Without Prejudice Settlement Held Binding Despite the Absence of a Formal Deed: Re MSB International Limited [2022] HKCFI 3751

Introduction

On 15 December 2022, the Court of First Instance (Hon Linda Chan J) handed down judgment in Re MSB International Limited [2022] HKCFI 3751, holding that a binding settlement agreement had been reached between the parties through a series of "without prejudice" letters and emails, notwithstanding the absence of a formal executed deed. The Court granted a stay of HCA 400 and HCCW 386, save for the purpose of enforcing the settlement terms. Our Mr Conti Wong and Dr. Simon Wu summarise the key takeaways for insolvency practitioners, litigators and creditors.

Background

MSB International Limited ("**MSB**") is a Hong Kong horse feed trader. MSB was originally owned by Sammy Tsui ("**Sammy**") and Morten Lok ("**Morten**"). In 2014, Sammy transferred his shareholding to Morten, who in turn transferred it to Ben Tsui ("**Ben**") in 2018. Subsequently, Ben and Sammy alleged that Morten was in control of a competitor company, which Morten denied. MSB sued Morten for breach of fiduciary duty and Keson Limited ("**Keson**") for dishonest assistance. On the other hand, Morten petitioned to wind up MSB on just and equitable grounds, alternatively seeking payment of a dividend and a share buy-out.

Settlement & Breakdown

From February to March 2022, the parties' solicitors negotiated a settlement. Cheung & Yip ("C&Y") for Ben, Sammy and MSB, and Tanner De Witt ("TDW") for Morten and Keson, exchanged offers and counter-offers on a "without prejudice as to costs" basis. On 22 March 2022, C&Y accepted TDW's HK$3 million offer plus other terms to settle the parties' disputes ("Settlement Agreement"). However, when putting the Settlement Agreement in formal writing, TDW proposed an additional term extending the release to related persons and entities, which the parties could not agree. That marked the breakdown of the settlement attempt. Morten and Keson asserted that the Settlement Agreement had always been subject to conditions and that no binding agreement arose. MSB, Ben and Sammy, on the other hand, sought specific enforcement of the Settlement Agreement.and the fund service company, failed to provide all requested documents and information.

The Court's Decision

Two issues were identified:

1. Whether TDW's HK$3 million offer was subject to conditions; and
2. If not, whether the terms agreed were sufficiently certain and complete to give rise to a binding agreement.

The Hong Kong Court of First Instance, presided over by the Honourable Madam Justice Linda Chan, held that:

- TDW's offer was **NOT** subject to those conditions;

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- A binding settlement agreement was made on 22 March 2022 when C&Y accepted TDW's offer;
- The settlement agreement was sufficiently certain and complete;
- The proceedings in HCA 400 and HCCW 386 should be stayed, save for the purpose of enforcing the settlement terms.

No "subject to contract" nor "subject to conditions"

The Court applied the objective test for contract formation, asking whether, looking at the correspondence as a whole, the parties intended to create legal relations and had agreed upon all essential terms.

- **No "subject to contract" in the key correspondence:** None of the letters or emails exchanged during the key negotiation period stated that the offers were subject to execution of any contract or deed.
- **"Deliberate omission" explanation rejected:** TDW's explanation that the omission of "subject to contract" was a deliberate choice was rejected as making "very little sense".
- **Not subject to conditions:** While TDW alleged that it had informed C&Y during telephone conversations that the negotiations were subject to conditions, the Court did not accept that those conditions had been stated. Alternatively, even if they had been stated, the Court held that TDW did not insist upon them in its subsequent written correspondence and had therefore waived them.
- **Post-agreement negotiations did not make the agreement conditional:** Negotiating further terms did not render the earlier binding agreement conditional.

Sufficiently certain and complete

The Court held that it was not open to Morten and Keson to argue uncertainty on essential terms when they had not taken issue in their evidence. In any event, the arguments had no merit:

- **Certainty of Parties:** The negotiations were conducted on the basis that MSB and Keson were parties to, and would be bound by the settlement. MSB had to waive its claim, while Keson was a party to HCA400 and was represented by TDW. Both were subsequently named as parties in the draft settlement agreement.
- **Certainty of Scope:** The terms were readily ascertainable from the correspondence. There was nothing uncertain about a settlement covering ongoing proceedings but not potential claims.
- **Costs:** The question of costs was dealt with in the undisputed terms set out in C&Y's letter to TDW dated 12 March 2022.

Significance of the Judgment and Practical Tips

This case provides welcome clarity on the enforceability of settlements reached through "without prejudice" correspondence. Key takeaways include:

1. **Objective test governs:** The parties' subjective beliefs are irrelevant. What matters is what was communicated by words or conduct and whether an objective observer would conclude that the parties intended to be bound.
2. **"Subject to contract" matters:** If the parties do not intend to be bound until a formal settlement agreement or deed is executed, that qualification should be stated expressly and consistently in the settlement correspondence, particularly in any offer, counter-offer or purported acceptance. The absence of such a qualification, particularly in a series of formal offers and counter-offers with stated deadlines, may weigh heavily in favour of a binding agreement.

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3. **Do not confuse "without prejudice" with "subject to contract":** "Without prejudice" concerns the protected status of settlement communications; it does not, by itself, prevent an offer and acceptance in those communications from creating a binding settlement. If no binding settlement is intended until formal documentation is executed, this should be stated expressly.
4. **Record oral qualifications in writing:** If an offer is subject to a condition mentioned during a telephone conversation, confirm that condition promptly in the subsequent written correspondence. Do not assume that an earlier oral qualification will continue to govern a later written offer or counter-offer. Where clarity is important, practitioners should keep material settlement communications in writing and promptly confirm any oral discussions. A request that future correspondence be put in writing may help to avoid later disputes about what was said.
5. **Use contractual language deliberately:** Expressions such as "offer", "final offer", "open for acceptance until", "automatically lapses" and "we accept" may strongly indicate an intention to create an immediately binding agreement. If that is not intended, make the offer expressly subject to contract or to execution of the formal settlement documentation.
6. **Drafting and negotiation of formal documents:** A subsequent formalisation exercise does not necessarily reopen an agreement already concluded. Parties may negotiate additional terms or implementation mechanics in a later "subject to contract" document without displacing an earlier binding settlement. Practitioners should therefore make clear whether the later document merely records or implements an existing settlement, or whether its execution is a condition to any settlement becoming binding.
7. **Certainty and completeness:** A settlement agreement covering ongoing proceedings need not cover all potential claims to be enforceable.
8. **Define the scope of the release at the offer stage:** Identify the parties and proceedings covered, whether the release extends to existing, potential or unknown claims, and whether affiliates, directors, shareholders, employees or other related persons are included. An important "clean break" or third-party release should not be left until the formal settlement document is drafted.
9. **Practical implications for insolvency practitioners and creditors:** Where a settlement is reached in the context of winding-up or bankruptcy proceedings, the parties should be clear as to whether the terms are binding. If execution of a formal deed is intended to be a condition of the settlement becoming binding, this should be expressly stated. Otherwise, the Court may find that a binding agreement has already been concluded and stay the underling proceedings accordingly.

Conclusion

The judgment confirms that a binding settlement can be reached through an exchange of "without prejudice" correspondence, even where the parties subsequently negotiate a formal written agreement. The decision underscores the importance of clarity in settlement negotiations, particularly regarding whether terms are intended to be binding or subject to contract. Where parties wish to avoid being bound until a formal deed is executed, they must expressly say so. The case also reaffirms the Court's willingness to stay proceedings where a binding settlement has been reached, in order to give effect to the parties' agreement.

For further details, please refer to the full judgment [2022] HKCFI 3751 (15 December 2022):
https://legalref.judiciary.hk/lrs/common/ju/ju_frame.jsp?DIS=149400&currpage=T

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Authors

Mr. Conti Wong, Partner, Commercial Litigation Department
Email: contiwong@pclawyers.com.hk

Dr. Simon Wu, Consultant
Email : simonwu@pclawyers.com.hk

Mr. Billy Tan, Trainee Solicitor
Email: billytan@pclawyers.com.hk

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