneh International Ltd v Government of the Republic of Uganda* [1993] 2 Lloyd's Rep 208, *IPCO (Nigeria) Ltd v Nigerian National Petroleum Corporation* [2005] 1 Lloyd's Rep 475, and *Dana Shipping and Trading SA v Sino Channel Asia Ltd* [2017] 1 HKC 281). The focus of the exercise is to consider the ease or difficulty of the enforcement of the award, and whether it will be rendered more difficult if enforcement is delayed, and to ascertain whether there is prejudice to the creditor as a result of the adjournment (*A v B* [2022] HKCFI 607).

14. In this case, the Defendants put emphasis on the fact that they do not have any assets, or (in their terminology) "any meaningful assets",

in Hong Kong. They argue that the Court should not order them to bring assets into Hong Kong, when none had previously existed to which the Plaintiffs could look for purposes of enforcement of any award in Hong Kong, and that to do so would be improving the position of the creditor and unfair to the Defendants (*Karaha Bodas Co LLC v Perusahaan Pertambangan Minyak Dan Gas Bumi Negara* [2003] 2 HKLRD 381).

15. As was pointed out in *X v Jemmy Chen* [2019] HKCFI 2172, if a debtor did not have assets within the jurisdiction of Hong Kong in the first place, this is one factor against the grant of security, although it is not the only relevant nor the determining factor, as illustrated in *Weili Su v Shengkang Fei* [2019] 2 HKLRD 1214. The particular facts in *Karaha Bodas* have to be borne in mind, to understand the reason why security was not ordered against the background of all the factors existing in the case: of there being existing security against assets in Hong Kong, the availability of other disclosed assets elsewhere and there being no evidence of dissipation in Hong Kong.

16. I am not satisfied that the Defendants in this case have been forthright with regard to their assets, nor that there is no risk of dissipation of their assets.

17. In their evidence, the Defendants claim that they never had any “meaningful assets” within Hong Kong which were available for enforcement. The 2nd Defendant’s assets are its interests under contracts for offshore oil and gas exploration and development in the Mainland. The 1st Defendant is a special purpose vehicle incorporated in the BVI, and its

purpose is to hold all the shares in the 2nd Defendant, which is a Bahamian company. According to the affirmation of the General Counsel of the Defendants, the 1st Defendant has “very limited assets” other than the shares in the 2nd Defendant. It was claimed that other than a bank account maintained by the 1st Defendant with CMBC in Hong Kong, it has no other assets, and that the bank account in question holds “minimum cash”. In support, the 1st Defendant produced selected bank statements and transaction records for April 2022 and May 2022, showing that it had balances of approximately US\$600 in the CMBC account. The Defendants also produced selected bank transaction records relating to the 2nd Defendant’s account with Citibank in Hong Kong, to show that it had balances of approximately US\$500 to US\$2,300 in the account, and that there have been “little usage and movement” in the account, and only “minimal amounts” held therein.

18. It was only when the Plaintiffs’ solicitors wrote to seek production and inspection of the full monthly bank statements of the 2 bank accounts, for the period from 1 October 2021, that the Defendants produced further bank statements. These show that from December 2021, the 2nd Defendant had at least received monthly payments of US\$600,000 in the Citibank account, and had on receipt immediately paid out the exact amount to an entity referred to as [REDACTED] (“Investments”).

19. Counsel for the Defendants sought to downplay this by claiming that these were of *de minimus* amounts, compared to the principal sum of US\$143 million under the Awards. I accept the submissions made

on behalf of the Plaintiffs, that the monthly receipt and payment out of US\$600,000 can scarcely be said to be of *de minimus*.

20. In my view, the Defendants only chose to make partial disclosure of their assets in Hong Kong, and have not been forthcoming in relation to the payments in and out of the 2nd Defendant's account of US\$600,000 per month. I do not agree that these are small amounts which do not need to be properly explained, as they do comprise assets of the 2nd Defendant in Hong Kong if they had not been paid out or dissipated. The Defendants have not adequately explained why the US\$600,000 had to be paid out from the 2nd Defendant's account to another entity, Investments, when on the Defendants' case, they formed part of the funds raised under the alleged "sell and leaseback arrangement" with [REDACTED] ("CN") and were to be used to repay the loans of the 2nd Defendant. The Plaintiffs' case is that these payments out of the 2nd Defendant's bank account in Hong Kong constituted dissipation of assets. On the evidence given by the Defendants, I am not persuaded that there has been sufficient and satisfactory explanation given that the funds transferred out of the 2nd Defendant's account were made in the ordinary course of the 2nd Defendant's business, or for its ordinary and normal expenses.

21. On the Plaintiffs' case, X which was a listed company and the Guarantor of the 1st Defendant under the SPA and the parent company of the 1st Defendant, had become delisted as early as [REDACTED] 2020. In [REDACTED] 2021, the Hong Kong Stock Exchange ("Exchange") had published a statement in respect of disciplinary proceedings which had

been taken against X and its 4 directors, including Mr [REDACTED] (“Y”), the only executive director of X and the sole director of the 2nd Defendant.

22. The Plaintiffs claim that according to the 2020 Annual Report of X which was published on 10 August 2021, the financial status of X and the Defendants has been in a state of deterioration. As at 30 June 2020, the X group of companies (“Group”) had defaulted in approximately HK\$4.554 billion of its total borrowings of HK\$9.21 billion. According to an earlier announcement which had been issued by X on [REDACTED] 2018, the 2nd Defendant had entered into a finance lease agreement with CN with a principal amount up to US\$406 million. According to the 2020 Annual Report, the 2nd Defendant and/or X had defaulted in repayment of its borrowings from CN. The ultimate controlling shareholder of X and a guarantor of certain debts of the Group, one Dr Z, had been adjudged bankrupt by the Hong Kong Court on [REDACTED] .

23. According to the 2020 Annual Report, the value of the total assets of the Group, which represented and/or included the assets owned by the Defendants, had changed dramatically from HK\$5.942 billion in 2019 to only HK\$498 million in 2020, with a decrease of over 91%.

24. The Plaintiffs highlighted the fact that the 2020 Annual Report of the Group contained a qualified opinion of the auditors, which stated that they had not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the consolidated financial statements of the Group. According to the auditors, they were unable to obtain sufficient audit evidence in relation to (*inter alia*) the impairment assessment of the assets of the Group as at 30 June 2020 and 2019.

25. On the Plaintiffs' case, the Defendants are in a dire financial situation and further delay in enforcement of the Awards would be prejudicial to the Plaintiffs, in that it would become more difficult to recover the amount due to them from the Defendants. This is more apparent when the conduct of the Defendants' officers and of their parent company is taken into consideration.

26. On 20 October 2020, X's listing was cancelled by the Exchange after 2 to 3 years of non-compliance with the Listing Rules and the suspension of its trading on the Exchange. There had been investigations into suspicious transactions conducted in the business of the Group, which investigations had eventually led to X's delisting. In the Statement of Disciplinary Action issued by the Exchange against X and its directors including Y, the Exchange noted that there had been a blatant refusal by the directors to procure X to comply with the repeated requests of the Exchange to publish the announcement of X's delisting, which constituted the directors' willful and persistent failure to discharge their responsibilities under the Listing Rules. The Exchange further stated that the retention of the directors' office would have been prejudicial to the interests of investors, had the company remained listed.

27. On behalf of the Defendants, it was argued that they should be kept separate from X, despite the fact that the 1st Defendant is a wholly-owned subsidiary of X, and the 2nd Defendant is a wholly-owned subsidiary of the 1st Defendant. They claim that their business of petroleum production is only one of the several lines of X's business, that the Defendants had reputable partners on the Mainland, and that they had or shared interests in oilfields on the Mainland. They claim that their business

had nothing to do with X's delisting which was more related to the international trading and bunkering business led by individuals who were not involved in the Defendants' line of business. The Defendants claim that irrespective of the financial results disclosed in the 2020 Annual Report of X, the Defendants remain going concerns and "*are likely to continue to do business*" (emphasis added).

28. In relation to the financial figures, the Defendants claim that the Group's interests in the oilfields depend on market conditions and on crude oil prices, and that these prices have recovered significantly since the 2020 Annual Report. They seek to place reliance on the draft accounts of X for the year ended 30 June 2021, to claim that the total assets of the Group have increased to approximately HK\$5 billion for the year ended 30 June 2021, and that there has been reversal of impairment loss, with a consequent sum of \$1,667 million written back into the books of the Group.

29. However, as pointed out by the Plaintiffs, these draft accounts of X for the period up to 30 June 2021 have still not been finalized, and are unreliable. The Plaintiffs highlighted that X's accounts for 2020 had been subject to the auditors' qualified opinion, and that the Defendants have failed to explain why their accounts up to June 2021 could not be finalized as at August 2022. In any event, the Plaintiffs highlighted the Defendants' acceptance that the value of their assets and interests in the oil fields are subject to severe and rapid fluctuation.

30. I do not accept the Defendants' attempts to play down the censure or disciplinary proceedings against Y, who is the executive director of X and also the sole director and controller of the 2nd Defendant.

A
B There are high standards expected of directors of listed companies, who
C should be trusted, and must be seen, to act in compliance with the Listing
D Rules and the obligations imposed thereunder on a listed company and its
E directors. If Y does not act in accordance with these high standards and
F cannot comply even with basic demands made by the regulators, it reflects
G very badly on his ability and intentions to comply with orders of the Court.
H If Y had no hesitation in flouting the Listing Rules, and in ignoring the
I repeated demands made by the regulators with regard to compliance, as the
J evidence has shown, he simply cannot be trusted with observing orders of
K the Court and of the Tribunal. He is just as likely to consider that the
L Defendants which he controls can be excused from complying with their
M obligations under the Awards to make payment, and can do what they like
N with their assets despite any Award or judgment made against the
O Defendants, or to find reasons to evade the Defendants' liabilities, pending
P appeals, or pending further hearings. That was the position taken by Y,
Q when he and X were directed by the Exchange to make the announcement
R of X's delisting, on the excuse and purported basis that X was still
S challenging the decision of the Exchange.
T
U
V

31. There is an interim of 9 months between the issue of the
summons to set aside the Enforcement Order and the adjourned hearing of
the application, and an interim of 7 months between the issue of the
summons for security and the adjourned hearing in February 2023.
I do not consider that there is undue delay in the Plaintiffs' application for
the Enforcement Order from the time when the Awards were made. I bear
in mind that any delay in enforcement is against the interests of the
Plaintiffs which have succeeded in obtaining a final and binding award,
and further against this Court's policy of enforcement of arbitration

agreements and arbitral awards. I have also considered the merits of the Defendants' setting aside application on a preliminary basis, and conclude in all the circumstances of this case that it is appropriate to order security to be furnished by the Defendants.

Disposition

32. I will make orders in terms of paragraphs 1 to 3 of the Plaintiffs' summons of 4 July 2022 ("**Summons**"), save that the amount of security is to be 40% of the amounts specified in the Final Award on Quantum.

33. Since the Defendants seeking to set aside the Enforcement Order are clearly outside the jurisdiction of Hong Kong, there is also good ground on the evidence to order them to provide security for costs, which on broad-brush basis, I will order in the sum of HK\$750,000. Orders will be made in terms of paragraphs 4 and 5 of the Summons, with HK\$750,000 substituting HK\$1,100,000.

34. The costs of the Summons are to be paid by the Defendants to the Plaintiffs, to be summarily assessed if not agreed. The Plaintiffs are at liberty to file and serve their Statement of Costs within 7 days and the Defendants are at liberty to file and serve their Statement of Objection within 7 days thereafter.

(Mimmie Chan)
Judge of the Court of First Instance
High Court

A
B
C
D
E
F
G
H
I
J
K
L
M
N
O
P
Q
R
S
T
U
V

The 1st & 2nd plaintiffs were represented by Kobre & Kim
Mr Jose Maurellet SC and Mr Alexander Tang, instructed by Li & Partners,
for the 1st & 2nd defendants

A
B
C
D
E
F
G
H
I
J
K
L
M
N
O
P
Q
R
S
T
U
V