

Important Legal Update: Dealing with Foreign and the PRC states in Hong Kong

Overview: absolute (and not restrictive) immunity now applies in Hong Kong

Prior to the 1997 handover of Hong Kong, originating proceedings / suit could be maintained in Hong Kong in respect of a foreign or the Chinese state's commercial (as opposed to sovereign) activities, and enforcement could be sought against a foreign or the Chinese state's commercial (as opposed to sovereign) assets. This is known as "*restrictive immunity*".

Two recent decisions have confirmed that since the handover, the Hong Kong courts do not have jurisdiction to hear proceedings (including both suit and enforcement proceedings) against a foreign or the Chinese state (i.e. PRC), unless that state waives its right to immunity. This is known as "*absolute immunity*".

These decisions give rise to some important issues which must be considered when dealing with a foreign or the Chinese state, and associated entities, such as State Owned Entities (**SOEs**) and Sovereign Wealth Funds (**SWFs**). Different law (legislation) deals with the circumstances in which claims may be advanced against the Hong Kong Government.

Which entities are entitled to absolute immunity?

The Chinese and foreign states (governments, including local governments, and their institutional units) enjoy "absolute immunity" in Hong Kong. Unless they waive their right to immunity, the Hong Kong court has no jurisdiction to hear claims against them. We anticipate that governments (both foreign and the Chinese) will likely assert their right to immunity when sued in Hong Kong.

Commercial entities associated with the state, such as SOEs or SWFs, may also be entitled to absolute immunity in Hong Kong. This will depend on the facts of each case. It does not turn only on ownership of the SOE or the SWF, but instead on the control that the state actually exerted in respect of the deal in question. If the SOE/SWF was led and controlled by the state in the deal in respect of which it is sued, the SOE /SWF is entitled to assert immunity from the jurisdiction of the Hong Kong courts. A SWF or SOE might act independently of the state on one deal and under its control on another.

SOEs and SWFs are less likely to assert immunity in respect of their commercial deals, as this should cause others to price this risk into future transactions. The PRC Government has publicly stated that SOEs will not claim immunity in respect of commercial contracts. Even so, risk remains that an SOE or SWF will claim immunity from the Hong Kong courts if it was under the control of the state in respect of the deal upon which it is sued.

When will absolute immunity not apply?

Waiver

In Hong Kong, immunity can be waived in a state-to-state treaty; or by expressly submitting to the jurisdiction of the Hong Kong courts after court proceedings or enforcement action has been commenced.

Key Issues

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Which entities are entitled to absolute immunity?

When will absolute immunity not apply?

Important points to note when entering into agreements with foreign states, the PRC Government and entities possibly acting under their control

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NOTE: waiver of immunity clauses commonly included in commercial contracts with states, SOEs and SWFs will NOT be effective in Hong Kong (although such clauses will be effective in other jurisdictions, such as the United Kingdom).

Arbitration

Chinese and foreign states, SOEs and SWFs cannot claim immunity from the jurisdiction of a Hong Kong arbitral tribunal. These immunities apply only to Hong Kong courts.

NOTE: foreign and Hong Kong arbitral awards are enforced through the courts in Hong Kong. That means that the Chinese and foreign states, and possibly also SOEs and SWFs, might seek to claim immunity from execution of an arbitral award in Hong Kong, no matter where that award is made. However, the award can still be enforced against the state's commercial assets in the many other (mostly developed) jurisdictions which adopt "restrictive immunity".

Important points to note when entering into agreements with foreign states, the PRC Government and entities possibly acting under their control

1. **Jurisdiction:** Do not include Hong Kong court jurisdiction clauses. Do use arbitration clauses, or court clauses from jurisdictions which adopt restrictive (and not absolute) immunity (e.g. UK, Singapore, New South Wales). When choosing non-HK court jurisdictions, one has to bear in mind whether it's practical or feasible to enforce such court judgments in the location of the counter-party or its assets. For example, if you intend to enforce the judgment in the PRC, it may not be appropriate to opt for court jurisdiction clauses because enforcing a foreign judgment in the PRC is almost impossible.
2. **Waiver clauses:** Do include a contractual waiver of immunity in the agreement – such clauses are effective in other jurisdictions.
3. **Counter-party DD:** Consider: (i) whether there is any level of state control over your counter party (particularly when dealing with SOEs and SWFs); and (ii) the location of the counter party's commercial assets - specifically, seek to confirm that the counter party has commercial assets in "restrictive immunity" jurisdictions, outside of Hong Kong and China.
4. **Treaty protection:** Consider whether the deal can be structured so as to take advantage of a state-to-state treaty which protects the investment.
5. **Deal-specific advice:** If you are potentially dealing with a foreign state/PRC government entity, seek deal specific legal advice.

This Client briefing does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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