

Winston Establishes the Enforceability of Keepwell Bonds in Significant Hong Kong Court of Appeal Victory

Winston's London Restructuring practice scores a significant win on appeal for Hong Kong and BVI liquidator claimants in the People's Republic of China (PRC) based Peking University Founders Group Limited (PUFG) insolvency.

Working with a senior London barrister and local Hong Kong (HK) lawyers, our team were successful in overturning a contrary first instance decision. The team obtained a HK Court of Appeal judgment establishing for the first time that a PRC parent's obligations to its bond issuer and guarantor subsidiaries under an English law keepwell deed give rise to a debt including obligations to maintain balance sheet and cash flow.

This is a significant decision affecting an estimated \$36bn of PRC offshore bonds protected by a keepwell* rather than a guarantee structure. The use of keepwells—similar to a letter of intent—has been a common feature of financing arrangements for mainland business groups and foreign lenders in order to comply with PRC foreign exchange regulations. Between 2017 and 2018 PUFG issued US\$1.7bn of offshore bonds via two BVI issuers. The bonds were written under English law and listed in HK. Each issuance was protected by keepwell deeds which included obligations for PUFG to maintain the issuer's balance sheet and cash flow. These were direct commitments to the BVI issuers and their HK guarantor parents representing contractual obligations to ensure payment of the bonds from the ultimate parent PUFG.

PUFG commenced a restructuring process in PRC by order of the Beijing court on 19 February 2020 in order to deal with its estimated US\$13bn of debt. The appointed PRC administrators rejected direct claims made by the bond trustees referencing the non-binding provisions of PUFG's keepwell commitment. In response the bondholders petitioned for the winding up of the issuers (in BVI) and the guarantors (in HK). The liquidators of the issuers and the guarantors then jointly sought declarations as to the effectiveness of PUFG's direct obligations to their entities. Those obligations, in common with the commitments to the bond trustees, were included in the keepwell deeds. Unlike the bond trustee drafting, these obligations to the issuers and guarantors were expressed to be legally binding and the bond documents were expressed to be under English law enforceable in HK. In a contested series of preliminary hearings in 2022 the HK Court agreed that it had jurisdiction to grant declaratory relief on the English law terms and accepted the liquidators' arguments that the outcome would be of use to the Beijing Court having oversight of the PUFG restructuring.

In a first instance decision of the HK High Court in May 2023, Mr Justice Harris found that the majority of contractual breaches of the keepwell deeds had occurred after the date of the commencement of PUFG's restructuring and did not cause loss, leaving most of the liquidators' claims without an effective remedy. Winston's London Restructuring team were then engaged by the liquidators of the issuers and guarantors to work with local counsel in pursuing the appeal. In order to do so the team applied for the admission of leading London barrister, Mark Philips KC and prepared a detailed appeal, attending the two day hearing in the Court of Appeal of HK in January 2024. The Judgment handed down on Friday 10 May 2024 grants declaratory relief under English law stating that there has been a breach of the contractual obligations causing a loss of approx. \$1.7bn. The PUFG administrators have retained dividend payments to meet such claims in a sum exceeding \$500m.

The Winston team consisted of partner Paul Fleming, associates Suzanne Labi and Tringa Kunoviku and trainees Katrina Hughes and Tim Law.

**nb. keepwell deeds have been used to a lesser extent in other jurisdictions incl. Malaysia, Portugal, Germany, Japan, Switzerland, Canada and USA.*

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