

Provisional Liquidations & the Taxation of Fees

DID YOU KNOW...that interim fees incurred by provisional liquidators (including agents' fees), previously thought to have been payable from the funds of an insolvent estate without formal taxation, are now required to be taxed.

As you may know, the decisions of the Honourable Mr Justice Barma in *Re Lehman Brothers Securities Asia Ltd (No. 1)* [2010] 1 HKLRD 43 and *Re Lehman Brothers Securities Asia Ltd (No.2)* [2010] 1 HKLRD 58 (collectively "Lehman Decisions") represented the first occasions on which the Court formally authorised the payment of interim fees incurred by provisional liquidators (including agents' fees) on the basis that "...in certain circumstances the court need not be involved in assessing remuneration (as [his Lordship has] held to be the position in relation to the remuneration of the Provisional Liquidators' agents, at least until such time as there may be a challenge to the amounts paid or agreed to be paid to them, in the context of the passing of the Provisional Liquidators' accounts)..." .

The Lehman Decisions were made in the context of provisional liquidations (now liquidations) described by his Lordship in colloquial terms as "*mega-insolvencies*" and which were, based on the evidence before the Court, "...of a scale and complexity, so far as Hong Kong is concerned, that has rarely been seen. They are part of insolvency proceedings around the world (in particular in the United States, the United Kingdom and Japan) in respect of the failure of the Lehman Brothers group, which was until then the fourth largest investment bank in the United States..." . Combined with the then provisional liquidators having "*filed very extensive evidence dealing with their remuneration, in which they provided a great deal of detail as to the work which they, their staff and their agents have carried out, explaining the work that was done, the persons by who it was done, the time taken in respect of*

it, and the reasons for doing it..." ; the Court formed the view that it was not necessary for the then provisional liquidators to submit their agents' fees for assessment, although an assessor was appointed by the Court to assess the provisional liquidators' remuneration and to also "...report on the adequacy of the scrutiny brought to bear by the Provisional Liquidators in respect of their agents' fees" . As regards the assessor's role in respect of agents' fees, his Lordship made the following observation:

"It seems to me that since the Provisional Liquidators will be seeking payment (on an interim basis) out of the [Hong Kong Lehman Brothers] Companies' assets of funds to meet such fees, it would be appropriate for the Court to be satisfied, to the extent that this could be conveniently done, that they had exercised the appropriate care and had taken the appropriate steps in scrutinising such fees - this would, I think, reduce the risk of a later challenge, and thus reduce the possibility of an interim payment being made in an excessive amount."

As an additional measure so as to safeguard company funds, an undertaking was provided by the then provisional liquidators and their three principal firms of solicitors that they would repay any excess amount of the interim payment allowed (other than in respect of the fees of three firms of Hong Kong solicitors instructed by them) should such fees and disbursements ultimately be found to be less than the amount of the interim payments received by them.

The Lehman Decisions were significant as the prevailing view among practitioners in the past had been that bills rendered by agents engaged by provisional liquidators should be taxed pursuant to a set of "Procedural Guides for Taxation / Determination of Bills in Liquidation Process" issued by the Court in 2004 ("Guidelines").

Accordingly, not only did the Lehman Decisions represent a departure from the approach previously required by the Guidelines, but they also demonstrated the Court's willingness to adopt a more flexible approach to the approval and payment of interim fees in large-scale insolvencies in circumstances where the practitioners themselves had already scrutinised their agents' fees and come to an agreed amount that the insolvent estate should bear.

A Change of Position in Respect of Fees

In the recent decision of *Re MF Global Hong Kong Limited HCCW 356/2011* ("MF Global"), another provisional liquidation of uncommon scale and complexity, the Honourable Mr. Justice Harris has reviewed the position on the approval and payment of interim fees incurred by provisional liquidators, holding that:

- the Lehman Decisions did not permit provisional liquidators to scrutinise the bills of costs or charges of agents so as to determine those bills for themselves and then make payment in respect of the same out of the estate without further involvement of the Court. His Lordship held that the Court is "*...concerned with the payment of costs and expenses out of the assets of an insolvent company*" such that he "*...can see no reason why the court should not require taxation (or possibly some other approval process as was the case in Lehman Brothers Securities Asia Limited (No. 2)) of such expenses*";

- the interpretation of the Lehman Decisions as no longer requiring the Taxing Masters to tax the fees of agents engaged by provisional liquidators was incorrect; and
- future fees and expenses should be taxed.

The MF Global decision represents a reversion to the practice of requiring fees and expenses incurred in a provisional liquidation to be taxed (or any commensurable determination process) and practitioners (and their agents alike) should be aware of this change in practice.

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