

Hong Kong Court of Final Appeal Upholds Dismissal of Bankruptcy Petition Where Debt Under Dispute Was Subject to Exclusive Jurisdiction Clause

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On 4 May 2023, the Hong Kong Court of Final Appeal (the “CFA”) handed down its judgment in [Guy Kwok-Hung Lam v Tor Asia Credit Master Fund LP \[2023\] HKCFA 9\[1\]](#), putting an end to the age-old debate on the effect of an exclusive jurisdiction clause (“EJC”) in the insolvency context.

The CFA upheld the Court of Appeal’s (the “CA”) decision (by majority) to dismiss the bankruptcy petition. The CFA endorsed the approach that in an ordinary case where the underlying dispute of the petition debt was subject to an EJC, the court should dismiss the petition unless there are strong reasons for the court to decide otherwise.

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1. Background

The dispute concerned a loan advanced by Tor Asia Credit Master Fund LP (the “**Petitioner**”), pursuant to a Credit and Guaranty Agreement (the “**Agreement**”), to a company (the “**Borrower**”) controlled by Mr. Guy Kwok-Hung Lam (the “**Debtor**”), whereby the Debtor agreed to provide a guarantee, as primary obligor, to pay in full of all amounts due and owed without any demand or notice. The Agreement contained an EJC in favour of the New York courts in relation to “*all proceedings arising out of or in relation to*” the Agreement.

The Agreement was subsequently amended and the maturity of the loan was extended. Notwithstanding that, the Borrower was still unable to make repayment. The Petitioner then presented a bankruptcy petition in Hong Kong against the Debtor. The Debtor resisted the petition and argued that there was no event of default and that, pursuant to the EJC, the Petitioner was required to bring proceedings in the New York courts first to establish the Debtor’s liability.

The Court of First Instance (the “**CFI**”) granted the bankruptcy order, on the basis that the Debtor was unable to demonstrate a *bona fide* dispute on substantial grounds in relation to the petition debt^[2]. The CA allowed the Debtor’s appeal and dismissed the bankruptcy petition^[3]. The CA held that if the dispute concerning the underlying debt fell within the scope of an EJC, the bankruptcy petition should not be allowed to proceed without strong reasons.

The Petitioner appealed to the CFA on the proper approach that Hong Kong courts should adopt in a bankruptcy petition where the dispute concerning a debt is subject to an EJC.

2. The CFA’s decision

The CFA unanimously dismissed the appeal and affirmed the decision of the CA.

(i) Jurisdiction and powers of the CFI

The Petitioner contended that parties could not contract out of the insolvency legislation and in these proceedings different considerations were to be taken into account from those involving the upholding of EJs in private actions. It was argued that to give presumptive weight to EJs was to erode and undermine the domestic insolvency regime.

Whilst the CFA confirmed that the CFI's jurisdiction in a bankruptcy matter was conferred by the Bankruptcy Ordinance (Cap. 6), and was not amenable to exclusion by contract, i.e. the parties' agreement not to invoke the jurisdiction of the CFI had no effect on its jurisdiction, it held that the parties' agreement to refer their disputes to a foreign court informed the CFI's discretion as to whether to exercise its jurisdiction.

The CFA observed that the CFI might exercise its discretion to decline jurisdiction in certain classes of cases, such as where the issue of *forum non conveniens* was raised or where the dispute in a particular action was covered by an arbitration agreement or an EJ.

(ii) The discretion to decline jurisdiction in bankruptcy

Having found that the CFI had the power to decide whether to exercise its jurisdiction, the CFA further held that the determination of whether the debt was *bona fide* disputed on substantial grounds was a threshold question which might or might not be engaged when the court decided whether to exercise its bankruptcy jurisdiction.

The CFA noted that in the event that the parties had agreed to have all their disputes under an agreement giving rise to the debt determined exclusively in another forum, the CFI had total discretion to choose not to exercise its bankruptcy jurisdiction and refrain from determining such threshold question.

The CFA considered that it was at this stage that the public policy interest in holding parties to their agreements was engaged. Should the CFI proceed with the petition and make a ruling on the threshold question, it assumed jurisdiction to decide a question which the parties had otherwise agreed would be determined in another forum.

The CFA was of the view that parties' agreement for certain disputes to be resolved in another forum would be highly relevant as to whether the CFI should exercise its bankruptcy jurisdiction at all. In the event that the underlying debt was subject to an EJ, unless the Petitioner could show that there were strong reasons, such as the risk of the debtor's insolvency impacting third parties, the debtor's reliance on a frivolous defence, or an occurrence of an abuse of process, the Court should normally dismiss the petition.

3. Comment

This decision crystallises the court's position on the effect of an EJ in the context of bankruptcy and winding up proceedings. Absent strong reasons, the Hong Kong court will not proceed with the petition before the adjudication of the petition debt by the agreed forum. It also underscores the importance attached by the courts to party autonomy.

The case also serves as an important reminder to parties when entering into agreements with EJs, they should be aware that such clauses will have significant impact on any insolvency proceedings to be commenced in Hong Kong and they may be required to first have the dispute over the underlying debt adjudicated in the agreed forum before commencing insolvency proceedings in Hong Kong.

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[1] https://legalref.judiciary.hk/lrs/common/ju/ju_frame.jsp?DIS=152321&currpage=T

[2] https://legalref.judiciary.hk/lrs/common/ju/ju_frame.jsp?DIS=137308

[3] https://legalref.judiciary.hk/lrs/common/ju/ju_frame.jsp?DIS=146843

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding these developments. Please contact the Gibson Dunn lawyer with whom you usually work, or the following authors in the firm's Litigation Practice Group in Hong Kong:

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