

# Hong Kong Court of First Instance Rejects Crown Immunity Claim by PRC State-Owned Enterprise

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In a judgment dated 8 June 2017, the Hong Kong Court of First Instance (the “Court”) rejected an assertion of Crown immunity by China National Coal Group Corporation (“China Coal”) (a PRC state-owned enterprise (“SOE”)) and granted a charging order against the shares it held in a Hong Kong company, China Coal Hong Kong Limited (*TNB Fuel Services SDN BHD v. China National Coal Group Corporation* [2017] HKCFI 1016).

The decision provides guidance on the approach by the Hong Kong courts to claims of Crown immunity in Hong Kong by Chinese SOEs.

## **Crown immunity in Hong Kong**

The common law doctrine of Crown immunity arises from the principle that “*the sovereign can do no wrong*” and provides that a sovereign cannot be sued in the courts of his own country.

In the 2010 case of *Hua Tian Long (No. 2)* [2010] HKLRD 611 (the “HTL Case”) the Hong Kong Court of First Instance found that the common law doctrine of Crown immunity subsisted in Hong Kong, notwithstanding the handover of Hong Kong to China in 1997. The immunity of the British Crown in the Hong Kong courts was

transferred to the PRC State.

Accordingly, the PRC Central People's Government ("CPG"), the domestic sovereign government of the Hong Kong Special Administrative Region, is entitled to claim immunity from suit and execution in the courts of Hong Kong.

Importantly, Crown immunity does not apply to Hong Kong arbitration (as opposed to litigation). Under Hong Kong law, it is generally accepted to be the position that a State party is bound by its agreement to arbitrate before a Hong Kong arbitral tribunal. However, Crown immunity will still be relevant to Hong Kong-seated arbitrations involving State parties, as it may be necessary to apply to the local courts for interim relief, and/or enforcement of any award.

In the HTL Case, which concerned a claim to Crown immunity by the Guangzhou Salvage Bureau ("GSB"), the court found that the material consideration to determine whether a corporation should be treated as part of the Crown, was the control which the CPG exercised over that corporation. In particular, the key test was *"whether the corporation in question was able to exercise independent powers of its own"*.

Whilst the "control test" applied in the HTL Case arises from the application of Hong Kong common law, the question of whether the entity in question meets the test will principally be a question of the lex incorporationis, namely PRC law. In the HTL Case, the court found that under PRC law, the GSB was part of the PRC State. However, the court in that case also accepted the submission by counsel for the GSB that the GSB was different from Chinese SOEs which *"enjoy powers of independent management and freedom from interference, with ownership of its assets and the capacity independently to assume civil liabilities"*.

## **Factual Background**

On 17 December 2014, the Applicant, a Malaysian private company ("TNB"), obtained an arbitral award for approximately US\$5.3 million against the Respondent, China Coal ("Award"). The details of the arbitration, including its seat, institution, and rules were not disclosed.

On 10 June 2015, the Court granted TNB leave to enforce the Award. Subsequently, in August 2015, TNB applied for a charging order over shares held by China Coal in China Coal Hong Kong Limited (the "Shares"). In April 2016, TNB successfully

obtained an *order nisi* with respect to the Shares.

China Coal, which is wholly owned by the Chinese government's State Asset Supervision and Administration Commission ("SASAC"), asserted that, as an entity of the CPG, it was entitled to Crown immunity in Hong Kong.

China Coal invited the Hong Kong Secretary for Justice ("SJ") to intervene in the proceedings, on the basis that the case raised issues of constitutional importance and public interest.

## **Judgment**

There were two issues to be determined by the Court. The first was whether there had been a valid assertion of Crown immunity by the CPG. The second was, given that an assertion of Crown immunity does not conclusively bind the court, whether the assertion was otherwise valid by reference to the *lex incorporationis* and the application of the "control test".

With respect to the first issue, Justice Mimmie Chan decided that China Coal's assertion of Crown immunity had not been validly made. Specifically, Justice Chan found that China Coal had "*failed to show authority to assert Crown immunity on behalf of the CPG, and that no such claim has been validly made on behalf of the CPG*". The only evidential support for this claim came from the affirmation of China Coal's general legal counsel. However, and significantly, pursuant to the SJ's intervention, a letter had been obtained from the Hong Kong and Macao Affairs Office of the State Council of the CPG ("the Letter"), the contents of which "*signally [defeats China Coal's] assertion of Crown immunity*".

The Letter, confirmed in general terms that China Coal, as an SOE, is "*an independent legal entity, which carries out activities of production and operation on its own, independently assumes legal liabilities and there is no special legal person status or legal interests superior to other enterprises*". The Letter further asserted that, save in certain "*extremely extraordinary circumstances where the conduct was performed [by the SOE] on behalf of the state via appropriate authorisation, etc.*", the SOE would not be deemed as a body performing functions on behalf of the CPG.

The Court approached the second issue through addressing two related questions. The first was whether China Coal was part of the CPG and the second whether it

was otherwise controlled by the CPG. With respect to the first question, Justice Chan found that *“as a matter of fact under PRC law, the Respondent is not part of the CPG, nor SASAC”* and was a distinct and independent corporate entity from the CPG.

This finding was made in light of an examination of the material provisions of the PRC Company Law, the PRC Constitution and Assets Law, among other legislation, insofar as they related to SOEs and extensive expert evidence on their meaning and application to China Coal under PRC law.

The Court also observed that the status of China Coal was readily distinguishable from that of the GSB in the HTL Case. In that instance the entity in question was a public institution, not, like China Coal, a separate legal entity. Furthermore, the GSB, unlike China Coal, had no shareholders, no paid-up capital, no right to independently acquire or dispose of assets, and no ability to assume independent civil liabilities.

With respect to the second question and the application of the common law “control test” by reference to the PRC law, Justice Chan determined that *“[i]n all, bearing in mind the nature and degree of the control which can be exercised by SASAC on behalf of CPG over [China Coal], [China Coal’s] ability to exercise independent powers of its own, and that its business and operational autonomy are in fact enshrined in and guaranteed under the applicable PRC law, I consider that the Respondent is not entitled to invoke Crown immunity”*.

In terms of both questions, the Court held as a matter of PRC law, China Coal *“is entitled to independent autonomy in its business operations, and it has not been established that [China Coal] is part of or controlled by the CPG to be entitled to Crown immunity against execution of its assets”*.

The Court dismissed China Coal’s assertion of Crown immunity and granted the charging order absolute against the Shares. China Coal was ordered to pay TNB’s and SJ’s costs of the application.

## **Takeaways**

It has been seven years since the handing down of the HTL Case, and the application of the “control test” to determine the existence of Crown immunity under Hong Kong law. The *TNB Fuel Services* judgment now provides further

guidance on the application of that test in Hong Kong, in particular when it comes to SOEs under PRC law. The rationale for the decision, including the detailed analysis of the nature and effect of the PRC statutory provisions governing Chinese SOEs, strongly suggests that such SOEs engaging in commercial activities will face a high bar in claiming Crown immunity in Hong Kong.