

The Issuance and Transfer of Digital Bonds under Hong Kong Private Law

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The clear potential and use cases of digital assets continue to expand across many different fronts and sectors. Hong Kong SAR and Singapore have already developed into important digital asset hubs. Each city benefits from supportive government positions, stream-lined regulatory frameworks, and robust financial markets infrastructures.

Legal certainty and balanced regulation of the many different forms of digital assets are necessary steps to continue the development of these markets. Moreover, consistent standards and legal frameworks across jurisdictions are required given the borderless nature of these products.

Hong Kong SAR and Singapore share many fundamental principles with English common law. Recent English law developments, including the work of the UK Jurisdictional Taskforce of LawtechUK and the Law Commission of England and Wales, have provided important clarity to the legal treatment of digital assets.

This paper considers whether Hong Kong law can support the issuance and transfer of debt securities using a system deploying DLT such as blockchain and concludes that Hong Kong law is sufficiently flexible and resilient to accommodate the issuance and transfer of these debt securities to serve the needs of market participants. We have also published a [separate paper](#) considering similar issues under Singapore law and have arrived at a similar conclusion.

We believe that Hong Kong and Singapore are well positioned to be global leaders in the next stage of digital asset development. We look forward to working closely with all market participants on next steps to continue the development and maturation of this innovative and transformative asset class.



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The digital assets landscape has evolved enormously since the introduction of Bitcoin, the first cryptocurrency, in 2009. In recent years, emerging distributed ledger technologies (“**DLT**”) like blockchain have been a catalyst for innovation in the financial markets. Infrastructure providers, both existing and prospective, have sought to utilise these new technologies to redesign the building blocks of financial market infrastructures. Existing financial products are likewise undergoing transformation. DLT-based technology including blockchain has been innovatively deployed both in digital securities issuances as well as to tokenise other real world assets.

In Europe, the development of the digital capital markets has been spearheaded by multilateral financial institutions such as the European Investment Bank (EIB) with its pioneer digital bond issues.¹ The European Securities and Markets Authority (ESMA) has also proposed a pilot regime to enable regulated institutions to develop DLT-based infrastructure.² In Hong Kong, the push towards tokenisation has similarly been from government initiatives. In February 2023, the Hong Kong SAR Government issued the first tokenised green bond³, setting a benchmark for the market for issuances of this type. The Hong Kong Government has also since released a report to summarise its experience from the tokenised green bond offering and outline potential next steps to promote the wider use of tokenisation technology in Hong Kong’s bond market.⁴ Issuers in the financial sector have similarly shown an interest in digital debt securities issuances and this is not confined to vanilla debt.

For example, issuers have issued digital structured notes⁵ and there is also interest in other financial asset classes such as digital funds and digital certificates of deposit.

These recent developments reflect the Hong Kong Government’s policy of and regulators’ continuous support of⁶ promoting Hong Kong as a sustainable digital hub and come against the backdrop of a growing digitalization effort in Asia. The digital securities market in Singapore has also been developing quickly in recent years. Digital asset exchanges and platforms which started under the Monetary Authority of Singapore’s (“**MAS**”) sandbox schemes, have completed their sandbox trial and have formally commenced operations. Today, there are several digital asset exchanges and platforms that have already been operating for a number of years. The Monetary Authority of Singapore’s commitment to developing Singapore’s digital ecosystem is also evident through initiatives such as Project Guardian, a collaborative initiative by the government with the financial industry to test the feasibility of applications in asset tokenisation and decentralised finance.⁷

Digital assets-specific legislation?

Given the novelty of digital assets, some civil law jurisdictions⁸ have enacted specific legislation or digital assets laws to give express recognition to the creation of digital assets and their dealings, with the hope that the legal certainty provided by the relevant legislation will encourage the growth of digital assets in their respective markets. Conversely, as a common law jurisdiction, the United Kingdom has not enacted any specific legislation on digital assets and questions have been raised as to whether the UK should do so to deal with any perceived uncertainties of the position under English law.

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- 1 EIB issues its first ever digital bond on a public blockchain issued by the European Investment Bank on 28 April 2021 (see [link](#)).
 - 2 ESMA publishes its report on the DLT Pilot regime issued by the European Securities and Markets Authority on 27 September 2022 (see [link](#)). In the United States, the trend towards tokenisation can also be observed, for example, by recent issues of tokenised treasury bonds. *Demand for Tokenized Treasury Bonds Soars as Crypto Investors Chase TradFi Yield* issued by CoinDesk on 23 May 2023 (see [link](#)). Regulators have also sought to help market participants in categorising their tokens to see if these are regulated as investment contracts or securities. *Infrastructure Tokenization: Does blockchain have a role in the financing of infrastructure* issued by the World Bank on 22 March 2023 (see [link](#)).
 - 3 HKSAR Government’s Inaugural Tokenised Green Bond Offering issued by the Hong Kong Monetary Authority on 16 February 2023 (see [link](#)).
 - 4 Report on Bond Tokenisation in Hong Kong issued by the Hong Kong Monetary Authority (“**HKMA**”) on 24 August 2023 (see [link](#)).
 - 5 BOCI issued the first tokenized notes, originated by UBS and placed to its clients in Hong Kong as announced by UBS on 9 June 2023 (the “**BOCI/UBS Deal**”) (see [link](#)).
 - 6 The HKMA and the Securities and Futures Commission (the “**SFC**”) issued a Joint circular on intermediaries’ virtual asset-related activities in January 2022, providing guidance for intermediaries who wish to engage in virtual asset-related activities and distribute virtual asset-related products (see [link](#)). This was followed by the SFC’s issuance of the Consultation Paper on the Proposed Regulatory Requirements for Virtual Asset Trading Platform Operators Licensed by the Securities and Futures Commission on regulatory requirements applicable to licensed virtual asset trading platform operators in February 2023. In May 2023, the SFC published its consultation conclusions, proposing to give retail access to virtual asset trading services (see [link](#)). In the market, HashKey Exchange and OSL have become the first cryptocurrency exchanges in Hong Kong to secure licences for retail investors to trade on their platforms, only two months after the SFC published its consultation conclusions (see [link](#)). On a related note, following the issuance of the Discussion Paper on Crypto-assets and Stablecoins in early 2022, the HKMA published the related conclusion paper, aiming to put in place a proposed new stablecoin regulatory framework by 2024 (see [link](#)).
 - 7 Project Guardian: Enabling Open & Interoperable Networks issued by the Monetary Authority of Singapore on 19 October 2022 (see [link](#)).
 - 8 Various civil law jurisdictions such as France, Switzerland, Liechtenstein, Germany and Malta have codified rules relating to digital assets. Some of these have been noted in paragraph 2.40 of *Digital assets: Final Report (Law Com No 412)* issued by the Law Commission of England and Wales on 28 June 2023 (the “**Law Commission Report**”). (see [link](#))

In the UK, in February 2023, the UK Jurisdictional Taskforce of LawtechUK (the “**UKJT**”) published its second legal statement on the issuance and transfer of digital securities under English private law (the “**UKJT Paper**”).⁹ The UKJT Paper addressed the critical questions of whether equity, debt or other securities can be validly issued and transferred under English law using DLT such as blockchain systems. The UKJT Paper concluded that, subject to the satisfaction of certain corporate requirements which primarily apply to digital shares in UK companies, English law can accommodate digital securities being circulated on a blockchain. With respect to debt and other contractual securities where issuers have freedom to choose the governing law, English law has been a preferred legal system for traditional debt securities in the euromarket. The UKJT paper confirms that English law can accommodate digital securities being circulated on a blockchain. The UKJT Paper confirmed that English law, in particular because of the inherent flexibility of the common law, can accommodate novel asset classes and financial structures such as digital securities without statutory intervention.

Following the publication of the UKJT Paper, in June 2023 the Law Commission of England and Wales released its final report on digital assets (the “**Law Commission Report**”) which focuses on crypto/intangible assets and sets out recommendations for statutory reform and common law development.¹⁰ While the report contains some recommendations for reform, the Law Commission Report concludes that the common law system in the UK is well placed to provide a coherent and globally relevant regime for existing and new types of digital assets, and that the common law is sufficiently resilient and flexible to accommodate new digital asset classes.

Hong Kong has deep and well-established capital markets and is an attractive venue for issuers (whether local or overseas-incorporated) to raise capital, including, potentially via the issuance of digital securities. There is flexibility in terms of the governing law for such issuances. Where the parties to a contract have chosen a foreign governing law, for example, English law, Hong Kong courts will generally recognise the choice of law.¹¹ Issuers may equally wish to use Hong Kong law as the governing law for their issuances of digital securities if the factual circumstances point towards that choice. For example, this may be where the investors are primarily located in Hong Kong and the Greater China region or where the issuances are denominated in Hong Kong dollars or offshore Renminbi. Government-linked or government-backed issuers as well as corporate issuers which have their centre of main interests in Hong Kong typically have a strong preference towards using Hong Kong law as the governing law.

As a common law jurisdiction, Hong Kong law has inherent flexibility that enables it to adapt to accommodate novel asset classes to meet commercial needs. For example, Hong Kong courts have recognised cryptocurrencies as a new category of “thing” to which personal property rights can attach.¹² The Hong Kong courts’ decision demonstrates that Hong Kong common law can be a firm foundation for the continued development of the digital securities market in Hong Kong.

In considering the application of Hong Kong legal principles to new financial structures, Hong Kong courts also frequently make references to the evolving jurisprudence in other common law jurisdictions. Given the common principles and approach across common law jurisdictions, there is substantial consistency in terms of the legal approach to digital securities and commonality in terms of the legal solutions adopted. This paper analyses similar issues as the UKJT paper (as supported by the Law Commission Report) under Hong Kong private law. It concludes that there is sufficient certainty under Hong Kong law to accommodate digital bonds, and that there is no need for widespread law reform for the valid issuance and transfer of digital bonds.



⁹ *Legal Statement on the issuance and transfer of digital securities under English private law* issued by the UKJT on 9 February 2023 (see [link](#)).

¹⁰ The Law Commission Report (see [link](#)). Note that the Law Commission Report mainly focuses on crypto-tokens (which is defined as “a notional quantity unit manifested by the combination of the active operation of software by a network of participants and network-instantiated data” (see page ix of the Law Commission Report)).

¹¹ Subject to the choice being *bona fide*, legal and not against public policy. See Paul Harris, *The Conflicts of Laws in Hong Kong* (Third Edition) (Sweet & Maxwell, 2017) at paragraph 5.005.

¹² *Re Gatecoin Limited (In Liquidation)* [2023] HKCFI 914 which recognizes the proprietary status of crypto currencies. A cryptocurrency is a digital asset based on blockchain technology, which records transaction data in a list of records (a block) with a timestamp, and one block is linked to another by cryptography (per Chan J, paragraph 12) (see [judgment](#)). Chan J considered common law authorities before concluding that crypto currencies are “property” which can be the subject matter of a trust. The existence of a third category of “thing” to which personal property rights can relate and the characteristics of this third category has been discussed in the Law Commission Report. The existing categories are chose in possession and chose in action.



Scope

This paper focuses on the question of whether Hong Kong law can support the issuance and transfer of debt securities using a system deploying DLT such as blockchain systems. The UKJT Paper discussed three types of digital securities: namely, digital bonds (ie digital debt securities), digital proprietary securities and digital shares (ie digital equity securities). However, given that there are potentially more initial use cases of tokenisation of bonds in the Hong Kong markets, this paper focuses on digital bonds.¹³ We note in particular that digital shares in Hong Kong companies raise a number of specific questions relating to corporate requirements imposed by the Companies Ordinance (Cap. 622, Laws of Hong Kong) (the “CO”), and these are beyond the scope of this paper.¹⁴



Forms of digital bonds

Native or non-native issuance?

A digital bond issuance can be structured as “native” or “non-native”. The term “native” in the context of digital debt securities refers to digital bonds issued directly on a DLT platform. In contrast, the term “non-native” refers to bonds first issued off-platform and then tokenised on a DLT platform.

As a starting point, the more common structure is a “non-native” issuance whereby the bonds are first issued off-chain and then tokenised on-chain. Conventional bonds may, for example, be issued into a top-level intermediary such as a central securities depository (“CSD”) and credited to the account of a participant in the CSD’s system before such bonds are tokenised.¹⁵ Under such a non-native, immobilization structure, fewer enforcement issues should arise since the intermediary or off-chain holder of the bonds has express rights to act against the issuer and can enforce the interests of holders. The more legally challenging scenario is where there is no intermediation and the digital bonds are created directly in the blockchain as native tokens. In that scenario, the holders’ rights as against the issuer and other third parties would depend entirely on the creation and transfer of such rights in the blockchain under Hong Kong law.

Bearer, registered and claim tokens

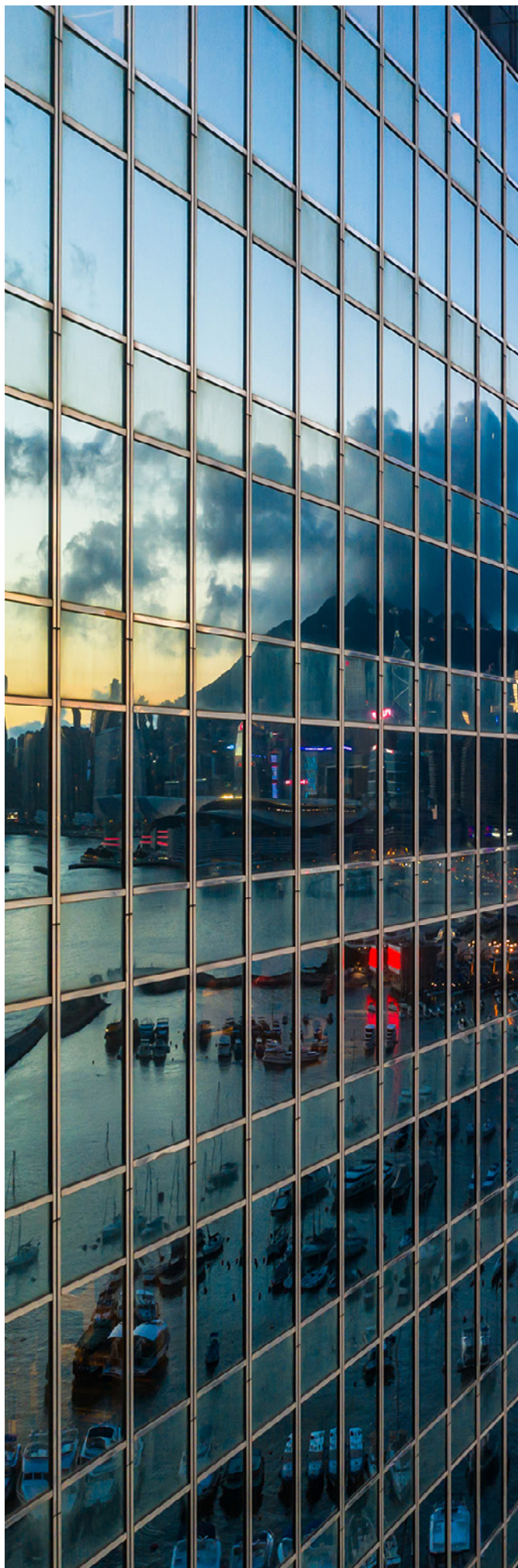
DLT such as blockchain systems can potentially facilitate the issuance of digital bonds (whether native or non-native) in the following main forms: (i) bearer form (the term we use in this paper is “bearer tokens”); (ii) registered form (ie registered tokens); or (iii) a form whereby the holder is identified by reference to records maintained by a third-party operator (acting in a principal capacity) (ie claims tokens):

- > **Bearer tokens:** These can be said to be digital replications of traditional bearer bonds. A bearer token is an intangible asset in its own right; the person who controls the token can exercise the rights to which the token holder is entitled. A bearer token is transferred via the transfer of practical control of the token (ie via the transfer of the token itself);
- > **Registered tokens:** Registered tokens may be seen merely as part of a record or data evidencing the holder of the relevant digital bond. Registered tokens are tracked and managed through a centralised registry system. Holders of the tokens, who are eligible to exercise their associated rights, are identified and recorded in a register maintained and controlled by a registrar which may be the issuer or an agent appointed by the issuer. The registrar’s primary function is to facilitate the transfer and updating of registered tokens during transactions through the entries on the register (which may be off-chain or on-chain);

¹³ Please refer to the definitions and various forms of digital bonds below.

¹⁴ The Law Commission Report and the UKJT Paper also acknowledge that the tokenisation of equity and registered corporate securities is less straightforward (see paragraph 8.78 of the Law Commission Report and paragraph 19 of the UKJT Paper).

¹⁵ An example of a “non-native” issuance is the Hong Kong Government’s tokenised green bond offering. These were registered tokenised bonds first issued in registered form off-platform and then tokenised on a DLT platform.



- > **Claims tokens:** Claims tokens are also mere data or evidence of rights. Such rights are determined by reference to entries in a DLT-based system controlled by a third-party operator rather than by the issuer or its agent as for registered tokens. The transfer mechanism refers to the updating of token balances recorded to a smart contract deployed by the operator.

Please see diagrams illustrating these three forms at the [Appendix](#).

Each form of token may give rise to different legal issues, irrespective of whether the securities are directly issued on the blockchain as “native” tokens or are issued indirectly by or through intermediaries as non-native tokens. Compared to bearer tokens, registered tokens and claims tokens may not give rise to as many novel legal issues under Hong Kong law: conventional registered bond structures already use electronic databases to record and effect transfers of beneficial interests in bonds without significant difficulty and it may not be a huge leap from an electronic database to one maintained on chain. Consistent with the approach under the UKJT paper, we have therefore focussed this paper on digital bonds intended to be capable of circulation without custodians or any other form of intermediation as these present more novel issues. Nevertheless, our discussion in this paper applies generally across all three types of tokens, including registered tokens and claims tokens save as specified otherwise.



In order to determine whether the various types of digital debt securities can be created and transferred, a number of legal issues have to be considered. Some of these issues are ones which capital markets lawyers will be very familiar with but with the added nuances presented by the digital or DLT element. As such, we consider the following key legal issues in connection with the issuance and transfer of digital bonds under Hong Kong law:

- > whether and how rights and interests can be “stapled” to digital bonds with the effect that holders would have direct rights against the issuer and can prevail over other third parties;
- > what the formalities are for the issuance and transfer of digital bonds; and
- > whether, in relation to Hong Kong-incorporated companies, local corporate law requirements can be met for the issuance and transfer of digital bonds.

Stapling

The purpose of stapling is to ensure that rights in respect of the token inherently form part of the token such that token holders obtain indefeasible rights upon issuance and on subsequent transfer of the token. The UKJT Paper¹⁶ describes stapling as referring to “a legal mechanism whereby the holder of a legal right or interest in an asset is identified by reference to a crypto asset, or to another digital object of property or a ledger record that is not itself an object of property (in the case of registered or similar structures)”.

Creation and issuance

The importance of ensuring that a digital security is validly constituted or issued is two-fold. First, the holder of the digital securities will need to ensure that it has direct rights as against the issuer. From the perspective of the issuer, it will need to make sure that its debt or other obligations in respect of the digital securities will be fully discharged upon payment to the holder of the digital securities. To put this in other words, in response to the question “who can exercise rights upon valid creation and issuance of a digital bond?” If rights are “stapled” to a bearer token, the answer would be that the controller of the token can exercise such rights. Conversely, if rights are “stapled” to a registered or claims token, the answer would be that you would look to the register or ledger to identify who can exercise such rights.¹⁷

Transferability

The importance of ensuring that a digital bond is validly constituted or issued is also pertinent on transfer: upon transfer of a digital bond, the rights or interests associated with it should simultaneously and automatically be transferred without the need for further acts or formalities.

While there is a direct relationship between the issuer and the first holder of a digital bond, as between the issuer and a subsequent transferee of the bond, there may not be any direct relationship and there is no privity of contract. A transferee will of course want to ensure that, by virtue of its control of the token, it can exercise rights against the issuer. From the perspective of the issuer, it will want to ensure that its obligations in respect of the digital bonds are fully discharged by payment to the holder, free from the assertion of claims by intervening holders.

Negotiability

As negotiable instruments, conventional bearer bonds, by virtue of mercantile custom,¹⁸ can be transferred by physical delivery without the need for a separate written document of transfer or notice to the issuer. Transferees also take the bonds free of any defects in the title of the transferor or of prior transferors, provided that such transfer is consistent with the intention of the transferor and provided that the transferee has taken the instrument in good faith for value and without notice of any previous defect in title. The question then becomes whether bearer tokens likewise have negotiable status.

¹⁶ Paragraph 85 of the UKJT Paper as endorsed by the Law Commission in the Law Commission Report in footnote 854.

¹⁷ In practical terms, suitable drafting would be included in the terms and conditions to the effect that the person entitled to exercise rights and interests in respect of the token is determined by the ledger record or entry in the DLT-based system used to identify the holder of the tokens.

¹⁸ Paragraphs 53-54 of the UKJT Paper, citing *Edelstein v Schuler & Co* [1902] 2 KB 144. Mercantile usage must be:

- i. notorious (*Tucker v Linger* (1883) 8 App. Cas. 508.);
- ii. certain (*Sewell v Corp* (1824) 1 C. & P. 392, 393; *Devonald v Rosser & Sons* [1906] 2 K.B. 728, 743.);
- iii. reasonable (*Paxton v Courtney* (1860) 2 F & F 131; *Tucker v Linger*, above; *Gibbon v Pease* [1905] 1 K.B. 810.); and
- iv. there must be general usage, ie one recognised and adopted by the commercial world in general (*Easton v London Joint Stock Bank* (1886) 34 Ch. D. 95, 113; reversed on a different point sub nom. *Sheffield v London Joint Stock Bank* (1888) 13 App. Cas. 333).

There is no intrinsic reason why a bearer token used to represent a digital bond should be treated any differently from a paper instrument used to represent a conventional bearer bond. However, as bearer tokens are newly developed instruments, it is arguable that mercantile custom granting bearer tokens the status of negotiability has yet to arise and so a bearer token cannot, properly speaking, currently be treated as “negotiable”. Nevertheless, we anticipate that the mercantile custom for bearer tokens will develop¹⁹ so that bearer tokens can be treated as negotiable instruments in the debt capital markets in the near future and, if so, the common law will be receptive and give effect to that practice. Even in the absence of mercantile custom, as a bearer token is a contractual arrangement between the issuer and the holders,²⁰ for all practical purposes, the legal effects of negotiability can be achieved by stapling the interests or rights onto the bearer token. It is apparent that stapling emulates the legal effect of negotiability via appropriate drafting and structuring.

Unlike bearer bonds (and bearer tokens), registered tokens and claims tokens are, by definition and in nature, not negotiable instruments. Nevertheless, this will not affect the transferability and tradability of registered and claims tokens. As discussed below, if rights are “stapled” to a ledger record or entry in a blockchain or DLT-based system evidencing the holder of the registered or claims tokens, the person entitled to exercise rights in respect of the relevant token will be determined by the ledger record or entry used to identify the holder of the token.²¹

Stapling techniques in the context of bearer, registered and claims tokens

Stapling as a legal technique, is clearly critical for bearer tokens. In this context, it is frequently said that rights or interests are stapled to the bearer tokens itself, enabling the tokens to be validly issued and transferred using a blockchain or DLT-based system.

In the context of registered tokens and claims tokens where a blockchain or DLT-based system is used as a register or record, rights or interests can be said to be “stapled” to a ledger record or entry in a blockchain or DLT-based system evidencing the holder of the bonds. In practical terms, suitable drafting would be included in the terms and conditions to the effect that the person entitled to exercise rights and interests in respect of the digital bonds is determined by the ledger record or entry in the DLT-based system used to identify the holder of the bonds.

Various options discussed in the UKJT Paper can be used to staple legal rights in digital debt securities under Hong Kong law, as follows:

- i. deed poll;
- ii. third party rights legislation;
- iii. open offer;
- iv. advance consent to transfer by way of novation; or
- v. use of a multilateral contractual framework.²²

We discuss each of these stapling techniques in turn.

(i) Deed poll

A deed poll is a unilateral promise by the maker that can be enforced by a person without being a party to the deed, provided they are named or sufficiently identified as the person for whose benefit the promise is made. A deed poll is commonly used where a party to a transaction wishes to confer rights on one or more other parties but it is not practicable to have each of the other parties physically executing an agreement. In the debt capital markets, a deed poll is most commonly used to confer upon the holder of the debt securities direct rights against the issuer. The deed poll allows for suitable drafting of provisions reflecting parties’ intention thus providing contractual certainty.

In conventional bond issuances, in addition to the use of deeds poll, a trustee structure is also frequently used whereby a third party trustee holds the issuer’s promise to pay principal and interest on trust for the bondholders under a trust deed. Any action to be taken under the bonds would be taken by the trustee on behalf of the bondholders, and individual bondholders have no right to sue the issuer but can only direct the trustee to sue by way of bondholders’ resolutions. We see no difficulty in constituting a digital bond using a trust deed.

(ii) Third party rights

Under Hong Kong law, a similar outcome could be achieved without the use of a deed poll, by virtue of the Contracts (Rights of Third Party) Ordinance (Cap. 623, Laws of Hong Kong) (the “**Third Party Rights Ordinance**”). The Third Party Rights Ordinance confers a third party a right to enforce a term of a contract where (i) the contract expressly provides that the third party may do so; or (ii) the term purports to confer a benefit on the third party.²³ In both situations, the third party must be expressly identified in the contract by name or as a member of a “class”.²⁴ For practical purposes, this would mean that the terms of the digital bonds should be carefully drafted to ensure that defined third party rights were conferred on a “class” of persons, namely each potential holder from time to time of the applicable digital bond.

19 The usage need not be of long standing, but it must have prevailed for a sufficiently long period in order to achieve certainty and notoriety. Thus, the courts may give effect to mercantile usage which establishes the validity of any new kinds of negotiable instruments. See Hugh Beale, *Chitty on Contracts* (34th Edition, 2022) at paragraph 36-005.

20 See paragraphs 55-57 of the UKJT Paper as endorsed by the Law Commission in the Law Commission Report at paragraph 8.12.

21 Paragraph 88 of the UKJT Paper.

22 Paragraph 88 of the UKJT Paper.

23 Section 4(1) of the Third Party Rights Ordinance.

24 Section 4(2) of the Third Party Rights Ordinance.

Lists of classes or terms of contracts, including “*negotiable instruments*” have been carved out from the application of the Third Party Rights Ordinance.²⁵ As discussed, bearer tokens are likely to be categorized as “negotiable instruments” under Hong Kong law. A transferee can sue directly under the negotiable instrument and would not need to rely on the Third Party Rights Ordinance. Nevertheless, third party statutory protection is applicable to registered tokens and claims tokens.

(iii) Open offer

Another stapling technique involves creating a direct contractual agreement between the issuer and each investor through an open offer made by the issuer. This common law approach could equally have application in Hong Kong. Under Hong Kong law, an issuer may offer to contract with any investor who agrees to a transaction on the basis of a set of pre-established terms of issue through the system. The terms of the issue would constitute a direct contractual relationship between the issuer and each investor. The terms could further be drafted to the effect that the issuer and each investor are released from their obligations to one another upon transfer of the digital bonds.

(iv) Advance consent to transfer by way of novation

Alternatively, interests could be stapled onto digital bonds by way of novation. Upon novation, rights and obligations pursuant to the terms of the digital bonds are extinguished between the issuer and the transferor, and a new contract between the issuer and the transferee will be created on the same terms (except, of course, as to the parties).²⁶ This stapling mechanism is the same principle frequently adopted in syndicated loan transactions in governing the relationship between each of the syndicated lender banks and the borrower, where an original lender party to the loan agreement may transfer by novation its rights and obligations under the loan agreement to a syndicate lender without consent of the borrower or other parties to the loan agreement on the basis that the borrower and other parties to the agreement had pre-consented to such future transfer by novation provided certain conditions are fulfilled.

(v) Multilateral contractual framework

Another method of stapling rights onto digital securities is through a multilateral contractual framework (or network rules) established between the issuer, any third-party operator and all of the investors in the blockchain or the DLT-based system.

The advantage of having a framework of network rules is that it does not require a new contract to be executed by all parties each time a new investor joins the system. Instead, a contractual relationship may arise between investors that each agrees to be bound even where they do not know each other’s identity and therefore have rights as against each other.

By allowing the parties to agree a bespoke set of rules applicable to transfers within the system, the network rules could be structured so that certain protections are granted to innocent acquirers in respect of instruments even if they do not have the status of negotiability. This is particularly relevant for financial market infrastructures (“**FMI**s”) (for example payment systems or central securities depositories) and other multilateral systems.

Although a contractual arrangement cannot bind third parties or prevent them from acquiring proprietary interests in contravention of the network rules, the network rules may provide for the transfer of interests between participants in the network and afford certain protections to innocent acquirers within the network. Where the interests are in digital securities that have been immobilised in connection with the network rules, the network rules may include protections to prevent transfers to third parties outside the network occurring to the detriment of the participants.

Hong Kong law potentially provides several mechanisms that could be used to staple legal interests onto digital securities. It is generally possible to structure arrangements using any of the above techniques so as to ensure that future purchasers have protection against the risk of the issuer revoking or amending its obligations. Nevertheless, these methods do not of course negate against all potential risks, for example in the case where two investors claim legal title to the same digital security with the first investor claiming to have been wrongfully deprived of the digital security. The Third Party Rights Ordinance provides that in the case of competing interests among various third parties, the enforcement of a contractual term by a third party is subject to any relevant conditions as provided under the contract. The onus is therefore on the contracting parties to formulate terms of the contract to cater for the possibility of competing interests among third-party investors.²⁷ This could be, for example, by providing for a method of determining the rightful holder in the terms and conditions or setting out dispute resolution terms in the case of competing interests.

Among the five stapling techniques, as discussed above, the deed poll and trust deed are regarded as the most resilient methods in the debt capital markets as the parties’ intention can be clearly elaborated by suitable drafting in the provisions of the deed poll and is most frequently used. Apart from deeds poll, multilateral rules are also commonly used in the market to govern the relationship between different parties. In appropriate cases, hybrids of the various stapling mechanisms (for example, a combination of deed poll and network rules in FMIs) may be adopted for the issuance and transfer of digital bonds.

²⁵ Section 3 of the Third Party Rights Ordinance.

²⁶ It has been argued that transfers in certain securities settlement systems such as CREST, take place by novation. See Michael Bridge, Louise Gullifer, Kelvin Low and Gerard McMeel, *The Law of Personal Property* (3rd Edition) (Sweet & Maxwell, 2021) at paragraph 27-096.

²⁷ Section 4(4) of the Third Party Rights Ordinance.



Practical structuring considerations

When preparing the terms and conditions of digital debt securities, in light of the issues above, parties will need to:

- > ensure that the contractual terms that confer rights on holders of digital securities are clearly drafted and unambiguous;
- > clearly provide that the holders of digital securities are to be identified by reference to the digital ledger or blockchain; and
- > include provisions in the terms and conditions to resolve competing interests among holders of digital bonds, for example provisions to the effect that the relevant transfer shall confer upon the transferee all rights and benefits and that the holder is entitled as against all previous holders rights over the digital bonds.

In addition, parties will want to think about crafting the risk disclosures for digital securities offerings and how best to mitigate issuer risk using such disclosures. Issuers will also want to carefully consider their target investor base. The digital nature of the issuance will in practice mean that the risk profile of the digital security will suit professional investors but this does not suggest that a digital security is not inherently suitable for retail investors by virtue of its terms and conditions. In fact, local securities and investor protections regulations may mean that the digital security market may also open to retail investors so long as selling restrictions and risk disclosures provisions are crafted carefully.

Formalities

Given the importance of deeds poll and trust deeds to constitute and transfer digital debt securities, this leads us to the question of what the formalities are for executing the relevant contractual documents in respect of issuing and transferring digital debt securities under Hong Kong law. Under Hong Kong law, there are no specific formality requirements for the issuance and transfer of bearer tokens, registered tokens or claims tokens.

Under English law, disposition of equitable interest or trusts subsisting at the time of disposition must be in writing and signed.²⁸ An oral disposition of equitable interest will be void. This is relevant in the scenario where, for example, digital bonds are held on trust. Under Hong Kong law, unlike the position in the UK, except for land-related interests, there is no equivalent requirement that equitable interests must be disposed in writing.²⁹ Therefore, the disposition of equitable interests in relation to digital bonds in Hong Kong should not raise any particular issues.

We note that there are formalities for execution of deeds poll and trust deeds under Hong Kong law for Hong Kong-incorporated companies.

²⁸ Section 53(1)(c) of the Law of Property Act.

²⁹ Section 6(1)(c) of the Law Amendment and Reform (Consolidation) Ordinance (Cap. 23, Laws of Hong Kong) was to the same effect to section 53(1)(c) of the Law of Property Act but this provision was repealed.

Deeds are required to be “signed, sealed and delivered” and must be in writing on paper or parchment. The last requirement for deeds to be *in writing on paper or parchment* is referred to as the “substance requirement” (ie, the requirement relates to the substance in which a deed is written on, not merely a requirement for a deed to be in writing). As it is uncertain whether these formalities requirements apply to overseas companies, there is some divergence in the market.³⁰

In the UK, the substance requirement for deeds was abolished by the Law of Property (Miscellaneous Provisions) Act 1989. However, there is no equivalent statutory provision in Hong Kong abolishing the substance requirement. Therefore, until the substance requirement is abolished in Hong Kong, the requirement presents a difficulty for deeds that exist only in electronic format.

As with the case of deeds poll, there are currently difficulties under Hong Kong law in accommodating an electronic trust deed within a digital system. The creation of a trust³¹ is one of the matters excluded from the legal recognition given to electronic signatures under the Electronic Transactions Ordinance (Cap. 553, Laws of Hong Kong) (“ETO”).³²

Nevertheless, for clarity, we stress that parties are free to execute a deed poll or trust deed in respect of the digital bonds physically in wet-ink signature. While it may be more convenient for a deed poll or trust deed to be executed electronically, there is no impediment to having a physically executed deed poll or trust deed for a digital bond issuance. Once issued, there is no issue for digital bonds to be transferred using digital instruments of transfer.

Local corporate law requirements

A Hong Kong-incorporated company that wishes to issue digital bonds, irrespective of whether the digital security is governed by Hong Kong law or another choice of law, will need to be mindful of the Hong Kong corporate law requirements under the CO.

Under the current legislation in Hong Kong, there are three main corporate law considerations with respect to issuance and transfer of digital debt securities, namely:

- > whether physical certificates are necessary for digital bonds;
- > whether a blockchain can be used as a register of digital bonds; and
- > whether physical instruments of transfer are necessary for digital bonds.

(i) Certificates for debentures

At common law, a “debenture” is an evidence or acknowledgment of indebtedness.³³ Under Hong Kong company law, the definition of “debenture” is non-exhaustive and includes common types of corporate debentures, including bonds and notes.³⁴ There would appear to be no reason why a digital security, including a digital bond and a digital note, would not be a debenture for these purposes even if it is not certificated.

Although under Hong Kong law, there is a requirement for a certificate to be issued for allotment or for transfer of debentures, the requirement can be dispensed with if the conditions of such allotment or transfer provide as such.³⁵

For completeness, historically we note that market convention has been to adopt certificates for debentures (whether in global or definitive form) and the transaction documents constituting such debentures will typically contain specific requirements.³⁶ Given the lack of specific statutory requirements, we see no issue for a certificate of debentures to be issued on a blockchain or other similar DLT technologies.

(ii) Register of debenture holders

A Hong Kong company issuing bonds which are “not transferable by delivery” is required to keep a register of debenture holders at the registered office of the company or at some other place in Hong Kong.³⁷ This requirement does not apply to bearer tokens.³⁸ In relation to registered tokens, the question is whether a blockchain or DLT-based system maintained by the issuer could serve as a register of debentures holders for this purpose.

An electronic record must satisfy three criteria to serve as a register of debenture holders under Hong Kong company law.

First, where company records are kept in electronic form, they must be capable of being produced in hard copy form.³⁹ This condition can be met by producing a hard copy printout of the data contained in the register.

Second, a register of debenture holders needs to contain certain specified categories of information, for example, names and addresses of holders.⁴⁰ This requirement can be met by having the information stored on the blockchain.

30 The Law Society of Hong Kong, Execution of Hong Kong Deeds by Foreign Corporations (see [link](#)).

31 Section 3 and Schedule 1 to the ETO.

32 Section 6 of the ETO.

33 At common law, “debentures” include “mere acknowledgements of indebtedness”. See *Palmer’s Company Law* (22nd Edition) (Sweet & Maxwell, 2023) at paragraphs 13.031 – 13.032. Given the inclusive statutory definition, the common law definition is also relevant.

34 Under section 2 of the CO, “debenture” is defined as “in relation to a company, includes debenture stock, bonds and any other debt securities of the company, whether or not constituting a charge on the assets of the company”.

35 Sections 318(2) and 323(3)(a) of the CO.

36 There is no express restriction that debenture certificates have to be in paper form, but the requirement for a company to have ready for delivery all the appropriate certificates was construed as requiring the certificate to be a physical one (see section 319 of the CO), and it is unlikely that market convention will move away from physical debenture certificates pending potential legislative changes in this space.

37 Section 308(1) of the CO provides that “If a company issues a series of debentures, or any debenture stock, that are not transferable by delivery, the company must keep in the English or Chinese language a register of the holders of the debentures or debenture stock”.

38 As they are “transferable by delivery”.

39 Section 655 of the CO.

40 Section 308 of the CO.

Third, the issuer is obliged to retain a degree of control over the register to fulfil its maintenance obligations under the legislation. Certain maintenance obligations in respect of register of debenture holders are stipulated under Hong Kong law, including:

- > a duty to register certain transfers of debentures;⁴¹
- > the right to refuse to register certain transfers of debentures;⁴² and
- > a duty to guard against falsification.⁴³

Accordingly, whether a blockchain can be used as a register of debenture holders would depend on whether the issuer company has sufficient control over the register to fulfil its duties of maintenance. As such, an off-chain system would undoubtedly satisfy the requirements. It then raises an important question of whether an on-chain register could fulfil the requirements with respect to the statutory maintenance obligations. Depending on the structure of the on-chain register, an on-chain register may still be feasible.

One way for the issuer (or its agent) to retain control of the register is through various technical means, such as a permissioned network or rules built into smart contracts. These mechanisms could ensure that the issuer maintains oversight and control over the distribution and management of the tokens, including the power to register or to refuse certain transfers of registered tokens as well as taking adequate precautions to guard against falsification of entries and taking steps to facilitate discovery of the falsification.⁴⁴

Conversely, as the rights of claims tokens are determined by reference to entries in a DLT-based system controlled by a third-party operator, it is arguable that the records evidencing the claims tokens do not qualify as a “register” under the CO given the issuer’s lack of control over the register. This may mean that directly issued native claims tokens are not currently possible for a Hong Kong incorporated company: since they are not “transferable by delivery”, a compliant register (which allows the Hong Kong issuer to exercise requisite control) would be required to be maintained.⁴⁵

Hong Kong-incorporated issuers are required to maintain the register of debenture holders at the company’s registered office or in a “place prescribed by regulations”, which is currently a place in Hong Kong.⁴⁶ While there is no barrier to corporate records being maintained in electronic form⁴⁷, it is a question whether such records can be said to be “in Hong Kong” where they are maintained in a blockchain (including both permissioned and permissionless blockchains)⁴⁸ accessible by the issuer from its premises in Hong Kong. There appears to be no

requirement for the register of debenture holders to be **exclusively** accessible from a place in Hong Kong as long as the register is within the control of the issuer. It appears that this requirement can be met by appropriate structuring.

(iii) Instrument of transfer of debentures

In practice, whether an instrument of transfer for the digital debt securities is required will depend upon the stamp duty requirements for the sale or purchase of the applicable securities. Under Hong Kong law, sales and purchases of Hong Kong stock and Hong Kong bearer instrument are subject to stamp duty.⁴⁹ However, in practice, instruments of transfer are rarely required in the debt capital markets because of certain stamp duty exemptions.

The categories of exempted instruments are drafted widely. In particular, the exempted category of “loan capital” includes debenture, debenture stock and funded debt. Other debt securities which are not included in the exempted categories can also be exempt from stamp duty requirements insofar as they are denominated or redeemable in any currency other than Hong Kong dollars. As such, only in limited instances will the issuances of conventional debt securities attract stamp duty under Hong Kong law. It appears that a similar position will apply for the issuance and transfer of digital bonds, and therefore an instrument of transfer will normally be dispensed of in sale and purchase of digital bonds.

Even if an instrument of transfer is required for transfer of digital bonds,⁵⁰ we see no reason why the blockchain or DLT based system cannot be paired with software to produce a document satisfying the requirement of a “proper instrument of transfer”.

For completeness, the above corporate law requirements do not apply to non-Hong Kong incorporated companies. Therefore, even where the governing law of the relevant transaction of digital bonds is Hong Kong law and that the issuer has a place of business in Hong Kong, the corporate law requirements are not applicable to the transaction if the issuer is not a Hong Kong-incorporated company.

To conclude, it appears that the corporate law requirements respect of issuance and transfer of digital debt securities can be met under Hong Kong law.

Based on the above, the three key legal issues in relation to issuance and transfer of digital bonds are stapling, formalities and local corporate law requirements. Each of these do not raise insurmountable obstacles under the current Hong Kong legal framework. Hong Kong law is inherently flexible and resilient to accommodate issuance and transfer of digital debt securities in the current capital market and there is no need for any specific changes in law for the digital bond market to develop.

41 Section 321 of the CO.

42 Section 321 of the CO.

43 Section 656 of the CO.

44 Another method is by “whitelisting”. The persons whitelisted may be limited to the issuer, its affiliates and its agents with the effect that control over the register is still retained by the issuer.

45 Section 308(1) of the CO.

46 Section 309 of the CO; section 3(1) of the Company Records (Inspection and Provision of Copies) Regulation (Cap. 622I, Laws of Hong Kong).

47 Section 654 of the CO provides that the term “company records” in the CO shall include “any register... required [by the CO] to be kept by a company”. Section 655 of the CO provides that “company records... may be kept in hard copy or electronic form”.

48 We note that it is more common to have a permissioned blockchain rather than a permissionless blockchain.

49 Head 2 and Head 3 to the First Schedule, Stamp Duty Ordinance (Cap. 117, Laws of Hong Kong).

50 Section 320 of the CO.



Specific questions

In light of the above discussion, we have set out below the specific questions concerning issuance and transfer of digital debt securities from a practical perspective:

Q Can digital debt securities be validly issued under Hong Kong law?

A Yes, there is no difficulty in principle for digital bonds to be issued using a blockchain or a DLT-based system under Hong Kong law. The features of conventional bonds can be replicated for digital bonds by adopting appropriate legal structuring techniques. Certain corporate law requirements will need to be complied with by Hong Kong-incorporated companies but these can be met under current Hong Kong law.

Q In what legal form(s) are digital debt securities capable of being issued under Hong Kong law?

A Digital debt securities are capable of being issued as bearer tokens, registered tokens and claims tokens. In the case of bearer tokens, rights or interests can be stapled to the token and passed with control of the token. In the case of registered tokens, rights or interests can be stapled to the token through the update of a register maintained by or on behalf of the issuer under the conventional registered model. Claims tokens are similar to registered tokens but the register is maintained by a third party which is not an agent of the issuer. Although there is a question as to whether directly issued claims tokens is possible for a Hong Kong incorporated company, use of a claims model is possible under an immobilization structure where the tokens are registered in the name of the custodian or depository.

Q Can a blockchain or DLT-based system be used as register of digital debt securities under Hong Kong law?

A Yes. A blockchain is a database and can be used as a register similar to any other database. In particular, an on-chain ledger may be used as a register of a Hong Kong company so long as the company has retained sufficient control over the register to comply with its maintenance obligations under the legislation.

Q By which mechanisms can rights and interests be legally stapled to a digital debt security in order to validly constitute a digital security under Hong Kong law?

A The use of deeds poll (or a trust deed), the Third Party Rights Ordinance, open offer, advance consent to transfer by way of novation and multilateral contractual framework are examples of

mechanisms that can be used to staple rights and interests to a digital debt security or other entry in a blockchain or DLT-based system. In appropriate cases, hybrids of the various stapling mechanisms (for example, a combination of deed poll and network rules in FMI) may be adopted.

Q Are digital debt securities capable of having the effects of a negotiable instrument under Hong Kong law?

A Bearer tokens can be granted the status of negotiability through development of a mercantile custom to that effect. The practical effects of negotiability can also be emulated through the legal structuring techniques discussed above.

Q By which mechanism are rights to digital debt securities capable of being transferred under Hong Kong law?

A There are various transfer mechanisms, including but not limited to transfer by way of “negotiation” (ie where the digital debt securities are granted the status of negotiability), legal assignment, novation and equitable assignment. The precise mechanism will depend on the precise nature of the digital debt securities and the stapling mechanisms used.

As for traditional negotiable instruments, “negotiable” digital securities are transferred by way of “negotiation”. For digital securities without the status of negotiability such as registered and claims tokens, such securities can be transferred pursuant to the transfer mechanism in the terms and conditions of the security and conclusively reflected on the register of debenture holders.

Q Can the corporate law requirements be met by issuance and transfer of digital debt securities under Hong Kong law?

A Yes. There is no requirement for a debenture certificate to be issued for allotment or transfer of debentures under Hong Kong law as such requirements can be dispensed of under the conditions of such allotment or transfer. In relation to whether instruments of transfer are needed, although stamp duty is generally payable on sale or purchase of debenture stock and bearer instruments, exemptions are frequently invoked for debt securities. Regarding the requirement for the issuer to maintain a register of digital debt securities, please refer to our responses in Question (3) above.



Final remarks

This paper seeks to provide an overview of potential legal considerations for the issuance and transfer of digital bonds under Hong Kong law.⁵¹ Based on the discussions in this paper, we believe that Hong Kong law is sufficiently flexible and resilient to accommodate novel asset classes to serve the needs of market participants. There is no need for law reform in order to allow valid issuances and transfers of digital bonds under Hong Kong law to take place.

Although this paper focuses on discussing digital bonds, the analysis and legal structuring techniques are generally applicable to other contractual securities including but not limited to equity securities, structured notes, repackaging, securitization and funds. For example, there have been tokens issued with a fund as the underlying asset. Such tokens have been structured with a pass-through to the fund units where the commercial terms of the tokens mirror the equivalent commercial terms of the units. Structuring considerations include ensuring that distributions pass-through from the unit holder to the token holder on record, ensuring that the distribution and maturity dates of the token work when having regard to the equivalent dates of the fund and whether similar voting and redemption rights should be given to token holders and various other considerations. In particular, although there are more restrictions for issuance and transfer of equity securities in terms of local corporate law requirements⁵², the above discussion on the corporate law issues for digital bonds generally applies to digital equity securities.

We note that there may be more difficulties in tokenising some other asset classes such as real estate property. For example, practical difficulties arise from the very nature of a real property, where it is difficult to break up real property into individual tokenised portions or where it may be difficult to transfer or sell such real estate property. Having said that, with the right structure and design, it may still be possible to structure tokens with a real property as the underlying asset. We anticipate further clarity or law reform to address other assets classes in tokenisation of financial markets.

Apart from the legal issues discussed in this paper, we note that there are still some potential issues to be considered in the context of digital debt securities. For example, given the global nature of digital securities and the securities market, in the case of a dispute, parties may need to deal with conflict of laws issues to determine which national laws apply to various aspects of collateral arrangements of digital debt securities. Parties may also wish to consider whether and how digital bonds can be structured to be interoperable between different blockchain platforms.

Certainly, as a leading financial centre in the debt capital markets, Hong Kong is already well positioned to play a leading role in the global development of digital bonds. We look forward to supporting and developing this space with clients and stakeholders, and to pushing forward tokenisation of other asset classes.

51 This paper does not cover matters of taxation, criminal law, partnership law, data protection, intellectual property, consumer protection, settlement finality, regulatory capital, anti-money laundering or counter-terrorist financing. Licensing issues have been excluded as these are issues particular to individual market participants. This paper also does not address the entire regulatory regime associated with issuing and dealing in securities nor issues relating to choice of law or private international law. Given the application of law in the context of tokenisation is highly fact-sensitive, this paper does not set out every potential factual scenario which would need to be considered for the issuance and/or transfer of digital bonds. This paper is not intended to represent any legal opinion or advice, and readers should assess each factual scenario on a case-by-case basis.

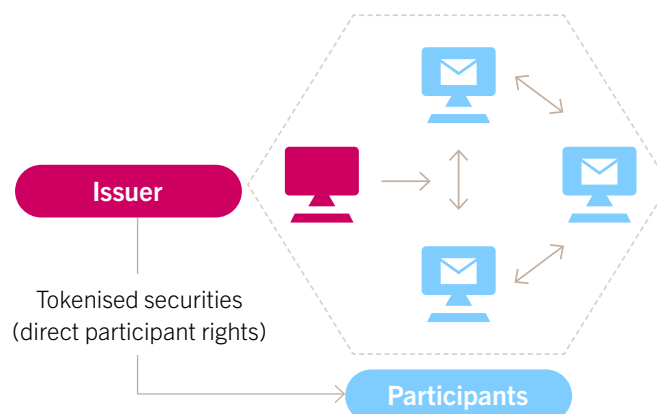
52 For requirements for share certificates, see sections 144 and 155 of the CO. For requirements for register of members, see section 627 of the CO. For requirements for instruments of transfer for shares, see section 150 of the CO.



Appendix: Models of issuance of digital bonds

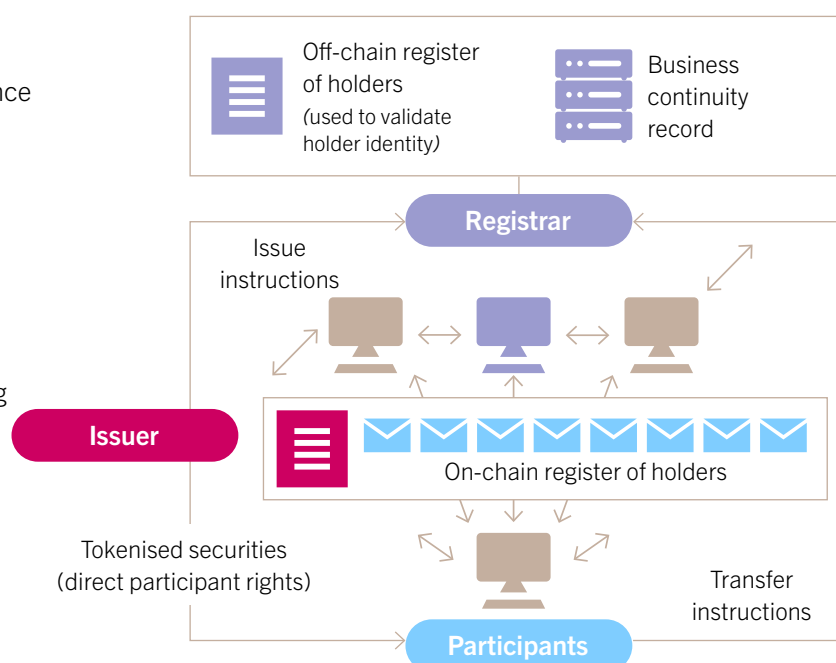
Structure 1: Bearer tokens

- > **Description:** rights determined by reference to exclusive control of tokens
- > **Characterisation of token:** intangible asset in its own right (tokens recognized as objects of property rights)
- > **Transfer mechanism:** transfer of practical control of tokens
- > **Control of tokens:** token holder has exclusive control



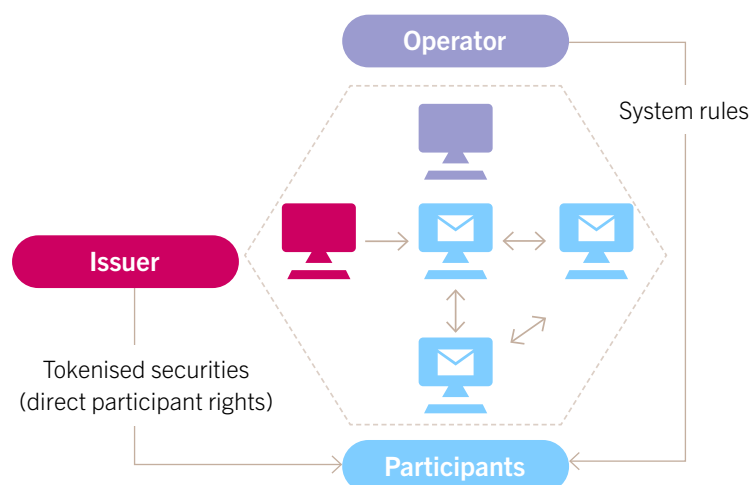
Structure 2: Registered tokens

- > **Description:** rights determined by reference to a DLT-based register controlled by a registrar (which may be the issuer itself)
- > **Characterisation of token:** mere data/evidence of rights
- > **Transfer mechanism:** updating token balances recorded to a smart contract deployed by the registrar
- > **Control of tokens:** registrar has overriding legal and practical powers to amend the record



Structure 3: Claims tokens

- > **Description:** rights determined by reference to entries in a DLT-based system controlled by a third-party operator
- > **Characterisation of token:** mere data/evidence of rights
- > **Transfer mechanism:** updating token balances recorded to a smart contract deployed by the operator
- > **Control of tokens:** operator has overriding legal and practical powers to amend the record



*The third-party operator may also maintain separate off-chain records for business continuity and other purposes.



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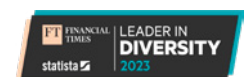
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