



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.**

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).

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.

(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)]: Incorrect (0 marks) – see section 6.4.1 and 5.5 of text: preferential creditors are paid out of assets subject to a floating charge (unless the company is in liquidation and there are sufficient assets to make those payments out of the general estate). 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.

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.

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.

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(DWH7)]: Incorrect (0 marks) - s.186 CWUMPO (section 6.3.7 of text); the mandatory stay also applies if a provisional liquidator is appointed.

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

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).

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?

The Bankruptcy Ordinance (Cap 6) (**BO**) provides the statutory requirements to be met for a bankruptcy petition to be presented against a debtor. Specifically, §4 of the BO states that a debtor:

- Is domiciled in Hong Kong: §4(1)(a) BO;
- Is personally present in Hong Kong on the day on which the petition is presented: §4(1)(b);
- At any time in 3 years ending with the day
 - He has ordinarily been resident, or has a place of residence, in Hong Kong; or
 - He has carried on business in Hong Kong: see §4(1)(c)(i)-(ii) BO.

For the purposes of this section, a debtor shall be considered to carry on business in Hong Kong if the debtor was (i) carrying on business as a firm or partnership of which the debtor is a member: §4(2)(a) BO; or (ii) carrying on business by an agent or manager of the debtor for such firm or partnership: §4(2)(b) BO.

Question 2.2 [maximum 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 Hong Kong Courts have a statutory power to wind up a registered non-Hong Kong company¹ provided three core requirements are satisfied. These core requirements have developed to justify the Court setting in motion its winding up procedures over a corporate body to which *prima facie* is beyond the limits of its territoriality. Specifically, (i) there had to be a sufficient connection with Hong Kong, but this does not necessarily have to consist of assets within the jurisdiction; (ii) there must be a reasonable possibility that the winding up order would benefit those applying for it; and (iii) the court must be able to exercise jurisdiction over one or more of the persons in the distribution of the company's assets: see *Re China Huiyan Juice Group Ltd* [2021] 1 HKLRD 255 at §19.

Question 2.3 [maximum 4 marks]

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

Further to section 193 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32) (**CWUMPO**) a provisional liquidator may be appointed by the Hong Kong Court any time after the presentation of a winding up petition and before the making of a winding up order: §193(1) **CWUMPO**.

¹ Article X **CWUMPO**

Commented [RD(DWH11)]: (2.5 marks). The list stated does not make clear whether all 3 elements are necessary or only 1. It is the latter.

Commented [RD(DWH12)]: (3 marks). FYI, Although China Juice is a more recent case, where there is a CFA case, the convention is to cite it. Here, the Yung Kee case

Commented [RD(DWH13)]: (3 marks). See note below; an important distinction

Further to section 193 of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap 32) (**CWUMPO**), a provisional liquidator may be appointed by the Hong Kong Court any time after the presentation of a winding up petition and before the making of a winding up order: §193(1) **CWUMPO**.

There are two instances for which applications are made for the appointment of provisional liquidators. First, there is evidence of mismanagement by the company directors, which gives rise to a risk that the company's directors may dissipate its assets before a winding-up order is made. In that regard, a provisional liquidator may be appointed to secure the company's assets and preserve their value until the winding-up order is made. Second, a provisional liquidator may be appointed where the company wishes to reorganize its debt and enter into a scheme of arrangement with its creditors².

Commented [RD(DWH14): Correct, but this cannot be the sole reason for appointment

A provisional liquidator's powers will be governed by the powers directed by the Court in the order appointing the provisional liquidator: §193(3) **CWUMPO**. In considering an application for the appointment of a provisional liquidator, the Hong Kong Court will have regard to the following factors:

- The commercial realities;
- The degree of urgency;
- The need for an order appointing a provisional liquidator; and
- The balance of convenience³.

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

Question 3.1 [maximum 5 marks]

Commented [RD(DWH15): (4.5 marks). See below re the 0.5

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.

The primary principle which underlies insolvency procedure is that this is a collective procedure which allows the general body of unsecured creditors of a company to share in the assets of the insolvent estate, equally, on a *pari passu* basis. In stark contrast to this underlying principle, an unfair preference payment by a company to a creditor prefers the interest of that creditor to the extent that such a creditor is placed in a better position than it would have been had the company entered insolvency. Given the global nature of business today, and the separate legal personality of companies, the look back period for unfair preferences to a "connected party" is extended to two years. This further underscores the importance of the collective nature of insolvency procedures.

Section 266 of the CWUMPO confers standing on a liquidator to apply to set aside an unfair preference provided that the statutory requirements are satisfied. A company gives an unfair preference to a person if:

- The person is a creditor of the company or a guarantor of the company's debt: see §266A(1)(a)(i)-(ii);
- The effect of the unfair preference is to put that creditor in a better position than it would have been in the event that the company entered into insolvent liquidation: see §266A(1)(b);

² Module at [6.3.8]

³ *Ibid.*

- At the time that the unfair preference was given the company was unable to pay its debts within the meaning of section §178; see §266B(2);
- The unfair preference was given (i) to a person connected with the company 2 years within the onset of insolvency: 266B(1)(b), or in all other cases, (ii) the period of six months ending with the onset of insolvency (i.e. the presentation of the petition): 266B(1)(c); and
- In giving the unfair preference the company was influenced by a desire to prefer the creditor⁴.

If the Court is satisfied that the above requirements are satisfied, by way of example, the court may order any of the following: (i) the property transferred be vested in the company: 266C(1)(a); (ii) release or discharge any security given by the company: §266C(1)(c); or (iii) require any person who received the benefit of the unfair preference to pay sums to the liquidator: §266C(1)(d).

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 has not adopted the UNCITRAL Model Law on Cross-Border Insolvency, nor is a party to any treaties dealing with cross-border insolvency. Before May 2021, there was no arrangement for a Hong Kong office holder to obtain recognition and assistance in the PRC. Thus, it was challenging, if not impossible, for a Hong Kong office holder to take any action in the PRC.

On 14 May 2021, the Supreme Court in Mainland of the PRC and the Hong Kong Court entered into a "Record of Meeting" for mutual recognition and assistance to Hong Kong office holders in the PRC. Presently, this is a pilot program that is limited in scope. Thus, the three regions in Mainland PRC to which the "Record of Meeting" applies are: (i) Shanghai municipality; (ii) Xiamen Municipality of the Fujian province; and (iii) Shenzhen municipality of Guangdong Province.

Under the "Record of Meeting" pilot program, a Hong Kong office holder must satisfy the following requirements before he/she may apply for recognition and assistance in one of the provinces as mentioned above:

- The debtor company's COMI is in the Hong Kong Special Administrative Region;
- The debtor company has its principal assets or a place of business/representative office in the three pilot regions listed above;
- The Hong Kong insolvency proceeding must be a compulsory liquidation, creditors voluntary liquidation, or a scheme of arrangement commenced by a liquidator or a provisional liquidator⁵; and
- None of the circumstances where the Mainland courts to refuse to grant recognition or assistance⁶.

⁴ Module at [6.3.15.1]

⁵ Module at []

⁶ [Kwm.com/hk/en/insights/latest-thinking/pilot-mechanism-in-cross-border-insolvency.htm](https://www.kwm.com/hk/en/insights/latest-thinking/pilot-mechanism-in-cross-border-insolvency.htm)

Commented [RD(DWH16): Rebuttable presumption of desire to prefer where beneficiary is a connected person.

Commented [RD(DWH17): (4.5 marks) Could also have referred to the pre-existing tools (e.g. s.327 and common law developments such as CEFC Shanghai)

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.

In Hong Kong, there is no equivalent to a UK administration procedure or US Chapter 11 to rescue a Hong Kong company facing financial difficulties. In Hong Kong, a company may seek to restructure its debts under a scheme of arrangement under 13 of the CWUMPO.

The scheme procedure is a three-stage process. First, an application is made to the Hong Kong Court seeking leave to convene a meeting of creditors. Second, a meeting is convened for a class of creditors or the company's creditors to vote on the proposed scheme. Before this meeting, the creditors must be provided an explanatory statement that must set out the scheme's effect to give such creditors sufficient information to make an informed decision. To proceed to the third stage of this process, the proposed scheme must be approved by a majority of the company's creditors, being over 50% in number representing 75% in value of the creditors voting at the meeting. Where there are classes of creditors, the scheme must be approved by all classes of the company's creditors. If the company attains the requisite statutory approval from the creditors, the scheme is submitted to the court for approval at a further court hearing. In considering whether to sanction the scheme, the court will have regard to (i) whether the procedural requirements have been satisfied and (ii) the fairness of the proposed scheme between the company and the creditors. If the court sanctions the scheme, the scheme will be binding on the creditors and the company.

A Scheme rather than a liquidation of a company may be advantageous to the company, creditors, and directors. The company will continue as a going concern after successfully implementing a scheme. This self-evidently benefits the company, its employees, and trade creditors. Indeed, if a company is placed into liquidation, then the company will cease to carry on business and be dissolved; if the company presents a petition for the appointment of provisional liquidators, this will trigger a statutory moratorium. This will provide the necessary breathing space for the company to negotiate with its creditors without having creditors bring claims against it or file a petition to wind up the company. Finally, without the scheme procedure, a company must obtain 100% of all the creditors to restructure its debt. While this may be possible in certain circumstances, a scheme allows a company to reorganize its debts where 100% consent may not be possible. Moreover, this significantly reduces the risks of holdout creditors seeking an unfair advantage over the company's other creditors.

As regards creditors, generally speaking, in a liquidation scenario, the unsecured creditors of a company typically expect to receive pennies on the dollar on their debts. By agreeing to a scheme of arrangement, the creditors are more likely to receive a higher sum in repayment of their debt.

As regards directors, provided that the scheme is implemented, this will avoid the detailed investigation of the company's affairs. Additionally, a scheme will minimize the risk of a director being personally liable for fraudulent trading.

One con to this procedure is that it does not automatically trigger a statutory moratorium which prevents individual creditors from enforcing their claims against the company without leave of the court. To address this issue, a company may present a winding-up petition seeking the appointment of a provisional liquidator for a restructure.

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)
Reference should be made to the majorities required

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

Question 4.1 [maximum 4 marks]

Commented [RD(DWH19): (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.

As a preliminary point, Mr Chan, the sole director of Mountainview Limited (**MV**), owes certain fiduciary duties to MV. Where a company is insolvent or in the zone of insolvency, as is the case here with MV, Mr Chan's duties shift to act in the best interest of the general body of MV's unsecured creditors. Mr Chan must be mindful of this duty because if Mr Chan were to act in breach of these duties if MV enters liquidation, a liquidator might bring actions against Mr Chan on behalf of MV. Thus, if Mr Chan fails to comply with his fiduciary obligations, Mr Chan may be subject to personal liability for civil and/or criminal penalties. In addition to Mr Chan's fiduciary duties, he must keep proper records. It is an offence to falsify or alter the books and records with the intent to defraud creditors: §272 CWUMPO.

Upon filing a winding up petition (which will be discussed below), Mr Chan must also be aware of the following. First, any disposition of MV's property is void unless the court validates it. While it is possible to seek retrospective validation, the prudent course for Mr Chan would be to seek prospective validation. Second, any creditor of MV who has been granted a security (i.e., a floating charge within 12 months of the winding up); a transaction at an undervalue; unfair preference; or fraudulent trading such transactions are liable for claw back a liquidator. Again, such a determination by the Hong Kong Court may result in personal liability for Mr Chan.

While there is no statutory definition of insolvency, a company will be considered "insolvent" if it cannot meet its debts under §178(1) of the CWUMPO. Suppose MV is unable to pay its debts within the meaning of §178(1) of the CWUMPO. In that case, MV may be placed into liquidation either by a creditors voluntary liquidation (**CVL**)⁷ or a compulsory liquidation. Regarding CVL, a director of CVL (i.e., Mr Chan) may convene a meeting to pass a special resolution to wind up MV. Following the special resolution, a meeting of creditors must be convened within 14 days of the date of the resolution to appoint a liquidator.

In respect of a compulsory winding up, such procedure may be commenced by **the company**, a contributory or creditor of the company. Creditors most commonly use this procedure. Upon such application, if the court is satisfied that the grounds for winding up a company under §177 are satisfied, an order will be made, and a liquidator will be appointed.

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]

In either scenario, upon the appointment of a liquidator, the powers of Mr Chan, as director, will be displaced and rest with the liquidator. More importantly, a liquidator will be appointed to secure the company's assets, adjudicate creditors' proofs of claim, investigate the affairs of a company, and distribute the assets of the MV's creditors in accordance with the statutory priority.

⁷ §228 CWUMPO

The sensible course for Mr Chan to adopt is to ensure MV acts in the best interests of its creditors. Rather than wait for a creditor to apply to the court to wind up MV, Mr Chan should consider placing MV into CVL. This will minimize a liquidator later bringing a fraudulent trading claim seeking personal liability against Mr Chan. The position will be even stronger provided Mr Chan has not given any unfair preferences or carried out any transactions at an undervalue. That being said, a liquidator appointed under either scenario is under an obligation to investigate the affairs of the company. Therefore, it will not be possible to appoint a partial liquidator to carry out the liquidation of MV.

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.

In Hong Kong, common forms of receivables capable of being security include but are not limited to cash deposits or trade receivables. Security can be granted over such assets by way of either a "fixed" or "floating charge". As regards a "fixed charge," this is a charge which automatically attaches to the identified asset, in this case, the cash deposits, immediately upon the creation of the fixed charge. This form of security is preferred by creditors as a charge is not allowed to deal with the asset subject to the secured asset without the consent of the charger. In contrast, a "floating charge" is a charge created over a specifically identified category asset that will crystalize into a fixed charge upon the occurrence of a specified event (by way of example, the presentation of a winding up petition). It is essential to bear in mind that GFL's classification of the charge as a "fixed" charge is not determinative of its nature and, if considered by a court, will largely depend on the extent of control the chargee may exercise over the charged asset⁸.

Here, GFL and Kite purportedly executed a security instrument whereby Kite agreed to grant a fixed charge over the cash deposits of Kite. Notwithstanding this fact, GFL failed to take control over the cash deposits by giving express written notice to Kite to pay the cash deposits into a separate account. Indeed, following the purported grant of the fixed charge, Kite continued to trade with its trade creditors, and the cash deposits were paid into Kite's normal operating account.

⁸ Module at [5.4]

Commented [RD(DWH21)]: (4.5 marks) Full marks if mentioned the 'new money' point (below) and that could also consider unfair preference

As a consequence, there are very strong prospects that a court, considering whether this charge was a fixed or floating charge, would determine that the charge created over Kite's cash deposits was a "floating" rather than a fixed charge. This is significant for two reasons.

First, under §267 of the CWMPPO, a floating charge may be invalid if it is granted 12 months before the onset of liquidation if the company is insolvent or, as a result of the charge, the company is invalid. Although it is not clear from the facts whether Kite was insolvent at the time charge was granted, if Kite was insolvent or insolvent following the grant of the charge, then the charge is invalid, and the liquidator could insist that the realizations be handed over to the liquidator. In that regard, the realizations would be available to the liquidator to apply towards the payment of the expenses of the liquidation and distributed to the unsecured creditors of the Kite.

Second, in the insolvency context, if Kite's unsecured assets are insufficient to meet certain statutory preferential claims (i.e., liquidation expenses and employment claims under §267), the floating charge assets will be applied to meet these claims: §265(1) CWUMPO. Thus, if the floating charge is not invalid under §267, it will not be possible to insist that the receiver's realizations are returned to the liquidator of Kite to be distributed to its unsecured creditors. However, as indicated above, the liquidator may require the return of the receiver's realizations to meet the expenses of a liquidator and the employment claims.

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(DWH22)]: Agree

Commented [RD(DWH23)]: Unless new money

Commented [RD(DWH24)]: (4 marks) A bit confused in parts but overall has the right elements

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]

- (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.

The BVI office holder has identified a clause in the FA that states that if SPL becomes insolvent, then all of the other provisions (including SPL's obligation of repayment) are void, and all of SPL's assets vest immediately in Mr Qi for the repayment of his shareholder loans. The effect of such provision raises two separate and distinct questions. First, if such provision is valid, would Mr Xu have had standing as a creditor of SPL to file a petition to wind up SPL in the BVI. If Mr Xu did not have standing to file a petition, then it will not be possible for the BVI office holder to seek relief in Hong Kong on the footing of said petition. Consequently, Mr Xu would have to issue a fresh petition in Hong Kong to wind up SPL under the Court's jurisdiction to wind up a non-Registered Hong Kong company. For the Court to grant such an order, the three core requirements (discussed more fully below) will have to be satisfied. For present purposes, as the question of standing is a matter of BVI law, it is assumed that Mr Xu had standing to file a petition. The next question is whether such a clause is valid under Hong Kong law.

Commented [RD(DWH25): If the clause is valid, how could he be in a better position in HK than he was in BVI?

As indicated above, the effect of the provision in the FA is to contract out of the insolvency legislation (i.e., the statutory priority of payments under Hong Kong law). Under Hong Kong law, in a liquidation scenario, Mr Qi's shareholder loans would be treated as the company's unsecured debt. In this regard, Mr Qi would be entitled to a *pari passu* distribution with the other unsecured creditors of SPL instead of the immediate repayment of his shareholder loan. In the premise, this provision may be void under the anti-deprivation rule. The case of *Belmont Park Investments Pty Limited v BNY Corporate Trustee Services Limited* helpfully distilled the principles a court will apply in determining whether the anti-deprivation rule has been violated to invalidate the provision. Courts have held that the anti-deprivation rule has been violated where (i) the party seeking to take advantage of the deprivation was trying to avoid the bankruptcy rules⁹; (ii) the deprivation did not take place for reasons other than bankruptcy¹⁰; and (iii) the asset is "flawed" in that the party seeking to take advantage of the provision cannot by contract qualify it in the event of his own bankruptcy¹¹.

Applying the above to the factual matrix of this case, the BVI office holder would have reasonable prospects of challenging the provision as being void under the anti-deprivation rule. This is because the creditors of SPL would be deprived of an asset by SPL under the terms of the FA playing such asset beyond the reach of its creditors. Therefore, if such a provision is void, then Mr Xu would have had standing, as a creditor of SPL, to file a petition in the BVI. If I am wrong, as indicated above, Mr Xu would have to file a fresh petition in Hong Kong and satisfy the three core requirements discussed below.

The BVI office holder may commence a liquidation in Hong Kong ancillary to the BVI insolvency proceedings. Alternatively, the BVI office holder may seek recognition and assistance from the Hong Kong court. It should be noted that the Hong Kong courts, under common law principles of modified universalism, have been willing to assist foreign courts and

⁹ *Belmont Park* at [71]

¹⁰ *Ibid* at [80]

¹¹ *Ibid* at [84].

office holders in cross-border insolvency matters. The appropriate procedure will primarily depend on the scope of the powers required by the office holder. If which will likely be the case here, the BVI will wish to have the full range of powers exercisable by a Hong Kong officer holder under the CWUMPO; the BVI officer holder should make an application for an ancillary liquidation. This is especially the case where there are potentially assets in the PRC.

To commence an ancillary liquidation in Hong Kong, the BVI office holder must satisfy the three core requirements for the Hong Kong court to exercise its jurisdiction to wind up a non-registered Hong Kong company. Specifically, (i) there has to be a sufficient connection with Hong Kong, but this does not necessarily have to consist of assets within the jurisdiction; (ii) there must be a reasonable possibility that a winding up order would benefit those applying for it; and (iii) the court must be able to exercise jurisdiction over one or more of the persons interested in the distribution of the company's assets: *Re China Huiyan Juice Group Ltd* [2021] 1 HKLRD at §19.

As regards requirement number one, there is a sufficient connection to Hong Kong. This is because (1) the FA Agreement is governed by Hong Kong law; (2) Mr Zhang, SPL's independent director, is resident in Hong Kong; (3) Mr Wong, SPL's bookkeeper, is resident in Hong Kong; (4) SPL has assets within the jurisdiction i.e., a Hong Kong bank account; and (5) it is believed that Mr Qi is resident in Hong Kong. Regarding the second core requirement, there is clear evidence that there is a reasonable possibility of a benefit to the liquidator. Based on the above facts, aside from the potential assets in the PRC, the only available asset of SPL is the bank account in Hong Kong. Finally, to satisfy the third core requirement, it must be shown that there is a person with a sufficient connection who has a substantial financial interest in the winding up. Here, Mr Qi, who is believed to be resident in Hong Kong, has that connection as well as a substantial financial interest, being the repayment of his shareholder loans. Suppose the Hong Kong court did not consider this enough to satisfy the core requirements, for the reasons set out above. In that case, requirements (1) and (2) are so substantial that the court would order the ancillary liquidation of SPL: *See Re China Medical* [2018] HKCA 111.

The sensible approach would be for the BVI office holder to obtain an ancillary liquidation order. However, in either case, the BVI officer holder will want to (1) obtain the production of documents and examine Mr Zhang, Mr Wong, and/or Mr Qi and (2) take steps to exercise power to deal with SPL's Hong Kong bank account.

As regards (1), section 286A of the CWUMPO, after a winding up order has been made upon an application by a liquidator, the court may direct a person (a) who is or has been an officer of the company; (b) a person who has or is a receiver or manager of the property of the company; and/or (c) any person who has taken part in the formation or management of the company: see §268A(2)(a), and (c)-(d), to attend before the court for examination: §286A(1). Section 286B then goes on to provide the court has the power also to order such person to swear an affidavit in relation to the formation or affairs of the company: §286D(1)(c) or to produce any documents or records relating to the dealings of the company: §286B(1)(d).

In respect of the production of documents and/or examination of witnesses, the BVI office holder has the powers set out above under an ancillary liquidation. If, instead, the BVI office holder intends to seek the assistance of the Hong Kong court to examine Mr Zhang and Mr Wong, the scope of the court's power is not unlimited. Accordingly, the powers available to the BVI office holder in Hong Kong will be limited to the powers available to the BVI office holder under BVI law, which, as I understand it is not as expansive as examination/production powers under Hong Kong law¹².

¹² Module at [7].

As regards (2), under an ancillary order, the BVI office holder will have the power to collect assets within the jurisdiction to deal with them in the primary insolvency proceedings. If the BVI office holder seeks to obtain recognition under common law principles, the case of *Re Lumena New Materials Corp (in provisional liquidation)* [2018] HKCFI 276 has confirmed that the court will assist a foreign office holder in dealing with assets within the jurisdiction.

As regards the assets of SPL in Mainland China, it may be possible upon further investigation to utilize the recently enacted pilot program. The procedure under the "Record of Meeting" is limited to the following three regions in the PRC: (i) Shanghai municipality; (ii) Xiamen municipality of the Fujian province; and (iii) the Shenzhen municipality. If SPL's assets are located within the regions as mentioned above and upon the BVI office holder obtaining an order for an ancillary liquidation, he/she may make an application for recognition provided (i) SPL's COMI is located in Hong Kong; (ii) SPL's principal assets or place of business/ representative office is in one of the three regions; (iii) the Hong Kong insolvency procedure is compulsory liquidation initiated by a liquidator or provisional liquidator; and (iv) none of the circumstances exist for the PRC Court to refuse recognition. The difficulty in the present case is that SPL is a BVI-registered company. Thus, unless it can be established that SPL's COMI is in Hong Kong, it is unlikely that the BVI office holder could seek recognition and assistance in the PRC. Moreover, it is unclear from the above facts whether any of SPL's assets are located within the three pilot regions.

*** End of Assessment ***

TOTAL MARKS: 41.5 out of 50

Formatted: Left

(4 marks) A bit confused in parts but overall has the right elements

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].