



**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).
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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.**

#### **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.

#### **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.

**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).

(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(DWH2):** 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(DWH3):** 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(DWH4):** 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(DWH5):** 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(DWH6):** Incorrect (0 marks) - 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(DWH7):** Incorrect (0 marks) – see rule 84 CWUR and 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(DWH8):** 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(DWH9)]:** 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]

**Commented [RD(DWH10)]:** (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?

Under the Bankruptcy Ordinance (BO) a debtor must be an individual and in particular, section 4 of the BO provides that a debtor must:

- (i) be domiciled in Hong Kong;
- (ii) be personally present in Hong Kong on the day on which the petition is presented; or
- (iii) at any time in the period of three years ending with that day:
  - (a) have been ordinarily resident, or have had a place of residence in Hong Kong; or
  - (b) have carried on business in Hong Kong.

### Question 2.2 [maximum 3 marks]

**Commented [RD(DWH11)]:** (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 three core requirements that must be shown in court in order to establish that an unregistered company in Hong Kong is sufficiently connected to Hong Kong, thereby said company can be wound up are:

- (a) there must be sufficient connection in Hong Kong (not necessarily referring to having assets within Hong Kong);
- (b) there must be a reasonable possibility that the winding up order would benefit those applying for it; and
- (c) the court must be able to exercise jurisdiction over one or more person interested in the distribution of the company’s assets.

### Question 2.3 [maximum 4 marks]

**Commented [RD(DWH12)]:** (4 marks)

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

A provisional liquidator can be appointed pursuant to section 193 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (CWUMPO).

A provisional liquidator can be appointed by filing an application in court any time after a winding up petition has been presented and in an urgent case, the appointment applicant can be made same time as the winding up petition. Note that, even when a voluntary liquidator has been appointed, the court still has jurisdiction to appoint a provisional liquidator. The court must be satisfied that there are circumstances justifying the

appointment of a provisional liquidator, for example - there is a risk that assets will be dissipated, or otherwise in jeopardy before a winding up order is made. The court will also take into consideration factors including commercial realities, the degree of urgency, the need for the order and balance of convenience. The court is empowered to limit and restrict the powers of a court-appointed provisional liquidator.

The function of a provisional liquidator includes:

- (a) preserving assets in the period after the presentation of the petition but before winding up order is made. The provisional liquidator does not have to realise those assets (save in situation where realising the assets is necessary to preserve them).
- (b) Sell assets only upon specific application is made in court.
- (c) To help facilitate a restructuring proposal (note that this cannot be the sole reason for appointment).

### 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.

A liquidator is empowered to take action against unfair preference as such transaction occurs when the insolvent company places a creditor in a better position than it would have been upon liquidation of the company. To successfully claim undue preference, the liquidator must show that:

- (a) At the time of the alleged undue preference was given, the company was unable to pay its debt or became unable to pay its debt as a result of the undue preference transaction.

This is presumed against a recipient who is "a person connected with the company", but such presumption is open to challenge by the recipient of the undue preference. To establish that one is a "person connected", he/she would be an "associate" of the company or director/shadow director of the company.

- (b) The company was "influenced by a desire" to improve the creditor's position when the company goes into liquidation. In practice, this element is difficult to establish. Based on the test set out and adopted in the cases of *Re MC Bacon* [1990] BCLC 324 and *Hong Kong Osman Mohammed Arab* [2017] HKEC 2435, a transaction will not be set aside as an unfair preference "unless the company positively wished to improve the creditor's position in the event of its own insolvent liquidation" and a person does not "desire" all of the "necessary consequences of his actions". Example of such undue preference is when a company gave to its bank a mortgage over an asset and the court considered there were no good grounds to grant the mortgage and that the company deseired to prefer the bank because personal bankruptcy proceedings were being threaten against the company's directors (see *Re Sweetmart Garment* [2008] 2 HK 252.

**Commented [RD(DWH13):** (3 marks) Need to say "why". Reason is the pari passu principle and that all creditors should be treated fairly amongst themselves. Should also state time limits and distinction between connected and unconnected parties; and requirement that party 'preferred' is a creditor or surety

**Commented [RD(DWH14):** Presumption of insolvency applies only to transactions at an undervalue, not unfair preferences (s266B(3))

**Commented [RD(DWH15):** Rebuttable presumption of desire to prefer where beneficiary is a connected person.

**Question 3.2 [maximum 5 marks]**

Commented [RD(DWH16)]: (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.

Such a statement would be correct prior to May 2021. Hong Kong has not adopted the UNCITRAL Model Law, has not sign any international treaties in relation to cross-border insolvency nor has it enter into any bilateral agreements with the Mainland. Therefore, prior to May 2021, the difficulty of cross-border insolvency matters between Hong Kong and the Mainland were dealt via common law.

Under the common law, there is now at least 2 cases where the Hong Kong courts gave recognition to officeholders from the Mainland, despite it not being a common law jurisdiction. However, under the Mainland law, for a proceeding (including those from Hong Kong) to be recognized in the Mainland, there needs to be reciprocity.

However from May 2021, new arrangement of cooperation mechanism was made between Hong Kong and certain areas of the Mainland, namely Shanghai, Xia Men and Shenzhen which are the designated pilot areas. Such cooperation mechanism stemmed from the record of meeting between representatives from Hong Kong and the Mainland and is intended to further Article 95 of the Basic Law – which states that “The Hong Kong Special Administrative Region may, through consultations and in accordance with law, maintain juridical relations with the judicial organs of other parts of the country and they may render assistance to each other”.

Based on the record of meeting, supplemented by an opinion of the Supreme Court:

- (a) A Hong Kong appointed liquidator or provisional liquidator is entitled to apply for recognition in the Mainland. Similarly, Mainland appointed administrators can apply for recognition in Hong Kong.
- (b) “Hong Kong Insolvency Proceedings” mean any collective insolvency proceedings commenced under CWUMPO or the CO, including compulsory liquidations, creditors’ voluntary liquidations and scheme of arrangement which involves a liquidator or provisional liquidator.
- (c) The debtor’s centre of main interest (COMI) must be in Hong Kong. For this purpose, COMI would generally mean place of incorporation of the debtor but the Supreme Court has also stated that other factors to be taken into account is the place of principal office, the principal place of business, place of principal assets of the debtor. The Supreme Court also stated that when a Hong Kong administrator applies for recognition and assistance before the Mainland courts, the COMI of the debtor shall have been in Hong Kong Special Administrative Region continuously for at least 6 months.
- (d) The Supreme Court also stated that a Hong Kong administrator may apply for recognition and assistance to the Hong Kong Insolvency Proceeding, if the debtor’s principal assets in the Mainland are in the pilot area, or it has a place of business or a representative office in a pilot area, the Hong Kong administrator.
- (e) Must obtain a letter of request from the Hong Kong Court to support the recognition application in Mainland court.



**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.

A scheme of arrangement (SOA) is a statutory mechanism which enables a company to propose compromises/arrangements with its members/creditors (or any class of them), including adjustments of debts owed to its creditors or reduction of share capital. If such propose scheme is approved it will be binding on all, or the relevant, creditors. SOA is governed by sections 668 to 677 of the Companies Ordinance and Order 102 rule 2 and rule 5 of the Rules of the High Court. Essentially, SOA is a three stage procedure as follows:

- (a) Stage 1 – The applicant company files an application in court (via originating summons) for leave to convene scheme meeting with creditors to consider, and if thought fit, approve scheme. The Court is empowered to provide directions on giving notice of and advertising such meetings to the relevant parties including inter alia creditors.

This application must be accompanied by an affirmation to provide explanation regarding the proposed SOA including exhibiting a copy of the draft explanatory statement (in compliance with section 671 Companies Ordinance), a draft scheme document, draft notices of scheme meeting, copy of proxy forms and draft advertisement to be published.

- (b) Stage 2 – The scheme meeting is convened where creditors vote on the proposed scheme.
- (c) Stage 3 – The applicant company files a petition for the Court to sanction the SOA. During this sanction stage, the court will also look into the issue of classification of creditors.

One of the downside of a Hong Kong SOA is the lack of moratorium. Contrary to other the mechanism of SOA of other nations such as that of Australia, UK or the US, there is on automatic moratorium that kicks in upon commencement of SOA which acts as a safe space for a financially distressed company to propose its scheme to creditors without being pressured by enforcement actions by creditors, for example. Due to the lack of statutory moratorium, or at all, the development in Hong Kong Law, namely the Rules of the High Court, is such that the court is empowered to make certain orders to stay court proceedings pending a winding up proceeding. The Court in *Eastman Chemical Ltd v Heyro Chemical Co Ltd* [2012] HKEC 272 has stated that pursuant to the Rules of the High Court, the court may grant a stay to aid a restructuring effort (one such as SOA) – as per UK Court in *BlueCrest Mercantile*.

Further, it is also a downside that the issue of classification of creditors are only considered during stage 3 of the SOA (sanction 3). As such, in reality, there is still a likelihood that the SOA will fail if the Court is of the view that the classification of creditors is not correct, after the all relevant creditors have considered the proposed scheme and scheme meetings had been convened with all necessary procedures complied. This will undoubtedly cause delay in the SOA process as the creditors would need to be re-classed, which would lead to increase in cost. It could be argued that matters concerning classification of creditors could also be decided by the court during stage 1 of the SOA.

In terms of procedure, unlike the UK SOA, in Hong Kong there is no requirement for a creditors' issue letter (also known as practice statement letter) to be issued to notify scheme creditors, on a confidential basis, that the company is proposing to apply to court to seek an

**Commented [RD(DWH17)]:** (3.5 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)  
Reference should be made to the majorities required

order to convene creditors meeting under a SOA and to provide details of the proposed scheme. As such, scheme creditors in Hong Kong do not get the benefit of an advance notice to consider the proposed scheme or rather to consider its options. Arguably, this benefits the applicant company as there is no risk of certain creditors taking steps which may adversely affect the company's proposed scheme before the applicant file its application in court.

Under a SOA, it is beneficial to the applicant company as it does not need to obtain approval of 100% of relevant creditors to contractually vary debts owed to creditors. Scheme is also useful where there may be hold-out creditors who seek an unfair advantage or preferential treatment against other similarly ranked creditors. Under the proposed scheme, the company would have the liberty to propose scheme viable to its business and once the proposed scheme is approved, it binds all the relevant creditors (including dissenting creditors).

#### 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.

From a legal insolvency point of view, an option available to Mr Chan would be to initiate liquidation of Mountainview Ltd through members' voluntary liquidation. When Mr Chan said that his company is in "financial difficulties" and "is unlikely to be able to continue in business", firstly, it should be ascertained whether Mountainview Ltd will be able to satisfy the ground of "inability to pay debts" under section 178 of the CWUMPO. Mountainview Ltd would be regarded as unable to pay debts:

- (a) If a creditor had issued a demand (as required under section 178 CWUMPO) for a sum of debt and for 3 weeks after the service of the demand, Mountainview Ltd neglected to pay the sum, or to secure or compound for it to the reasonable satisfaction of the creditor; or
- (b) If Mountainview Ltd is unable to satisfy execution (or other process) issued on a judgment, decree or order of any court in favour of a creditor.; or
- (c) If it could be proved to the satisfaction of the court that Mountainview Ltd is unable to its debt and in determining whether Mountainview Ltd is unable to pay its debt, the court shall take into account the contingent and prospective liabilities of the company.

If items (a), (b) or (c) could be proved, then Mountainview Ltd is unable to pay its debt thus it is possible for Mr Chan to enter into a members' voluntary liquidation, as long as it can settle all its liabilities within 12 months from the commencement of the proceedings.

In terms of procedural requirements:

- (d) Mr Chan is required to sign a "certificate of solvency".
- (e) The shareholders of Mountainview Ltd must pass a special resolution for winding up and appointment of liquidators.

**Commented [RD(DWH18):** (1.5 marks) Given the question it is perhaps more likely that a CVL is necessary. Should be explored in any event. An important omission

Should also advise that if company is insolvent owes duties to creditors ahead of the company

**Commented [RD(DWH19):** Only if company can meet all liabilities within 12 months

Once liquidator is appointed, the liquidator will take over control of Mountainview Ltd from Mr Chan and will investigate the affairs of the company including the conduct of Mr Chan. This is part of the appointed liquidator's statutory duty therefore, there is no such thing as a "friendly liquidator" who will not investigate the company's too closely as such liquidator is risking breach of statutory duty and professional negligence. Broadly, the duty of the liquidator also includes realising assets to make payments to creditors and then shareholders. The fees of the liquidator will also be paid out of the assets of the company with excess fund thereafter to be paid to members of Mountainview Ltd.

Commented [RD(DWH20)]: Correct

#### 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.

Commented [RD(DWH21)]: (0.5 marks) A good note on unfair preferences but misses the thrust of how you should advise L:

>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

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.

The liquidator of Kite is entitled to take action to challenge the charge given in favour of GFL on the ground that such transaction amounts to an undue preference. Essentially, the liquidator would have to argue that, by Kite granting the said charge, Kite had placed GFL in a better position than it would have been upon liquidation of Kite. To successfully claim undue preference, the liquidator must show that:

Commented [RD(DWH22)]: May be

- (c) The charge was executed 6 months prior to the commencement of the liquidation. On the facts, it appears that the charge was executed "some months ago" – as long as it is within 6 months before the liquidation of Kite, such charge could be argued to be an undue preference.
- (d) At the time of when the charge was executed, the company was unable to pay its debt or became unable to pay its debt as a result of the undue preference transaction. On the facts, it appears that Kite was indeed already having financial difficulties and in fact, such financial difficulties are what prompted GFL to convince Kite to execute a charge over its receivables.
- (e) The liquidator must also show that Kite was "influenced by a desire" to improve the creditor's position when the company goes into liquidation. By applying the test set out in the cases of *Re MC Bacon* [1990] BCLC 324 and *Hong Kong Osman Mohammed Arab* [2017] HKEC 2435, the charge will not be set aside as an unfair preference

“unless the company positively wished to improve the creditor’s position in the event of its own insolvent liquidation” and a person does not “desire” all of the “necessary consequences of his actions”.

On the facts, there might be difficulty in establishing that Kite indeed was “influenced by a desire” to improve the GFL’s position when it goes into liquidation. Kit’s liquidator would have to try to argue that there is no good grounds for Kite to grant such charge in favour of GFL as it does not benefit Kite’s course of business and that GFL indeed had concerns (and had communicated such concern via medium which could be used as evidence in court) that Kite was unable to pay its debt at the time of the transaction (i.e. charge).

If successful, the transaction would be set aside. Under section 266 of CWUMPO, the court could order that the charge given by Kite in favour of GFL be released or discharged, direct GFL to pay to Kite’s liquidators any benefits (including the receivable) received by GFL. Should there be any debt owed by Kite to GFL, such debt would be proved via proof of debt and the liquidator will pay GFL accordingly following the relevant distribution under the law.

#### Question 4.3 [maximum 6 marks]

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;

**Commented [RD(DWH23)]:** (0.5 marks) for mentioning the new mechanism re Mainland

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].

- (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.

In Hong Kong, foreign judgments can be enforced either via:

- (a) Statutory recognition via Foreign Judgments (Reciprocal Enforcement) Ordinance (FJREO); Foreign Judgments (Restriction on Recognition and Enforcement) Ordinance; or
- (b) Common law.

The FJROE applies to judgments from 15 jurisdictions such as inter alia Australia, France, Malaysia etc, but does not include BVI. Therefore, the BVI liquidator will not be able to rely on FJROE to seek recognition of the BVI winding up order.

Commented [RD(DWH24)]: Not relevant; see module text

The BVI liquidator could consider enforcing the BVI winding up order by common law. The BVI should take note of the following:

- (a) There is no requirement for the foreign judgment to originate from a common law jurisdiction therefore the BVI winding up order would qualify for enforcement in Hong Kong under common law.
- (b) An enforcement action upon the winding up order must be brought within 6 years after the date on which the winding up order becomes enforceable.
- (c) The law is trite in that foreign monetary judgment can be enforced in Hong Kong if it is a final and conclusive on the merits. A winding up order would satisfy this requirement.
- (d) The foreign judgment must be for a fixed sum and must also come from a competent court. If the judgment sum is clearly set out in the BVI winding up order, then this would not be an issue. There is also nothing to suggest that the BVI court is not a "competent" court.
- (e) The BVI liquidator is required to file a write endorsed with a short statement of claim. If the claim is defended by SPL in the Hong Kong court, it is likely that the matter would be dismissed summarily.

#### Assets in Mainland (but not sure where assets are located)

There could be 2 scenarios arising from this point. Scenario 1 – If the assets are situated within any of the designated pilot areas (i.e. Shanghai, Xia Men and Shenzhen), the appointed liquidator could rely on the new "cooperation mechanisms". In order to rely on the new cooperation mechanism, the recognition application must be applied by a Hong Kong appointed liquidator or provision liquidator – the BVI liquidator would not have locus to file such recognition application in the Mainland.

Commented [RD(DWH25)]: Hence should consider ancillary liquidation

Scenario 2 – if the China assets are situated outside of Shanghai, Xia Men and Shenzhen, neither the BVI Liquidator nor a Hong Kong appointed liquidator could seek recognition nor assistance from the relevant China court to assist with location the assets, if any.

**\* End of Assessment \* TOTAL MARKS: 32 out of 50**

