



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 8C

HONG KONG

This is the **summative (formal) assessment** for **Module 8C** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

The mark awarded for this assessment will determine your final mark for Module 8C. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
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3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
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6. The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **8 pages**.

ANSWER ALL THE QUESTIONS

QUESTION 1 (multiple-choice questions) [10 marks in total]

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

Any reference to “CWUMPO” in the questions below means the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32).

Question 1.1

Select the **correct answer** to the question below:

As a lawyer practising Hong Kong law, you are asked to advise a client on a tricky legal issue. There are no Hong Kong authorities dealing with the issue but there is a 1985 decision from the English House of Lords more or less directly on point. It has not been cited in the Hong Kong court. Can you rely on it in forming your advice?

- (a) Yes, because it is a House of Lords decision pre-dating the Handover in 1997 so is binding on the Hong Kong court.
- (b) No, because all decisions of the English court ceased to have any relevance in Hong Kong after the Handover in 1997.
- (c)** Yes, it is not binding as such but the decision will form part of the common law as at the date of the Handover in 1997 and would be persuasive as the common law at that date forms part of Hong Kong law.
- (d) No, because the decision is from the House of Lords and not a Privy Council decision on appeal from Hong Kong.

Commented [RD(DW-H1)]: Correct (1 mark). The decision would be persuasive

Question 1.2

Realisations from a floating charge will always be paid in full to the holder of that charge, even if the company granting the charge goes into liquidation. (You may assume that the floating charge is not open to challenge by the liquidator).

- (a) This statement is true because a creditor by way of a floating charge will always stand entirely outside of the liquidation.
- (b) This statement is untrue because all of the costs of the liquidation must always be paid first out of those realisations.
- (c)** This statement is untrue because creditors with a statutory preferential claim must first be paid out of those realisations (unless the same can be paid out of uncharged assets).
- (d) This statement is untrue because **both (b) and (c)** are correct (that is, the costs of the liquidation must always be paid first out of those realisations and thereafter creditors with a statutory preferential claim must first be paid out of the realisations).

Commented [RD(DW-H2)]: Correct (1 mark). Option (a) is not correct due to the rules on payment of preferential creditors; (b) is not correct because the charged assets are not available to the liquidators

Question 1.3

Upon a bankruptcy order being made against an individual, that individual remains free to deal with his assets provided he reports to his trustee in bankruptcy after doing so.

(a) This statement is true.

(b) This statement is untrue because upon bankruptcy the bankrupt's assets are vested in the trustee.

(c) This statement is untrue because although the assets remain the bankrupt's own he must obtain permission from the trustee before dealing with those assets.

Commented [RD(DW-H3)]: Correct (1 mark). Bankruptcy differs in this regard from corporate insolvency in Hong Kong. In the latter, the company remains the owner and there is no automatic vesting.

Question 1.4

A petition to wind up a company on grounds of insolvency can be presented when a company is unable to pay its debts. Section 178 of CWUMPO provides three circumstances in which a company shall be deemed to be unable to pay its debts. **Which one of the following** is one of those circumstances?

(a) A creditor has properly served a demand (statutory demand) in the prescribed form and the company has, for three weeks after service, neglected to pay the sum demanded.

(b) Where the statutory definition of "insolvency" (appearing elsewhere in the same Ordinance) is satisfied.

(c) Where the company is insolvent according to its balance sheet.

(d) Where a judgment has been made against the company.

Commented [RD(DW-H4)]: Correct (1 mark). The key thing to remember is that there is no statutory definition of "insolvency" in the relevant Hong Kong legislation

Question 1.5

When a company goes into liquidation, the role of the liquidator is to:

(a) Realise the company's assets, adjudicate the proofs of debt submitted by those claiming to be creditors and distribute dividends to creditors.

(b) Investigate transactions entered into by the company to determine whether there are any that can be impeached pursuant to the legislation (or otherwise).

(c) Investigate the cause(s) of failure of the company and the conduct of the directors.

(d) All of the above.

Commented [RD(DW-H5)]: Incorrect (0 marks). Whilst this is something the liquidator should do, the other points at (a) and (c) also need to be addressed, hence (d) is correct.

Question 1.6

A winding up Petition was presented on 1 April 2019 and the winding up order was made on 5 June 2019. After her appointment the liquidator discovers that a payment was made by the company to a third party on 5 April 2019. Which of the following provisions is **most likely** to be considered by the liquidator (and should be her **first** consideration)?

(a) Void dispositions after the commencement of winding up - pursuant to section 182 of CWUMPO.

(b) Unfair preferences - pursuant to sections 266, 266A and 266B of CWUMPO.

Commented [RD(DW-H6)]: Correct (1 mark). The other options are also possible but (a) should easily be the first option to look at because the legislation deems the transaction to be void (the commencement of the winding up being 'backdated' to the date of the petition). It would be for the recipient to persuade the court that the payment could be retained. For the others, the liquidator would have to prove certain elements.

(c) Transactions at an undervalue – pursuant to sections 266B, 266D, 266E of CWUMPO.

(d) Fraudulent trading – pursuant to section 275 of CWUMPO.

Question 1.7

Select the **correct** answer:

A receiver appointed pursuant to a charge created by a company (A) over its assets in favour of its bank (B), acts as:

(a) Agent of the company granting the charge – in this case A.

(b) Agent of the company appointing him – in this case B.

(c) An officer of the court.

(d) An employee or officer of the Official Receiver's Office.

Question 1.8

Between them, CWUMPO and the Companies Ordinance (Cap 622) (CO) provide a comprehensive statutory regime relating to corporate rescue.

(a) This statement is true – the provisions of these two statutes provide a comprehensive package of provisions relating to corporate rescue.

(b) This statement is untrue – CWUMPO alone provides a comprehensive regime for corporate rescue as well as for liquidations.

(c) This statement is untrue – CO alone provides for such a regime.

(d) This statement is untrue – Hong Kong has no comprehensive statutory regime for corporate rescue.

Question 1.9

Select the **correct** answer:

Part X of CWUMPO gives the Hong Kong court jurisdiction to wind up non-Hong Kong companies in certain circumstances. Aside from this section, other provisions relating to cross-border insolvencies are contained in:

(a) The UNCITRAL Model Law on Cross-Border Insolvency as adopted in Hong Kong.

(b) Parts of CWUMPO other than Part X.

(c) Guidance in common law judicial decisions.

(d) The Foreign Judgments (Reciprocal Enforcement) Ordinance (Cap 319).

Question 1.10

Select the **correct** answer:

Commented [RD(DW-H7)]: Correct (1 mark). It should be remembered that the receiver also owes duties to the charge-holder (here, B), but acts as agent of the chargor

Commented [RD(DW-H8)]: Correct (1 mark). Although the CO contains provisions for schemes of arrangement, those provisions could not be said to be "a comprehensive statutory regime relating to corporate rescue". As one example, there is no moratorium.

Commented [RD(DW-H9)]: Correct (1 mark). Hong Kong has not enacted the Model Law; part X is the only part of CWUMPO dealing with the subject matter; and Cap 319 deals only with enforcement of foreign judgments

A liquidator appointed by the Cayman Islands court over a Cayman incorporated company believes that the company has a legal action it should pursue against defendants in Hong Kong. Leaving aside any potential jurisdictional challenges as regards the action itself (for example, the presence of an arbitration clause), the liquidator:

- (a) must first obtain an ancillary winding up order in Hong Kong.
- (b) can commence the litigation in the name of the company without further order in Hong Kong.
- (c) Must first seek a recognition order in Hong Kong and must obtain a letter of request from the Cayman court for such purpose.
- (d) Must first seek a recognition order in Hong Kong and can do so based solely on the Cayman winding up order and without a letter of request.

Commented [RD(DW-H10): Correct (1 mark). See for example the *Irish Shipping* case

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

Describe the effects of the compulsory liquidation of a company upon a creditor who is pursuing the company by way of a civil action.

The effect of a compulsory liquidation of a company on a creditor pursuing the company by civil action is that the claim is liable to a stay upon application by the company to the court where the winding up petition has been submitted to the court. Section 181 of the CWUMPO provides that at any time after the presentation of the winding up petition and before the winding up order is made, the company or any creditor or contributory of the company may, where any action, including a civil action is pending against the company in the court of first instance or the court of appeal, apply to the court in which the action is pending, for a stay of those proceedings. The Court will exercise its discretion to determine whether or not to grant a stay.

When the winding up order is made or a provisional liquidator is appointed, section 186 of the CWUMPO provides that all claims against the company are stayed. The claims against the company that were already commenced cannot be proceeded with except with the Court's leave and subject to any terms imposed by the Court.

If the company did not make an application to stay the creditor's civil action when the winding up petition was filed, after the winding up order is made, the creditor's civil action will be stayed. The winding up of the company by the Court is deemed to commence at the time of the presentation of the petition for winding up according to section 184(2) of the CWUMPO.

Commented [RD(DW-H11): 2 marks out of 3. Should also mention the restrictions on retaining attachments etc. (s.183)

Question 2.2 [maximum 4 marks]

Identify each method by which a company can go into liquidation in Hong Kong and briefly describe the circumstances in which each method would usually be implemented.

There are 2 main ways that a company can go into liquidation in HK and a third option for ceasing to exist: i) voluntary liquidation by way of members' voluntary liquidation or creditors voluntary liquidation; ii) compulsory liquidation by the Court and iii) deregistration of the company.

Voluntary liquidation by members occurs when the company will be able to settle all its liabilities within 12 months of the commencement of liquidation. The directors are to issue a

Commented [RD(DW-H12): 3 ½ marks out of 4. Should deal with s.228A liquidation (urgency); but additional ½ mark given for deregistration

certificate of solvency (s233 of CWUMPO) and the members are to pass either a special or ordinary resolution seeking the appointment of a liquidator. Liquidation commences on the date the resolution for winding up is passed.

A creditors voluntary winding up occurs where the company decides to place itself in liquidation but it is not solvent. A creditors' voluntary winding up is preferred over a compulsory liquidation because it reduces the expense and time of a court process. This option is also adopted over a court process because it offers the advantage of no ad valorem being payable to Government. The directors of the company by their volition or at the shareholders' request are to convene a shareholders' meeting to pass a special resolution for the company winding up. The special resolution has to be at least 75% majority of the creditors, as defined in section 564 of the Companies' ordinance. The creditors' voluntary winding up commences on the date of the passing of the resolution. The liquidator is appointed at the shareholders' meeting but he has limited powers until his appointment is confirmed at the creditors' meeting. The meeting of creditors is to be notified to creditors by post 7 days before the meeting is held and be advertised in the HK Gazette and in an English and Chinese newspaper. Section 228A outlines the procedure for an urgent liquidation.

The compulsory liquidation of a company occurs with an application by the company or a creditor to the Court for the company to be placed in liquidation. There are six scenarios listed in section 177 of the CWUMPO where a petition may be made for a company to be wound up by the court. They include where the company is unable to pay its debts, the company has no members, the company does not commence any business for a whole year from its incorporation or it suspends business for a whole year or the court deems it just and equitable for a winding up order to be made. The petition is made to the Court and the court then determines whether it will grant the order, adjourn or dismiss the application.

Question 2.3 [maximum 3 marks]

Commented [RD(DW-H13)]: 3 marks out of 3. Good answer

Where a creditor presents a petition for the compulsory winding up of a company, a court hearing date is fixed approximately two (2) months after the date of presentation. Does Hong Kong law permit an officeholder to be appointed in the meantime (that is, during this interim period of two months before the petition is heard)? If "yes", in what circumstances? If "no", what is the policy reason for not permitting such appointment?

Yes, HK law permits the appointment of an officeholder in the interim period from the presentation of the winding up petition and before the winding up order is made. While the title is not formal in HK law, there is the function of a liquidator appointed provisionally. Section 193 of the CWUMPO provides that the Court may appoint liquidators provisionally at any time after the presentation of a winding up petition and before the making of a winding up order in respect of a company. The Court on appointment will limit or restrict the powers he may exercise.

The circumstances for the appointment of a provisional liquidator are limited and have been outlined in the case *Re Legend International Resorts Limited*. Those circumstances include urgent circumstances where the assets of the debtor company are in peril. The provisional liquidator is tasked with preserving the assets of the company and not to realise the assets unless it is necessary to preserve their value. A provisional liquidator can be appointed to help facilitate a restructuring proposal but that cannot be the sole reason for his appointment.

The court is not likely to allow the appointment of a provisional liquidator solely for the purpose of facilitating a restructuring proposal because HK law was not designed expressly to facilitate this. As explained in the *Re Legend International Resorts* decision, there must be some commercial realities, degree of urgency and need demonstrated.

The Court will also not allow the appointment of a liquidator provisionally immediately before a winding up petition is presented to avoid having the Official Receiver appointed as provisional liquidator when the winding up order is made. This was the court's finding in *Re Kong Wah Holdings Ltd* and *anor*

It appears from the *Re MF Global Hong Kong Ltd* decision that the policy reason for making the appointment of provisional liquidators under section 193 restricted is that this appointment does not fall within the definition of a liquidation under section 2(1) and therefore no ad valorem tax is payable on realisations.

Commented [RD(DW-H14): Not sure this is quite right but is not needed for the answer in any event.

QUESTION 3 (essay-type questions) [15 marks in total]

Question 3.1 [maximum 9 marks]

Question 3.1.1 [maximum 7 marks]

Describe Hong Kong law as it applies to corporate rescue, discussing any advantages / disadvantages to the current system.

HK lacks a formal corporate rescue regime like the Chapter 11 process in USA. There is no legislation dealing with corporate rescues. Also there is no recognition of corporate groups under HK law. The only mechanism available to a company is seeking to restructure its debts is the scheme of arrangement.

Commented [RD(DW-H15): 4 ½ marks out of 7. A good answer. Given it is the only statutory method available, it would be have been preferable (and additional marks awarded) to include some more detail (e.g. need to get classes of creditors right (and what a class it); the court's involvement (including the sanction stage); the majorities needed; 'downside' represented by *Gibbs* principle)

The court has only informal work-outs for corporate restructuring efforts.

There have been workouts in the banking sector as well. For example, banks as financiers have recognised a need to work together to achieve a best outcome and have therefore worked with the debtor company to formulate a restructuring plan that results in debt rescheduling or debt to equity swap, known as a London Approach.

Commented [RD(DW-H16): Informal workouts not a court process

There was a guideline published by the Hong Kong Monetary Authority (*HKMA*) known as the Hong Kong Approach to Corporate Difficulties. It was issued by the Hong Kong Association of Banks (*HKAB*) and reissued as joint guidelines by the *HKMA* and *HKAB* in November 1999 and was intended to reflect the practice in the banking sector in the event of a corporate debtor (the *Guidelines*). The Guidelines encouraged the approach that bank creditors should support debtors who are in difficulty by not hastily withdrawing facilities, issuing warrants or appointing receivers but to provide additional capital or reschedule existing debts. While the Guidelines do not bind non-bank creditors who are free to proceed and issue winding up proceedings, the Court retains discretion whether it will grant the winding up order on the basis that a restructuring is likely to benefit the creditors as a whole and that the petitioning creditor is merely trying to promote its own position by forcing payment ahead of other creditors. This was the finding of the Court in *China Solar Energy Holdings Ltd*.

With the use of schemes of arrangement for restructuring purposes, practitioners have applied to have a provisional liquidator who will be given the power to investigate whether a scheme of arrangement will be possible. However, the ruling of the Court of Appeal in *Re Legend International Resorts Limited* has ruled against the appointment of provisional liquidators solely for the purpose of a restructuring on the basis that this is not supported by the statute. Disadvantages

1. Informal work-outs by a court are not set or structured. The Court's ruling will be determined on a case by case basis.
2. While a Scheme of arrangement plan is being processed by the company through the court, there is no moratorium on creditors' actions. There have been amendments to the court rules to allow the court discretionary power to grant a stay and it is believed the court will consider a scheme of arrangement is likely to be a just circumstance for permitting a stay of a creditor claim. The process for successfully passing a scheme of arrangement is a technical one that can be costly if for example the correct voting from class of creditors is not obtained.
3. The Guidelines issued by HKAB and HKMA are formal but not statutory, compliance is not mandatory but is merely "strongly recommended" and expected from HKAB members.
4. The Guidelines have a number of disadvantages. They (i) do not apply to non-bank creditors and are not binding on them. They are therefore free to commence winding up proceedings against debtor companies. HK has an increasing number of "other creditors" such as bondholders, private equity and hedge funds who are not in the same financial position as banks and may not have the same security as banks and therefore do not share the same approach to debtors in financial distress; (ii) The Guidelines stipulate the appointment of a financial advisor over the troubled company but the company has to pay his fees. Further, there is no priority given to banks who provide funding to troubled companies, to recover those monies invested; (iii) other banks do not have to agree to an approach and there are no sanctions against them if they don't agree.

Question 3.1.2 [maximum 2 marks]

Discuss the possible reforms that have been (or are) under consideration with regard to corporate rescue.

The main reform being considered as to corporate rescue has been the tabling of the Corporate Rescue Bill since 2001. The main aim being to allow a provisional supervisor to be appointed with a view to exploring restructuring or other rehabilitation procedures. There has been dicta in HK decisions by a commercial court judge calling for an amendment to section 193 of the CWUMPO to provide expressly for provisional liquidators to be given restructuring powers: *Re China Oil Gangran Energy Group Holdings Ltd.*

Question 3.2 [maximum 6 marks]

Although Hong Kong has little specific legislation dealing with cross-border insolvency, the Hong Kong courts have supported foreign insolvencies through the common law. Discuss.

The Court has assisted foreign representatives by relying on common law principles. Discussing this would entail reviewing some decisions of the HK court in using common law principles to assist foreign insolvencies.

The Court has for example assisted rehabilitation proceedings by refusing to allow enforcement of a judgment against Hong Kong assets held by the company. In *CCIC Finance v GITIC* the court took a 2 staged approach to deal with issues of liability and enforcement separately. The court, even if it established liability would still exercise discretion to determine whether to allow enforcement against assets held by the company in HK if it considers it will assist rehabilitation proceedings. The court in this case stayed garnishee proceedings issued against a company which was subject to bankruptcy proceedings in the PRC.

Commented [RD(DW-H17)]: 1 mark out of 2. The answer should refer to and examine briefly the elements of and reasons for failure of the Corporate Rescue Bill– how a possible reform failed can be a good indicator as to the direction a jurisdiction is likely to take

Commented [RD(DW-H18)]: 3 marks out of 6. Should also deal with ability to sue or get own documents without recognition (*Irish Shipping; Bay Capital*); letter of request needed; *Singularis* principles. Part X jurisdiction and core requirements. Additional ½ for referring to new material

Another example of the HK court assisting foreign insolvencies is in one 2016 decision where Justice Harris in *Re Kaisa Group Holdings Ltd* sanctioned a scheme of arrangement application on behalf of a non HK company listed in HK and incorporated in Cayman Islands. The scheme was to compromise the company's offshore debts which included bilateral facilities and was part of a multi-jurisdictional restructuring process. The court was satisfied that there was a sufficient connection between the scheme concerning the company and HK to justify the court exercising its discretion to sanction the scheme.

In 2018, in *CW Advanced Technologies Ltd*, Justice Harris allowed an application by a bank for provisional liquidators to be appointed over a HK company that was part of a Singapore group of companies. The HK company admitted that it was insolvent and its principal company which was based in Singapore had applied for a 6-month moratorium. The HK court granted the application by the Bank because it was satisfied that the company had admitted it was insolvent and it was undisputed that the debt was owed to the bank. The court was satisfied that the discretionary requirement was satisfied because the Bank's supporting evidence showed the need for independent investigations into the company's affairs and the need to preserve assets and the company did not dispute the Bank's evidence.

The latest example of how the HK courts have used common law to assist foreign insolvencies are reflected in three decisions by Justice Harris in March 2021 regarding the appointment of provisional liquidators in offshore jurisdictions where recognition and enforcement are sought in HK to postpone insolvency proceedings commenced in HK. These decisions have been regarded as a "new era" for HK cross border insolvency regime. The most recent is 12 March 2021, HK court of first instance where Justice Harris recognised a Bermudian soft touch provisional liquidation of Ping An Securities Group, a HK listed investment holding company incorporated in Bermuda. The Court adjourned the HK winding up petition brought against Ping An for 2 months finding that the provisional liquidators had provided evidence that they may be able to secure a restructuring of its debts. The Court noted that although HK courts can recognise soft touch provisional liquidators, there is no statutory mechanism for those office holders to secure a moratorium on the enforcement of debt. The only way they can achieve it is by securing an adjournment of a winding up petition against the company being restructured.

The earlier decision in March 2021 was *Re Lamtex Holdings Limited*. On the application to recognise the appointment of soft touch provisional liquidators, Justice Harris declined to recognise the appointment in Bermuda. He held that the restricted view that the common law recognition favours proceedings in a debtor's place of incorporation does not serve HK well. The Judge allowed the HK winding up to proceed because the appointment in Bermuda was viewed as an attempt to engineer a de facto moratorium and block previously filed winding up proceedings in HK. Lamtex centre of main interests appeared to be in mainland China and HK where all the company's largest Chinese creditors were in favour of a winding up. In addition, the provisional liquidators had not presented a credible plan to restructure the company's debts.

The Lamtex decision was a continuation of the principles established in the November 2020, in *Re FDG Electric Vehicles* decision. In this case, Justice Harris clarified that the offshore provisional liquidators are not entitled to a general stay in HK of winding up proceedings following a standard recognition order. The Court's approach therefore shows the discretion remains with the Court to determine on a case by case basis how it will deal with applications by foreign insolvency office holders.

QUESTION 4 (fact-based application-type question) [15 marks in total]

Question 4.1 [maximum 4 marks]

Commented [RD(DW-H19): This paragraph shows a good interest by referring to material which post-dates the guidance text. Caution though as these recent cases change the landscape quite a lot!

Commented [RD(DW-H20): 2 marks out of 4. The first step is to examine validity of the charge. For example, s.267; registration. A liquidator can also recoup costs reasonably incurred in realizing charged assets, but in reality only if does so before being aware of the receiver or with the receiver's consent.

A receiver is appointed pursuant to a floating charge over all the assets and undertaking of Pacific Tin Mines Limited (PTM), a Hong Kong company. Shortly after the receiver's appointment, PTM is put into liquidation. The liquidator writes to the receiver and asks her to hand over all assets (or realisations from assets) of PTM under her control so that the liquidator can pay the costs and expenses of the liquidation and make a distribution to PTM's unsecured creditors. You are asked to advise the liquidator. What (if any) assets or realisations should be handed over by the receiver?

The appointment of a receiver has the effect of crystallising a floating charge. The appointment of a receiver takes effect when the document of appointment is received and accepted in writing by the receiver. The receiver's primary duty is to the debenture or charge holder and not the company. The realisations made by the receiver out of the assets charged are generally not available to the liquidator for payment of the liquidation expenses. This position in common law *Buchler v Talbot* has been followed in HK in *Re Good Success Catering Group Ltd* albeit this case is said to have received negative judicial treatment. However, if there are insufficient assets to meet those claims from the uncharged assets available to the liquidator, then the charged assets must be used to meet the claims of preferential creditors.

Section 179 of the CWUMPO designates the expenses and costs of the liquidation as having a prescribed priority therefore falling within the category of a preferential creditor. If there are no other assets available to liquidator therefore the receiver will be required to provide any sums available from the charged assets to cover these expenses. The claim for expenses to distribute to unsecured creditors would not fall within the category of preferential creditors and therefore the receiver does not have to hand over any proceeds for settling this expense.

Question 4.2 [maximum 4 marks]

A liquidator is appointed over luxury car dealer Billion Happy Limited (BH) and learns that BH has recently been granted a facility by Hammerhead Finance Co Limited (HF). HF has shown the liquidator a document entitled "Receivables Purchase Agreement", claiming that all accounts receivables due from BH's customers therefore belong to HF. The document also asserts that as an alternative to ownership of the receivables, HF has a fixed charge over the receivables. Advances from HF to BH were sporadic and could not necessarily be matched to invoices. Further, some customers of BH had paid certain invoices to an account with HF, but which account BH then operated for working capital purposes.

Telford Co Limited (TC) contacts the liquidator of BH to say that TC had been helping BH sell its cars to wealthy businessmen on the Mainland. TC shows the liquidator an agreement asserting that if BH goes into liquidation then it is deemed that immediately before the liquidation, all cars held at BH's showrooms belong to TC.

The liquidator asks for your thoughts on what issues she should consider when dealing with HF and TC.

When dealing with both HF and TC, the liquidator is being asked to determine as liquidator whether the interest held by HF and TC are fixed or floating charges. The liquidator has a responsibility to adjudicate the claims by HF and TC to determine whether they are recoverable or are to be rejected. The general position is that assets subject to security will not be available for realisation by the liquidator. A floating charge has to be registered within 1 month of execution and preferential creditors have to be paid first out of the floating charge assets.

Commented [RD(DW-H21): I think this is a reference to rule 179 of the winding up rule. Not relevant here. In fact, this whole paragraph is a bit confusing.

Commented [RD(DW-H22): 4 marks out of 4. Good answer

In relation to HF's claim, HK law recognises a security arrangement like the one entered into by HF called a Receivables Purchase Agreement where the financier buys the right to be paid receivables from the business of the company. The receivables purchase agreement usually requires that the company pay into a specific account all receipts from those receivables covered by the security. It is important to consider whether the arrangement is truly by way of sale because if it is by sale then it is not a security per se and no registration is required. If on the other hand the arrangement is in fact a secured financing arrangement, then the Receivables Purchase Agreement is considered a floating charge which section 335(5) of the Companies Ordinance requires must be registered. Registration must be done within one month of the date of its execution. If a floating charge is not registered, then it is void against the liquidator and creditors. The fact that advances from HF to BH were sporadic and could not be matched to invoices is relevant to determining whether it was an absolute sale or a secured financing arrangement. Also, while some customers of BH paid certain invoices to an HF account, BH would operate this account for working capital purposes, this negates from the absolute sale arrangement and leans more to a secured financing arrangement which would need to be registered. A major test for identifying a floating charge is the measure of control the secured creditor has over the asset. The agreement provides that as an alternative to ownership of the receivables, HF has a fixed charge over the receivables. The question is whether this in fact operates as a fixed charge. A fixed charge is a charge in relation to a specific asset and attaches as soon as the charge is created or the asset is acquired by the debtor. The debtor cannot deal with the asset without the consent of the charge creditor. It is doubtful whether this is in fact a fixed charge. Consideration is to be given to the authority *Re Spectrum Plus Limited* for the 3 features to identify a floating charge. A floating charge must be registered within 1 month of execution to be valid against the liquidator.

The Liquidator must consider the principles governing impeachable transactions to determine whether any contract is to be set aside. For example, whether any of the contracts are an unfair preference. Also, a floating charge given by a company is void if it is created within 2 years of the commencement of the winding up in favour of a person connected to the company or within one year for any other person. If HC is connected to BH and the agreement was entered into within 2 years of commencement of the liquidation, then the floating charge is void.

In relation TC the liquidator is to consider whether this purported agreement between BH and TC is an ipso factor clause which HK law recognises but which must not breach the anti-deprivation principle. This anti-deprivation principle provides that a creditor is not be put in a better position than other creditors if the mechanism is considered a fraud on the insolvency laws. The principle is aimed at preventing a party like TC from using a contractual arrangement to give an advantage to one of the contracting parties in the event of the insolvency of the other. The HK court will consider the reasoning of the UK Supreme Court *Belmont Park Investments Pty Ltd* where the court noted that if the arrangements are part of a genuine commercial transaction and not entered into with the intention of creating an advantage on the insolvency of one of the parties, then the arrangement should not be struck down as a consequence of the principle. The liquidator should therefore consider that the UK Supreme Court decision is not binding so the general position remains that the arrangement seems to provide an advantage to TC above other creditors.

There is also the issue of priority of the claims by HF and TC as both lay claims to the receivables of BH. The rule in *Dearle v Hall* on equitable assignment of choses in action will be applicable to determining priority.

The liquidator has to consider any executory contracts by BH albeit there is nothing in HK law to deal with this.

Question 4.3 [maximum 7 marks]

Commented [RD(DW-H23)]: 3 marks out of 7. Good on recognition but should add ability to get documents that belong to the company (*Bay Capital*), or sue if enough evidence, without any order. Consider whether could take control of the Hong Kong subsidiary (either by winding up or using powers as shareholders to change board). Ancillary liquidation and core requirements. Actions against recipients?

Cyberbay MedTech Limited (Cyberbay) is a Cayman Islands company listed on the Stock Exchange of Hong Kong. This company appeared in the self-assessment questions in your guidance text, where you were asked to consider the steps that the Cayman-appointed officeholder might take in an effort to restructure the company's indebtedness due to holders of certain Notes. The joint provisional liquidators (JPLs) have now uncovered concerns about accounting irregularities in its Mainland operations and there are also press reports that the founder and Chairman has disappeared in the Mainland and cannot be contacted.

Upon further investigation, it appears that the Chairman's disappearance certainly looks as if it is linked to the "accounting irregularities" with large sums of money (raised from the issue of the Notes and the bank borrowing) being paid to entities with no apparent real business with Cyberbay. There is an individual in Hong Kong, Mr Pottinger, who is a friend and business associate of the Chairman. It is believed that Pottinger has information that will help shed light on the payments. The JPLs ask you if there is anything they can do in Hong Kong in this regard. Advise them.

HK law contains no cross-border insolvency provisions. It has not adopted the UNCITRAL Model Law on Cross Border Insolvency and is not a party to any treaties or bilateral agreements that deal with cross border insolvency. Nevertheless, the HK court follows common law to assist the Cayman appointed liquidators as endorsed by the Court of Final Appeal in *Chen Li Hung and another v Ting Lei Miao and others*.

The two main common law decisions that offer guidance to the liquidators are: (i) *A Co v B* (a 2014 decision); and (ii) *Singularis Holdings v Pricewaterhouse Coopers*.

In order to get assistance from the HK court to compel Mr Pottinger to be examined on oath or to produce documents, according to *A Co v B*, the Cayman liquidators should obtain a letter of request from the Cayman Court to the Hong Kong Court seeking the recognition of their appointment and for an order compelling Mr Pottinger to produce any information relating to Cyberbay and its Chairman or attend court to be examined.

The *Singularis* decision has clarified that the common law power to assist foreign liquidators has to satisfy two conditions as follows: (i) the power exists in the jurisdiction of principal liquidation; and (ii) the power exists in the assisting jurisdiction.

Considering the HK law position, the court has granted recognition orders to permit foreign officeholders to seek the production of documents or examination of individuals in HK as in *Re BJB Career Education Co Ltd* and *Re Centaur Litigation SPC*.

The liquidator therefore needs to be satisfied the power exists in Cayman law to compel the examination of a person like Mr Pottinger to be examined or to produce documents. It will be a matter of Cayman Islands law to determine that Mr Pottinger can be compelled to provide information. Being satisfied that HK courts have given assistance in this context in the past, the liquidators can make the application to court for assistance.

TOTAL: 35 MARKS OUT OF 50

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*** End of Assessment ***