

## Insights

# HONG KONG COURT MAKES SECURITY FOR COSTS ORDER AGAINST MAINLAND PARTIES WITH NO ASSETS IN HONG KONG

Apr 28, 2025

## SUMMARY

In *Y and Another v GI and Another* [2025] HKCFI 1317<sup>[1]</sup>, the Hong Kong Court of First Instance (“Court”) allowed the defendant’s application for security for costs against the plaintiffs in respect of the plaintiffs’ application to set aside an arbitral award.

In doing so, the Court found that the plaintiffs were resident outside Hong Kong, had no assets available in Hong Kong and the setting aside application had little prospect of success.

## BACKGROUND

A dispute arose out of an arrangement where the 1<sup>st</sup> Defendant (“D1”) invested HK\$100 million in the Group, which comprised the 1<sup>st</sup> Plaintiff (“P1”), 2<sup>nd</sup> Plaintiffs (“P2”) and the 2<sup>nd</sup> Defendant (“D2”).

An arbitration was commenced by D1, and the arbitrator ruled in favour of D1.

In gist, the arbitral award ordered that:

1. A total sum of US\$111,475,737 (with interest) was to be paid to D1.
2. P1 and P2 were to transfer some shares to D1, and in exchange D1 was to pay the total purchase price of US\$100 million to P1.
3. Crucially, pursuant to a set-off mechanism agreed between the parties, D1 was entitled to set-off the amounts owing to D1 against the purchase price of the shares owing to P1. Under the set-off mechanism, if D1 exercised the right of set-off, P1 would waive the purchase price and D1 “*shall be deemed to have paid the purchase price in full*”.

P1 and P2 applied under section 81(1) of the Arbitration Ordinance to set aside the arbitral award, on the ground that the set-off mechanism was contrary to the public policy in Hong Kong.

In response, D1 applied for security for costs of more than HK\$3.5 million, on the basis that (a) P1 and P2 were both ordinarily resident in the Mainland, with their central management and control outside Hong Kong, (b) the Group (of which P1 and P2 formed part) was in serious financial difficulties, and (c) substantial difficulties would be encountered by D1 in enforcing any costs orders against P1 and P2.

Opposing the security for costs application, P1 and P2 submitted that D1 was liable under the award to pay the purchase price for the shares of US\$100 million, which sum exceeded the security sought by D1. (P1 and P2 had no assets in Hong Kong, apart from the claim made of their entitlement to the purchase price.)

## COURT'S DECISION

The Court first endorsed the decision of an earlier court decision<sup>[2]</sup> that Order 23 rule 1 of the Rules of the High Court applied to a court application to set aside an arbitral award under section 81 of the Arbitration Ordinance.

Order 23 rule 1(1) provides:

*“Where, on the application of a defendant to an action or other proceeding in the Court of First Instance, it appears to the Court –*

*(a) that the plaintiff is ordinarily resident out of the jurisdiction,*

*...*

*then if, having regard to all the circumstances of the case, the Court thinks it just to do so, it may order the plaintiff to give such security for the defendant's costs of the action or other proceeding as it thinks just.”*

After considering the relevant legal authorities in respect of the circumstances where the court should make an order for security for costs, the Court allowed D1's application for security for costs (albeit at a reduced amount of HK\$2 million), and the following factors were considered by the Court:

1. P1 and P2 were resident outside Hong Kong. P1's registered address and principal place of business was in Shenzhen. P1 was a subsidiary of a listed company in the Mainland and its key personnel were resident in Nanjing. P2, being a subsidiary of P1, had its headquarters in Nanjing and its primary operation was in the Mainland. Neither P1 nor P2 were registered in Hong Kong under Part 16 of the Companies Ordinance.

2. Under the set-off mechanism which was permitted and acknowledged in the arbitral award, P1 and P2 were not entitled to receive the purchase price when D1 exercised its contractual set-off. According to the Court's interpretation of the arbitral award, no sum at all was due from D1 to P1 and P2 for the transfer of the shares, when D1 exercised the set-off mechanism.
3. Even if D1 did not exercise the set-off mechanism, the amount due to D1 (US\$111 million plus interest of around US\$20.6 million) exceeded the amount payable by D1 to P1 (US\$100 million). Therefore, the costs incurred by D1 were not capable of being set-off, should D1 succeed in the setting aside application.
4. D1 also pointed out that the Supreme People's Court on the Mainland had issued a Consolidation Notice in respect of the Group (of which P1 and P2 formed part). The effect of the Consolidation Notice was to centralize all proceedings and enforcement actions against the entities in the Group involving a large number of debt claims, in order to protect the struggling business of the Group. The Court was of the opinion that this Consolidation Notice would appear to support D1's claim that the Group was facing a large number of claims on the Mainland, such that enforcement against P1 and P2 would be subject to delay and difficulties on the Mainland.
5. The Court also concluded that it was clear without going into detailed arguments that P1 and P2's application to set aside had little prospect of success. P1 and P2 contended that the set-off mechanism was contrary to the public policy in Hong Kong, because it was "*in breach of the spirit of the Hong Kong Listing Rules*". The Court said that, given that P2 was a Shenzhen listed company, the Hong Kong Listing Rules did not apply. In any event, the set-off mechanism which was said to be unjust to P1 in depriving of it of payment of the purchase price of the shares had been agreed to and accepted by the parties. The Court commented that it also was an important public policy of Hong Kong to recognize and enforce contracts, arbitration agreements and arbitral awards.

## CONCLUSION

Apart from confirming the Hong Kong court's jurisdiction to order security for costs against parties in setting aside proceedings of arbitral awards, this is another decision by a Hong Kong court which expressly stresses the importance of the finality and enforceability of arbitral awards.

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[1] Date of Reasons for Decision: 1 April 2025

[2] *P1 v D (Arbitration: Security for Costs)* [2024] 5 HKLRD 699

## RELATED PRACTICE AREAS

- Litigation & Dispute Resolution

- Business & Commercial Disputes
- International Arbitration

## MEET THE TEAM



### **Glenn Haley**

Hong Kong SAR

[glenn.haley@bclplaw.com](mailto:glenn.haley@bclplaw.com)

[+852 3143 8450](tel:+85231438450)



### **Ian Cheng**

Hong Kong SAR

[ian.cheng@bclplaw.com](mailto:ian.cheng@bclplaw.com)

[+852 3143 8455](tel:+85231438455)

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