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Ref : Chans advice/241

To: Transport Industry Operators

Interpleader

The Hong Kong High Court issued a Decision on 13 May 2021 to deal with an interpleader action concerning the stakeholding of US\$700,000 in relation to a dispute over some management fees between two transport operators. [HCMP510/2020] [2021 HKCFI 1373]

Background

The underlying dispute between the two transport operators arose from a particularly bitter business divorce, which started in 2014. The dispute concerned a Debt (management fees) allegedly owed to PB Shipping by PB Logistics in the amount of US\$700,000 which was repayable by agreement. On 3 July 2014, PB Shipping issued a Statutory Demand against PB Logistics for payment of the debt. PB Shipping's position was that if the Debt was not repaid, it would issue a petition to wind-up PB Logistics.

Shortly after receipt of the Statutory Demand, PB Logistics engaged K Sit as its solicitors. PB Logistics denied both the Debt and the repayment agreement. K Sit was instructed to commence proceedings to restrain PB Shipping from presenting a winding-up petition.

To try to obviate the need to seek an injunction against PB Shipping, on 16 July 2014 PB Logistics deposited a sum of US\$700,000 ("Sum") with K Sit. On instructions, K Sit wrote to PB Shipping's solicitors, DLA, on the same day denying liability for the Debt and proposed that K Sit would stakehold the Sum on the following terms ("Stakeholder Arrangement"):

- "(1) [PB Logistics] does not believe that there has been any overpayment of management fee but is ready and willing to meet the alleged claim of US\$700,000 if [PB Shipping] is able to provide and prove, by proper documentation, that there was an overpayment of US\$700,000 of management fees from [PB Shipping] to [PB Logistics]; and
- (2) As proof of their good faith, and to secure the alleged debt of US\$700,000, [PB Logistics] has deposited a sum of US\$700,000 with us. We confirm that we are now holding as stakeholders in escrow the said sum, to release to [PB Shipping] upon the alleged debt being proved by proper documentation to be produced by [PB Shipping] to [PB Logistics] ..."

On 21 July 2014, in response to K Sit's letter, DLA (a) asserted that adequate evidence of the debt had been provided; and (b) agreed to withhold the presentation of a winding up petition.

"In view of the above, we believe that [PB Shipping] has provided compelling evidence in relation to [PB Logistics'] liability to pay the sum of US\$700,000 to [PB Shipping]. We therefore look forward to receiving the sum of US\$700,000 held by you in escrow within the next 7 days. In view of fact that [PB Logistics] has already paid you the sum of US\$700,000 in escrow, we would agree, on behalf of [PB Shipping], not to present any winding-up petition against [PB Logistics]."

In response to DLA's request to pay over the money, K Sit informed DLA by letter dated 25 July 2014 that it would not release the Sum as PB Shipping had failed to provide sufficient evidence of

the Debt. DLA then asked K Sit on 4 August 2014 for an undertaking to maintain and not to diminish the Sum save with the written consent of both PB Logistics and PB Shipping or pursuant to an order of the court. By their letter dated 8 August 2014, K Sit did not give the undertaking in the terms sought by DLA, but instead undertook to notify DLA if the Sum was to be released to any party other than PB Shipping (“Undertaking to Notify”). The Stakeholder Arrangement was reiterated in the letter.

On 24 July 2014, PB Logistics commenced proceedings against PB Shipping (HCA 1413/2014) for a declaration that no debt was due and owing from it to the latter. Pleadings were filed in HCA 1413/2014 and the action reached the discovery stage in early 2015, but there had been no further progress since.

Apparently, the matters went into hibernation until 2020. By a letter dated 8 April 2020, SSW informed K Sit that SSW had replaced it as PB Logistics’ solicitors and requested that K Sit transfer the Sum to them. In accordance with the Undertaking to Notify, by letter dated 14 April 2020 to DLA, K Sit enclosed a copy of SSW’s said letter and inquired about PB Shipping’s position to the request.

By their letter dated 17 April 2020, DLA required K Sit to confirm, under threat of “urgent injunctive relief from the Court against [them] ... as stakeholder/ escrow agent”, that it would not release the Sum to SSW in the absence of a corresponding undertaking from SSW that it would (a) release the Sum to PB Shipping upon receipt of proper documentation to prove the Debt; and (b) inform PB Shipping of the release of the same to any other party.

Legal proceedings were threatened by SSW (letter dated 17 April 2020) against K Sit unless the Sum was paid over to them. Similar demand was made by DLA (letter dated 20 April 2020) on the basis that PB Shipping had provided “uncontroversial and credible evidence” of the Debt and legal action against K Sit was also threatened.

K Sit indicated by letter on 20 April 2020 that in light of the conflicting claims to the Sum and the threat of litigation against them, they would have to review the matter urgently with external legal advisors and that pending such review, they would not be releasing the Sum to SSW. The prospect of interpleader proceedings was also indicated.

On 21 April 2020, Statutory Demand was issued by PB Logistics against K Sit in respect of an alleged debt of US\$700,000 incurred on 8 April 2014 as “money on account”.

K Sit took out the Interpleader Proceedings on 8 May 2020. Pursuant to the Order of Master Ho dated 3 September 2020 made upon a Consent Summons of the parties, K Sit paid the Sum into Court on 4 September 2020. On 19 November 2020, Master Wong gave an Order granting interpleader relief in favour of K Sit in respect of the Sum which was stakeheld by K Sit. On 27 November 2020, PB Logistics appealed against the Order of Master Wong.

Essentially, two issues were raised by PB Logistics in the appeal, namely, (i) whether there was a tripartite agreement between itself, PB Shipping and K Sit in respect of the stakeholding of the Sum; and (ii) whether interpleader relief should be declined because K Sit had taken side and put itself into a difficult position where it faced two alleged claims.

Applicable principles

Order 17 of the RHC governs interpleader proceedings. Pursuant to the provisions thereunder interpleader relief will only lie if the following conditions are fulfilled :

(1) A party is under a liability in respect, *inter alia*, of money;

- (2) He is, or expects to be, sued in respect of that money by two or more persons with adverse claims thereto;
- (3) He claims no interest in the said money;
- (4) He does not collude with any of the competing claimants; and
- (5) He is willing to pay the money into court or dispose of the same in accordance with the directions of the court.

Whilst interpleader relief is discretionary, an order will normally be made where the aforementioned conditions are met: *HKCP 2021*, Vol 1, [17/1/11].

Where an applicant expects to be sued by competing claimants, there must be a real foundation for such an expectation: *DLA Piper Hong Kong v China Property Development (Holdings) Ltd* [2010] 1 HKLRD 903 (CA), at §22.

Collusion (O 17, r 4(b)) does not necessarily entail moral wrongdoing. Rather, it means that the applicant for interpleader relief must not have “played the same game” as one of the competing claimants: *Famous Zone Electronics Ltd v HSBC Ltd* [1998] 3 HKC 723, at 727G.

The legal rights and obligations of a stakeholder had been set out in *Manzanilla Ltd v Corton Property and Investments Ltd*, unrep, English Court of Appeal (Civil Decision), 13 November 1996, [1996] Lexis Citation 3767, pgs 5-6, *per* Millett LJ (as he then was) :

“Where a stakeholder is involved, there are normally two separate contracts to be considered. There is first the bilateral contract between the two principals which contemplates two possible alternative future events and by which the parties agree to pay a sum of money to a stakeholder to abide the happening of one or other of them. In the present case it consisted of a series of written contracts for the sale of land, and the relevant events were the failure of the contracts by the repudiatory breach of one party or the other. The second contract is the tripartite contract which results from the deposit of the money with the stakeholder on terms that he is to keep it until one or other of the relevant events happens and then pay it to one or other of the parties accordingly. The stakeholder is a party to the second contract but not the first. His rights and obligations are not normally expressly spelled out. They are implicit in the transaction itself, and must be discovered, not by implying terms, but by analysing the relationship of the parties which arises from the deposit of the money.

The following propositions emerge from the authorities:

- (1). The relationship between the stakeholder and the depositors is contractual, not fiduciary. The money is not trust money; the stakeholder is not a trustee or agent; he is a principal who owes contractual obligations to the depositors: ... The underlying relationship is that of debtor and creditor, and is closely analogous to the relationship between a banker and his customer.
- (2). Until the specified event occurs, the stakeholder is entitled to retain the interest on the money. This is usually described as his reward for holding the money: ... This right may be excluded by special arrangement, and was excluded in the present case.
- (3). Until the event happens the stakeholder holds the money to the order of both depositors and is bound to pay it (strictly speaking an equivalent sum) to them or as they may jointly direct: ...
- (4). Subject to the above, the stakeholder is bound to await the happening of the event and then to pay the money to one or other of the parties according to the event. The money is payable to the party entitled on demand, and if the stakeholder fails to pay in accordance with a proper demand he is liable for interest from the date of the demand: ...
- (5). If the occurrence of the event is disputed, the stakeholder cannot safely pay either party, for if he mistakenly pays the party not entitled the payment will not discharge his liability to the other. In these circumstances he may (i) interplead and

- pay the money into Court; (ii) retain the money pending the resolution of the dispute; or (iii) take the risk of paying one party. The choice is entirely his.
- (6). If he takes the second course, he may notify the parties that he is content to abide the outcome of the dispute. There is then no need to join him in any proceedings which are taken to resolve it. If he is not joined, the Court cannot order the money to be paid to the successful party. All it can do is to declare that the successful party is entitled to give a good receipt for the money: ...
 - (7). If the stakeholder is not content to abide the outcome of the proceedings, he may be joined in order to bind him. This was done in the present case, albeit on the application of the stakeholder."

Analysis

There was plainly a tripartite stakeholder agreement between PB Logistics, PB Shipping and K Sit by which the Sum was held by K Sit pending proper documentary proof of the Debt. If not for the Stakeholder Arrangement offered on 16 July 2014, PB Shipping might have petitioned for PB Logistics' winding-up. It was very difficult to understand PB Logistics' contention that there was no tripartite stakeholder agreement.

Most of the arguments advanced on behalf of PB Logistics to contend that there was no tripartite agreement were without merit, eg, the suggestion that it was inconceivable that K Sit could on one hand act as the solicitors for PB Logistics and on the other hand as the stakeholder. It was plainly a bad point. Solicitors frequently wear 2 hats acting (a) for one of the parties to a transaction and (b) as the stakeholder for a payment in the transaction.

There were 2 other points advanced by PB Logistics to argue that the tripartite agreement in this case was uncertain. Firstly, the absence of time limit for PB Shipping to provide proper documentation to prove the Debt. Secondly, the arbiter of whether the Debt was proved was not agreed upon.

As to the first point, the law normally deals with it by way of an implied term that the evidence should be produced within a reasonable time. The Judge saw no reason why the case in question should be treated differently. In fact, PB Shipping's position was that proper documentation had indeed been provided to PB Logistics. The obstacle to the resolution of the matter was not delay in the provision of documentary proof but PB Logistics' disagreement with what was provided.

In respect of the lack of agreed mechanism by which the adequacy of the proof could be determined, oversight of such kind is not surprising in the absence of a detailed stakeholder agreement. However, if the adequacy of proof was disputed, no doubt the parties would expect the court to be the arbiter. That was what transpired in the case in question - PB Logistics duly took out HCA 1413/2014 for the matter to be resolved.

The Judge agreed with the following *dicta* of Millet LJ in *Manzanilla Ltd*, p 8 :

"In my judgment the Purchaser's first proposition is contrary to the ordinary understanding on which deposits are paid to stakeholders and on which the Court acts when resolving subsequent disputes as to the entitlement to the money. The parties do not foresee the existence of any dispute; they intend the money to abide the happening of an event; if there is a dispute whether the event has happened they expect the Court to resolve it; and the question for the Court will be whether the event has happened or not, because that is the determinative event."

Further, in the case in question it might be said that the dispute by PB Logistics and PB Shipping over the adequacy of the proper documentation for proving the Debt was overtaken by the proceedings initiated by PB Logistics.

The Judge did not agree with PB Logistics that K Sit had assumed the role of the arbiter under the Stakeholding Arrangement.

In the premises, there was no merit in the first issue in the appeal in question.

The second issue was even more difficult to understand. The allegation of collusion between K Sit and PB Logistics itself was based apparently on the proposition that K Sit was advancing PB Logistics' position on whether the Debt was sufficiently proved. Plainly, K Sit was discharging their duties as PB Logistics' solicitors. There was nothing in the point.

As for the alleged collusion with PB Shipping, it was based on nothing but the fact that K Sit had informed PB Shipping of SSW's request to have the Sum transferred to them and had refused to comply with SSW's request in the face of PB Shipping's objection. Pursuant to the Undertaking to Notify, K Sit was obliged to notify PB Shipping in respect of the requested transfer. Given the dispute between PB Logistics and PB Shipping over the transfer of the Sum to SSW, K Sit's position was governed under the 5th proposition stated in *Manzanilla Ltd*. If K Sit did not elicit PB Shipping's consent to the transfer, it would run the risk of being sued by PB Shipping. The Judge saw no basis for any accusation of collusion between K Sit and PB Shipping.

The Judge also saw no inexplicable delay in the case in question, save that of PB Logistics and PB Shipping over the resolution of HCA 1413/2014. As stakeholder, it was proper for K Sit to wait for the determination of the court in respect of the dispute over the Debt.

Disposition

For these reasons, PB Logistics' appeal was dismissed with costs to K Sit and PB Shipping.

Please feel free to contact us if you have any questions or you would like to have a copy of the Decision.

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