



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.
2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
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).
4. You must save this document using the following format: **[studentID.assessment8C]**. An example would be something along the following lines: 202122-336.assessment8C. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words "studentID" with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. 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:

A receiver can be appointed –

- (a) only pursuant to a charge over shares.
- (b) only by the court.
- (c) only pursuant to a legal mortgage over land.

(d) any of the above.

Commented [RD(DWH1)]: Correct (1 mark) – A ‘receiver’ can be appointed by the court or under a charge document (whether over shares or land, or indeed other assets).

Question 1.2

When a trustee in bankruptcy is appointed, she may seek to unwind a transaction of the bankrupt if the transaction was entered into at an undervalue. **What is the “look-back” period** for such actions (that is, what are the oldest transactions that the trustee can look at in order to be able to take such action):

- (a) It depends on whether the person with whom the bankrupt transacted is an associate of his or not.
- (b) Two (2) years before the date of the bankruptcy order.
- (c) Five (5) years before the date of the petition on which the bankruptcy order was made.**
- (d) Five (5) years before the date of the bankruptcy order.

Commented [RD(DWH2)]: Correct (1 mark) – s.49 and s.51(1)(a) Bankruptcy Ordinance (section 6.2.10.1 of text). Although the commencement of a bankruptcy is the date of the order, most of the provisions dealing with the trustees’ ability to challenge earlier transactions use the date of the petition as the starting point of the ‘relation-back’ period. For some provisions, the time period changes depending on whether the other party to the transaction is connected to the bankrupt, but not for transactions at an undervalue.

Question 1.3

Which of the following **is correct** in describing whether the Hong Kong court can make a winding up order against a company that is not incorporated in Hong Kong:

- (a) The Hong Kong court can wind up such a company only if a director resides in Hong Kong.
- (b) The Hong Kong court has no jurisdiction to wind up such a company.

(c) As a matter of common law, the Hong Kong court has the right wind up such a company.

(d) The Hong Kong court has a statutory jurisdiction to wind up such a company, and can exercise that jurisdiction if certain requirements are met.

Commented [RD(DWH3): Correct (1 mark) – s.327 CWUMPO (section 7 of text).

Question 1.4

Select the **correct** answer:

A receiver is appointed over the entirety of a company's assets and the company goes into liquidation. Assuming the charge under which the receiver is appointed (and the receiver's appointment cannot be challenged), realisations made by the receiver:

(a) must first be used to satisfy the costs and expenses of the liquidator.

(b) must first be used to satisfy the whole of all claims by employees but no other claims.

(c) must first be used to satisfy the claims of preferential creditors as described in the relevant section of CWUMPO.

(d) will be kept entirely by the receiver for the benefit of the charge holder irrespective of what claims, preferential or otherwise, exist against the company.

Commented [RD(DWH4): Correct (1 mark) – see section 6.4.1 of text. Note the question refers to the charge being over all of the company's asset, such that there would be no uncharged assets for the liquidator to meet the preferential claims out of uncharged assets.

Question 1.5

Select the **correct** answer:

The date of commencement of liquidation for a Creditor's Voluntary Liquidation is:

(a) the date on which the creditors pass a resolution to wind up the company.

(b) the date on which the court approves the appointment of liquidators.

(c) the date on which the members pass a special resolution to wind up the company.

(d) the date on which notice of the liquidator's appointment is registered at the Companies Registry.

Commented [RD(DWH5): Correct (1 mark) – s.230 CWUMPO (section 6.3.3 of text). Note, however, that a liquidator has limited powers pending the creditors' meeting.

NB: for distinction between members' resolution and creditors' resolution in this context see sections 228(2) and 230 CWUMPO.

Question 1.6

Select the **correct** answer:

Hong Kong legislation provides a statutory definition of insolvency in –

(a) the Companies Ordinance (Cap 622).

(b) the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32).

(c) the Companies (Winding Up) Rules (Cap 32H).

(d) none of above.

Commented [RD(DWH6): Correct (1 mark) – see section 6.3.1 of text.

Question 1.7

Select the **correct** answer:

In a compulsory winding up, there is a mandatory stay of litigation claims against the company:

- (a) from the date on which the petition is presented.
- (b) from the date of commencement of the liquidation.
- (c) from the date of the winding up order.
- (d) There is no statutory provision for a mandatory stay; whether the claimant can continue is a matter for the court's discretion.

Commented [RD(DWH7)]: Correct (1 mark) – s.186 CWUMPO (section 6.3.7 of text); the mandatory stay also applies if a provisional liquidator is appointed.

Question 1.8

Select the **correct** answer:

In a compulsory winding up, at the first meeting of creditors where a resolution is proposed for the appointment of a liquidator, a creditor holding security from the company:

- (a) is not allowed to vote.
- (b) can vote and the whole amount of its claim is counted.
- (c) can vote if it has valued its security and the amount that is counted is the difference between its claim and that value.
- (d) must get special permission from the chairperson of the meeting to vote.

Commented [RD(DWH8)]: Correct (1 mark) – Rule 84 CWUR (section 5.5 of text).

Question 1.9

In considering what previous court decisions are binding on the Hong Kong courts, which of the following statements **is correct**?

- (a) A 1995 decision of the English House of Lords is binding.
- (b) A 1993 decision of the UK Privy Council on an appeal from Hong Kong is binding.
- (c) A 1996 decision of the UK Privy Council on an appeal from the Cayman Islands is binding.
- (d) None of the above because they all pre-date the Handover in 1997.

Commented [RD(DWH9)]: Correct (1 mark) – The *China Field* decision confirmed that pre-1997 decisions of the Privy Council on appeals from Hong Kong were and remain binding (section 4.1 of text).

Question 1.10

A liquidator appointed in another jurisdiction wants to seek Hong Kong recognition of his appointment. Which of the following **is correct**?

- (a) He must make an application to the High Court of Hong Kong using the provisions of the UNCITRAL Model Law.
- (b) He must first seek permission from the Ministry of Justice in Beijing.

(c) No recognition is possible.

(d) None of the above.

Commented [RD(DWH10): Correct (1 mark) – Hong Kong has not enacted UNCITRAL; the Ministry of Justice in Beijing would not be involved (“1 country, 2 systems”); the courts have developed a practice of giving recognition to foreign office holders in certain circumstances.

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

What are the jurisdictional requirements as regards a debtor for the Hong Kong court to be able to exercise its bankruptcy jurisdiction over that person?

Commented [RD(DWH11): (2.5 marks). Should include the source (s.4 of Bankruptcy Ordinance) given a specific reference to jurisdictional requirement

The jurisdictional requirements a debtor must satisfy in order to exercise its bankruptcy petition are:

- a) That it is domiciled in Hong Kong;
- b) That it is personally present in Hong Kong on the day on which the petition is presented; or,
- c) That at any time in the period of 3 years ending with that day:
 - a. It has been ordinarily resident, or has had a place of residence, in Hong Kong; or,
 - b. Carried on business in Hong Kong.

Question 2.2 [maximum 3 marks]

Commented [RD(DWH12): (3 marks)

What are the “core requirements” that enable the Hong Kong court to exercise its jurisdiction to wind up a non-Hong Kong company?

The following three “core requirements” to enable the Hong Kong court to exercise its jurisdiction to wind up a non-Hong Kong company are that:

1. There must be a sufficient connection with Hong Kong;
2. There must be a reasonable possibility that a winding up order would benefit the applicants; and
3. The Court must be able to exercise jurisdiction over one or more persons in the distribution of the relevant company's assets.

This was affirmed by the Court of Final Appeal in *Kam Leung Sui Kwan v Kam Kwan Lai & Ors.*

Question 2.3 [maximum 4 marks]

Commented [RD(DWH13): (3.5 marks). Full marks if mention that powers are as prescribed by the court (powers depend on circumstances)

When can a provisional liquidator be appointed, and in what circumstances and for what purposes?

A provisional liquidator may be appointed by the court at any time after the presentation of a winding-up petition and before the making of a winding-up order pursuant to Section 193 (1).

An application to appoint a provisional liquidator may be made at the same time as the winding-up petition in urgent matters.

In order to appoint a provisional liquidator, the court must be satisfied that:

1. There is a good *prima facie* case for the winding-up order; and,

2. The company's assets are in jeopardy.

A provisional liquidator may be appointed:

1. To preserve the company's assets to ensure their availability for distribution should a winding-up order be made, but not to realise them; and
2. To explore a restructuring of the company (although this cannot be the sole purpose).

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

Question 3.1 [maximum 5 marks]

Describe why you think a liquidator is able take action to challenge an unfair preference and set out what a liquidator must show to succeed in such a claim.

Section 266 of the CWOMPO provides for the liquidator to apply to court to restore the position of the company to what it would have been if it goes into liquidation and that it has been found to have given an unfair preference.

An unfair preference claim can be made by a liquidator if s/he believes that the company placed a person or entity in an advantageous position by a specific transaction (eg transfer of assets or a financial payment) up to 6 months prior to the company being placed into liquidation. This period is extended to two years if the transaction was entered into with a person or entity which is connected to the company.

However, the liquidator is also required to set out in his/her application that:

1. The company was unable to pay its debts or became unable to pay its debts in consequence of the unfair preference.
2. The company was influenced, in deciding to give the unfair preference, by a desire to put the recipient into a better position than it otherwise would have been in an insolvent liquidation. If the recipient is connected with the company, such desire is presumed.

Question 3.2 [maximum 5 marks]

Hong Kong has limited formal arrangements to deal with cross-border insolvency. Given that Hong Kong and the Mainland are one country, does this statement stand correct for the Mainland? Discuss.

Hong Kong's common law recognition of foreign insolvency proceedings have been in situ for some time and followed different rules to that in the Mainland, which is not a party to any international treaties, model laws or EU legislation that are relevant to restructuring or insolvency procedures.

However, China has entered into several bilateral treaties that contain detailed provisions for recognising and enforcing judgments and orders made by foreign courts.

However with the Cooperation Arrangement on Mutual Recognition of and Assistance to Bankruptcy (Insolvency) proceedings between the Courts of the Mainland and of the Hong Kong Special Administrative Region (the ROM) being signed into effect by the Mainland's Supreme People's Court (SPC) and Hong Kong's Department of Justice on 14 May 2021,

Commented [RD(DWH14): (3.5 marks) Need to say "why". Reason is the pari passu principle and that all creditors should be treated fairly amongst themselves. Also, see below

Commented [RD(DWH15): Unfair preference only applies to creditors or sureties

Commented [RD(DWH16): (4 marks) a bit confusing in parts, and could also refer to how common law tools have been used to recognise PRC insolvency processes in HK

there is the ability for Hong Kong liquidators to obtain recognition and assistance by the Intermediate People's Courts in the following three pilot cities in the Mainland being:

1. Shenzhen;
2. Shanghai; and
3. Xiamen.

The Hong Kong Court will require a letter of request and evidence of the officeholder's claim against assets held in one of the three pilot areas. Should the Hong Kong Court agree that one of the three pilot areas is the appropriate jurisdiction to recover a company's assets, the letter of request is likely to be granted.

Conversely, The Cooperation Mechanism also provides the procedures to Mainland officeholders (i.e. administrators in Mainland bankruptcy proceedings) to obtain recognition and assistance in Hong Kong. The Cooperation Mechanism is widely considered a major breakthrough for cross-border corporate insolvency and debt restructuring matters of the Mainland and Hong Kong.

Thus in essence, mutual recognition of and assistance to corporate insolvency and debt restructuring proceedings entered into by either the Mainland or Hong Kong with any other jurisdiction can now be recognised, and any recognition procedures that need to be applied in Hong Kong to recognize a foreign insolvency proceeding now also applies to the Mainland.

Therefore I consider that the statement regarding its procedures stands correct in that it does also apply to the Mainland.

Commented [RD(DWH17)]: ?

Question 3.3 [maximum 5 marks]

The scheme of arrangement is, in essence, Hong Kong's only statutory tool for corporate rescue. Describe it, listing the pros and cons.

Pursuant to Section 669 of the Companies Ordinance, a scheme of arrangement can be proposed to be entered into by a company with its creditors or members or any class of them, (as the case may be). It is a statutory, binding compromise reached between a company and its shareholders or creditors with regards to its financial obligations. It is a mechanism which will seek to compromise the company's debts, with a view to the business continuing to operate. Creditors will often accept less than the amount they are owed, in full and final settlement of any claims they may have against the company.

Commented [RD(DWH18)]: (4 marks) Should also mention that due the 'Gibbs' principle, a Hong Kong Scheme will only compromise debts arising from obligations governed by Hong Kong law. This is a possible downside in the modern environment where a sophisticated debtor is likely to have debts due under other governing laws
Also, as classes are important, should outline requirements (similarity of legal rights, not interests)

Pros include:

1. It requires a majority in number (i.e. more than 50%) representing at least 75% in value of the creditors or members present and voting, in person or by proxy, agree to the scheme. Without access to the scheme of arrangement, the approval of 100% of the creditors or members, would likely be required to implement a restructuring or reorganization. This may be very difficult to achieve if there are numerous creditors.
2. It is sanctioned by the Court, giving it effect by legal process which has been properly considered. Thus if a creditor subsequently is unhappy with the scheme, or was not present at the meeting in order to vote for the same, it remains binding.
3. Dissenting creditors or members can be bound by a scheme of arrangement, avoiding the ability of a creditor blocking the entire scheme.

Cons include:

1. There is no moratorium. Nevertheless if implemented within an provisional liquidation, that will provide the company with the requisite moratorium. with standalone schemes of arrangement.
2. If one class of creditors (or members) are not able to achieve a majority vote to approve the scheme, then the scheme in its entirety is unable to proceed to court sanction.
3. Regardless of the voting, the Court is still able to reject the scheme.

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

Question 4.1 [maximum 4 marks]

Mr Chan is the sole director of Mountainview Limited, which is a Hong Kong incorporated company. Mr Chan comes to you and tells you that the company has financial difficulties and is unlikely to be able to continue in business. A friend has told him that his only option is that he must go to court to wind up the company, and that he should ensure he appoints a "friendly" liquidator who will not investigate the company's affairs too closely. Mr Chan asks whether his friend is correct and to advise him generally on what he should do and his position as a director.

If the company, is facing financial difficulties and, based on information received, appears to be insolvent then Mr Chan can seek to wind up the company. A creditor, a shareholder or the company itself can file a winding-up petition against the company.

However the winding up of a Company is a legal process with oversight by the court. Moreover the liquidator is an officer of the court, and any liquidator will perform their duties in accordance with the legislation and rules that govern his appointment. Indeed, one of the mandated roles of a liquidator is to investigate transactions or payments made during the relevant period (as defined in CWUMPO to determine whether such transactions or payments should be voided. This role also encompasses investigating and considering the conduct of the director.

Whilst there is no statutory obligation on a director of a company to initiate a liquidation when it is in financial difficulty, he should be aware that directors may be held personally liable for a breach of their fiduciary duty to act in the best interests of the company by continuing to trade during insolvency. Of particular importance is the risk of criminal liability/prosecution if the company continues to trade whilst it is unable to pay its employees.

On the appointment of the winding-up order, the powers of the directors of the company will cease. The liquidator will take control of the company. Nevertheless, Mr Chan will be required to :

- (a) deliver to the provisional liquidator or liquidator the company's assets, books and papers and seal;
- (b) attend the office of the provisional liquidator or liquidator for interview to provide information of the company's assets and dealings;
- (c) submit a sworn statement of affairs of the company (similar to a balance sheet) (or a supplementary affidavit, if required by the provisional liquidator or liquidator) within 28 days from the date of the appointment of the provisional liquidator or the date of the winding-up order;
- (d) attend meetings of creditors and contributories when notified by the provisional liquidators or liquidators; and

Commented [RD(DWH19): (1.5 marks) Answer should also advise Mr. Chan of the availability of voluntary liquidation options

Commented [RD(DWH20): But a company cannot petition on the basis of a resolution by directors alone (Emmadart) and there is no indication that Mr. Chan is (necessarily) the only shareholder

Commented [RD(DWH21): Same for voluntary liquidators

(e) continue to co-operate with the provisional liquidator or liquidator until the liquidation is concluded.

Directors who fail to perform their duties such as failure to keep and preserve company's accounting records that comply with section 373(2) and (3) of the Companies Ordinance (Cap. 622), failure to prepare and submit the statement of affairs or a supplementary affidavit, etc. may be prosecuted and disqualified from acting as directors for a certain period of time.

Thus, the advice received from his friend to appoint a "friendly" liquidator is incorrect; the liquidator will be required to investigate any financial transactions that appear to have been made to the detriment of the company and its creditors if it appears that they have occurred.

Question 4.2 [maximum 5 marks]

Kite Limited is a Hong Kong incorporated company involved in an import / export business. It buys goods on its own account from suppliers in Mainland China, then sells them on to buyers in Europe at a mark-up. The company has been in difficulty for some time, for example due to reducing margins; unfavourable credit terms leading to a mis-match between the dates on which Kite must pay its suppliers and the dates on which it gets paid by its buyers, thus affecting Kite's cashflow; European buyers going straight to Mainland suppliers, etc.

Goshawk Financial Limited (GFL) is one of Kite's lenders. Having been troubled by the way Kite's business has been heading, some months ago GFL insisted that Kite execute a charge over its receivables, also insisting that the charge was stated to be a "fixed charge". Kite agreed and executed the document. No separate account was opened and Kite continued to trade with its customers as before, with money being paid into and out of its normal operating account (not held with GFL).

Recently, GFL appointed a receiver pursuant to the charge executed in its favour. The company has also been wound up on a petition presented by another creditor and a liquidator appointed. The receivables appear to be Kite's only assets. The liquidator asks for your advice on whether she can insist that the receiver hand over realisations he makes in order that the costs and expenses of the liquidation can be met and the unsecured creditors paid at least a partial dividend.

Ordinarily, the security agreement in respect of receivables would require the debtor to receive or transfer related payments into a specific account. Based on the facts of the case, this was not done by Kite.

Moreover, the receiver has a primary duty owed to the charge holder, rather than the company. The receiver is entitled to payment of its costs and expenses out of the charged assets and is entitled to exercise a lien over such assets until payment is otherwise made. In respect of fixed charges, charges are made over a specific asset(s) with attachment being automatic. During the period of a fixed charge, the chargee creditor has authority over the asset(s) and the debtor therefore cannot deal with it without consent.

Unfortunately, the liquidation of Kite does not affect the receiver's right to take possession of and/or sell the charged assets, and the primary duty to the chargeholder remains, thus any realisations made out of the charged assets are not available to the liquidator in order to make a partial dividend to unsecured creditors.

Question 4.3 [maximum 6 marks]

Commented [RD(DWH22)]: (0.5 marks) Makes the point that realisations are for secured creditor not liquidation estate, but misses a number of considerations for the advice that should be given to the liquidator:

- >First step in any such situation is to check the validity of the charge – execution, registration etc
- >Say 'fixed charge' but court will look at substance: Spectrum. Here, can use the receivables so floating charge more likely
- >When entered into? Within time period that means may be void against liquidator unless new money (s.267, 267A)
- >If any of the above, L can ignore and insist on being handed all of the receivables
- >Next to consider: was it an unfair preference (security can be UP – see Sweetmart)? If so, L may also be able to get receivables. Say 'may' because would need to make application and notoriously difficult to show company was influenced by desire to prefer.
- >If charge is valid (as floating charge), L cannot lay claim to the receivable (Leyland Daf case) except for preferential creditors (s.265(3B)) – note only asset so there will not be any 'free assets' in estate to meet those

Commented [RD(DWH23)]: (4.5 marks)

Outline of elements should be included is as follows (not all would be needed for full marks):

Question asks that advice be given to L; answer should be written accordingly

The FA clause that all provisions (including repayment to Xu) are void if SPL insolvent is almost certainly void due to the anti-deprivation principle

Whether L is properly appointed would be a matter for BVI law L will be able to take certain steps in Hong Kong without a formal recognition order

Obtain documents from the company's bank (Bay Capital)

Bring an action against Mr. Qi (perhaps for breach of fiduciary duty) (Irish Shipping – but see recent decision of Nuoxi Capital which creates some uncertainty)

IF can find him; also query if has assets (litigation worthwhile?).

Need to investigate

L should obtain a recognition order to take other steps that 'belong' to an office-holder as opposed to the company itself (e.g. examination of individuals):

The Hong Kong court is receptive to such applications from legal systems similar to Hong Kong (BVI is one)

The Hong Kong court will need the originating court (BVI) to make a letter of request

The powers that the liquidator can then exercise in Hong Kong must be powers that he has as a liquidator in the home (i.e. BVI) jurisdiction and that he would have if appointed as a liquidator here in Hong Kong (the Singularis principle)

Note that although the jurisdiction to examine in Hong Kong's legislation is a broad one (s.286B), some jurisdictions restrict the power to examine to officers or closely related parties, so this should be checked carefully, certainly as regards Mr. Wong (no suggestion he is an officer). Need to check with BVI lawyers. [nb, some development in more recent cases re basis on which examination powers are exercised]

Re possible assets in the Mainland and the new "co-operation mechanism":

- o The location of the assets should be identified: at present the mechanism only applies if the debtor's (SPL's) principal assets in the Mainland are in a pilot area or it has a place of business in such an area. The pilot areas are Shanghai, Xiamen and Shenzhen

- o In any event, the mechanism only applies to proceedings commenced under the specifically identified Hong Kong legislation (CWUMPO, CO etc.). It is therefore unlikely that the liquidator could use the mechanism via a recognition application (i.e. he is 'only' a BVI liquidator which the Hong Kong court has recognised for the [1]

Mr Xu entered into a Framework Agreement (FA) with his business associate, Mr Qi. The FA is governed by Hong Kong law. The idea was to develop a resort project in Fiji. The FA provided that Mr Qi would incorporate a BVI company to purchase a 100% interest in the project from its original owners. To this end, Mr Qi incorporated Sunrise Pacific Limited (SPL) in the BVI. He was (and remains) the sole director and shareholder of SPL, telling Mr Xi that this was necessary because the original developers of the resort trusted him and him alone. The FA provided that Mr Xu would inject USD 20 million into the project by advancing that sum to SPL. The FA also provided that if the project could not be developed and sold on to a buyer within a period of two (2) years from the date of the FA, then SPL will pay a sum of USD 22 million to Mr Xu (representing a return of his investment plus USD 2 million to represent interest).

Mr Xu remitted the USD 20 million to SPL but over the months that followed became concerned that the project was not progressing, with many excuses coming from Mr Qi. He subsequently discovered that the project had not even started (and may be a scam entirely). More than two (2) years has passed since the date of the FA and SPL did not pay any money to Mr Xu. Mr Xu therefore obtained a winding up order over SPL in the BVI.

The BVI liquidator appointed has identified:

- (a) There is a clause in the FA that states that if SPL becomes insolvent then all other provisions (including the requirement to pay Mr Xu) are void, and all assets automatically and immediately vest in Mr Qi in order to repay shareholder loans Mr Qi has made;
- (b) SPL has a (supposedly independent) director, Mr Zhang, who lives in Hong Kong; and SPL also has a book-keeper, Mr Wong, who lives in Hong Kong. Neither Mr Zhang nor Mr Wong are replying to emails from the liquidator;
- (c) SPL has a bank account at a bank in Hong Kong;
- (d) It is not known where Mr Qi is currently, but it is believed he is a Hong Kong resident;
- (e) SPL is believed to have assets in the Mainland, but the liquidator is not sure where these assets are located.

The liquidator asks for your advice on what steps he can take in Hong Kong, including as regards a concern he has that Mr Xu in fact had no standing to bring the winding up proceedings in the first place given the clause in the FA at (a) above. The liquidator has also read about a new "co-operation mechanism" between Hong Kong and the Mainland that he would like to use in respect of (e) above.

With regards to Mr Xu's standing to bring the winding up proceedings, the liquidator should be aware of the "anti-deprivation" principle, which prohibits a creditor from being in a better position than other creditors if a clause within a contract is considered "a fraud on the insolvency laws".

In determining whether the anti-deprivation principle has been violated, the courts have developed the following factors to assist in such determination:

1. Is the intention to evade insolvency laws?
2. Does the clause operate in situations other than upon insolvency?
3. Is the assets concerned "flawed"?

Whilst clauses that modify a contract upon insolvency (known as *ipso facto* clauses) as appears to be the case in the FA, are usually upheld, it would be a perversion for Mr. Xu to be being deprived of his investment, or the receipt of a distribution in SPL's insolvency, as it would appear that the clause was created in order to evade insolvency laws, and, the clause operates in situations other than upon insolvency. Thus it would be likely that the Court would not permit the ipso facto clause to be invoked, and his standing as a creditor of SPL, and therefore to bring an application to wind up the company remains valid.

With regards to steps that can be taken in Hong Kong, the liquidator could seek recognition of his BVI appointment in order to obtain information from the director, the book keeper, and from the bank. The powers available to officeholders (either through a Hong Kong winding up or recognition of a foreign appointment) include the production of documents and examination of individuals in Hong Kong, and as such would assist the BVI liquidator in his/her appointment. However, the powers available through recognition are more limited than through liquidation, and it may be prudent to consider a winding up petition in Hong Kong itself. Moreover, if the utilization of the new Cooperation Mechanism between Hong Kong and the Mainland is to be obtained, it is only available to Hong Kong liquidators, and not to foreign officeholders.

In order to obtain recognition or a liquidation, the petitioner must satisfy the court that SPL is sufficiently connected to Hong Kong by satisfying the following "three core requirements" as approved by the Court of Final Appeal:

- There must be a sufficient connection with Hong Kong,
- There must be a reasonable possibility that the winding up order would benefit those applying for it.
- The court must be able to exercise jurisdiction over one or more persons in the distribution of the company's assets.

Further, recent decisions in Hong Kong have highlighted the need to identify if a company's center of main interest ("COMI") is in fact Hong Kong, or elsewhere. Whilst a company's COMI generally means the place of incorporation, the Court will accept that there are other factors which influence where a company's COMI exists. In this case it could be argued that SPL's COMI is in fact Hong Kong, as, its director is there, as is the book keeper, and the company's bank account, and as such the operational aspect of the business is conducted from there.

If indeed there are assets in the Mainland, then the Cooperation Mechanism would provide the necessary recognition required by Hong Kong office holders to obtain assistance by the Intermediate People's Courts. The Hong Kong Court will require a letter of request and evidence of the officeholder's claim against assets held in one of the three pilot areas being Shenzhen, Shanghai; and Xiamen.

*** End of Assessment ***

TOTAL MARKS: 37 out of 50

Formatted: Left

(4.5 marks)

Outline of elements should be included is as follows (not all would be needed for full marks):

Question asks that advice be given to L; answer should be written accordingly

The FA clause that all provisions (including repayment to Xu) are void if SPL insolvent is almost certainly void due to the anti-deprivation principle

Whether L is properly appointed would be a matter for BVI law

L will be able to take certain steps in Hong Kong without a formal recognition order

Obtain documents from the company's bank (Bay Capital)

Bring an action against Mr. Qi (perhaps for breach of fiduciary duty) (Irish Shipping – but see recent decision of Nuoxi Capital which creates some uncertainty)

IF can find him; also query if has assets (litigation worthwhile?). Need to investigate

L should obtain a recognition order to take other steps that 'belong' to an office-holder as opposed to the company itself (e.g. examination of individuals):

The Hong Kong court is receptive to such applications from legal systems similar to Hong Kong (BVI is one)

The Hong Kong court will need the originating court (BVI) to make a letter of request

The powers that the liquidator can then exercise in Hong Kong must be powers that he has as a liquidator in the home (i.e. BVI) jurisdiction and that he would have if appointed as a liquidator here in Hong Kong (the Singularis principle)

Note that although the jurisdiction to examine in Hong Kong's legislation is a broad one (s.286B), some jurisdictions restrict the power to examine to officers or closely related parties, so this should be checked carefully, certainly as regards Mr. Wong (no suggestion he is an officer). Need to check with BVI lawyers. [nb, some development in more recent cases re basis on which examination powers are exercised]

Re **possible assets in the Mainland** and the new "co-operation mechanism":

o The location of the assets should be identified: at present the mechanism only applies if the debtor's (SPL's) principal assets in the Mainland are in a pilot area or it has a place of business in such an area. The pilot areas are Shanghai, Xiamen and Shenzhen

o In any event, the mechanism only applies to proceedings commenced under the specifically identified Hong Kong legislation (CWUMPO, CO etc.). It is therefore unlikely that the liquidator could use the mechanism via a recognition application (i.e. he is 'only' a BVI liquidator which the Hong Kong court has recognised for the purpose of taking certain steps in Hong Kong; he is not appointed under a proceeding commenced under CWUMPO or CO).

o However, the Hong Kong court does have jurisdiction to wind-up non-Hong Kong companies (s.327) if the core requirements are satisfied. These are:

☐ there must be sufficient connection with Hong Kong, (not necessarily meaning the presence of assets within the jurisdiction);

☐ there must be a reasonable possibility that the winding up order would benefit those applying for it; and

☐ the court must be able to exercise jurisdiction over one or more persons interested in the distribution of the company's assets.

o The liquidator could therefore make an application for an ancillary liquidation and it may then be possible that the new mechanism can be utilised (subject to the other criteria being met) – the mechanism making it clear that the COMI of the debtor (COMI in Hong Kong being a requirement) does not necessarily require the company to be incorporated in Hong Kong. [the answer is may be because where, as here, the company is already in liquidation in its jurisdiction of incorporation, the liquidation here would be ancillary – it is yet to be tested whether the Mainland courts will take issue with this. However, for the purpose of this assessment, marks will be awarded for identifying a s.327 winding up as a possible method of accessing the new cooperation mechanism].