



**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.**

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

#### Question 1.2

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

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

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

#### Question 1.3

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

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

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

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

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

#### Question 1.4

Select the **correct** answer:

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

- (a) must first be used to satisfy the costs and expenses of the liquidator.
- (b) must first be used to satisfy the whole of all claims by employees but no other claims.
- (c) must first be used to satisfy the claims of preferential creditors as described in the relevant section of CWUMPO.
- (d) will be kept entirely by the receiver for the benefit of the charge holder irrespective of what claims, preferential or otherwise, exist against the company.

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

#### Question 1.5

Select the **correct** answer:

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

- (a) the date on which the creditors pass a resolution to wind up the company.
- (b) the date on which the court approves the appointment of liquidators.
- (c) the date on which the members pass a special resolution to wind up the company.
- (d) the date on which notice of the liquidator's appointment is registered at the Companies Registry.

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

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

#### Question 1.6

Select the **correct** answer:

Hong Kong legislation provides a statutory definition of insolvency in –

- (a) the Companies Ordinance (Cap 622).
- (b) the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32).
- (c) the Companies (Winding Up) Rules (Cap 32H).
- (d) none of above.

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

### Question 1.7

Select the **correct** answer:

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

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

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

### Question 1.8

Select the **correct** answer:

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

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

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

### Question 1.9

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

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

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

### Question 1.10

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

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

(c) No recognition is possible.

(d) None of the above.

## 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?

Pursuant to section 6 of the Bankruptcy Ordinance (Cap 6), an individual must meet the following requirements to be subject to the Hong Kong court's bankruptcy jurisdiction:

1. the individual must be domiciled in Hong Kong;
2. the individual must be personally present in Hong Kong on the date of presentation of the petition; or
3. at any time in the three years ending on the date of presentation of the petition, the individual must have (i) been ordinarily resident, or have had a place of residence in Hong Kong or (ii) carried on business in Hong Kong.

### 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 decision in *Re Yung Kee* (2015) 18 HKCFAR 501, sets out the following three core requirements for winding up a company that is not registered in Hong Kong:

1. The debtor company must have a 'sufficient connection' with Hong Kong. While having assets within the jurisdiction will usually satisfy this requirement, it is not an absolute necessity. The requirement can be satisfied by other connections such as the debtor company carrying on business activities in Hong Kong (*Re China Medical* [2014] 2 HKLRD 997) and, in the case of winding up applications arising from shareholder disputes, by the shareholder having a connection to Hong Kong;
2. There must be a reasonable possibility the winding up order would benefit the petitioner(s). Again, typically this will be satisfied if there are assets in the jurisdiction that can be realized in the liquidation process. Where there are no assets in the jurisdiction, the courts will review the practical benefit that could be obtained – for example, in *Re Solar Touch Ltd* [2004] 3 HKLRD 15, the court held this limb was not satisfied as the petitioner sought the appointment of liquidators to carry out investigations in PRC, but the PRC would not (at that time and in that region) recognize the liquidators appointment; **and**
3. The Hong Kong court must have jurisdiction over at least one person or entity interested in the distribution of the debtor company's assets. A creditor presenting a winding up petition alone will not satisfy this requirement – they must do "something more" to demonstrate that they are subject the court's jurisdiction. This may include having a place of residence, place of business or employment in Hong Kong (see *Re China Medical* [2014] 2 HKLRD 997).

**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.

**Commented [RD(DWH11):** (2.5 marks). Correct criteria but wrong section

**Commented [RD(DWH12):** Section 4, not 6

**Commented [RD(DWH13):** (3 marks)

**Question 2.3 [maximum 4 marks]**

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

The purpose of a provisional liquidator ("PL") being appointed is to preserve and protect assets before a winding up order can be made. They are therefore often appointed in circumstances where there is an immediate risk to the security of assets that would constitute part of the liquidation estate. For example, if there is evidence those controlling the company are seeking to dissipate its assets for their own personal benefit.

Unlike final liquidators, it is not their role to realise assets. However, they may be entitled to do so if that is necessary to preserve their value.

PLs can also be appointed to assist in facilitating a restructuring proposal (such as a scheme of arrangement) but that cannot be the sole reason for their appointment – there must still be a need to preserve assets.

PLs will therefore only be appointed if the following requirements are met:

1. A winding up petition must have been presented (although in urgent cases, it may be possible filed at the application to appoint a PL can be filed at the same time as the petition is presented); and
2. There must be sufficient circumstances to justify the appointment of a PL. These may include the assets of the debtor company being in jeopardy or at risk of dissipation prior to the date a winding up order can be made (see *Re Union Accident Insurance co Ltd* [1972] 1 All ER 1104). In determining whether this requirement has been met, the court will balance various factors including the commercial realities of the situation, the urgency of the risk, the necessity of a PL's appointment and interests of /prejudice to be suffered by each party (i.e. the balance of convenience).

Once appointed, the PL's powers will be derived from the order that appointed them.

**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.

In order to succeed in an unfair preference claim pursuant to CWUMPO s266, 266A and 266B, a liquidator must show:

1. The company entered into a transaction which placed a creditor (or a guarantor) in a better position than it otherwise would been on the company's insolvency.
2. The transaction was entered into during the six months prior to the commencement of the company's winding up, or where the beneficiary of the transaction was a 'person connected to the company', within two years prior to the commencement of the company's winding up. The commencement of the company's winding up will be deemed to begin on the date of presentation of the winding up petition giving to the liquidation.

**Commented [RD(DWH14):** (3.5 marks). Should refer to need to show likely to be wound up when petition is heard

**Commented [RD(DWH15):** (4.5 marks)

3. The company must have been unable to pay its debts as they fell due at the time of the transaction or became unable to pay its debts as they fell due as a result of the transaction. There is a rebuttable presumption that this criterion is met if the transaction is with a 'person connected to the company'.
4. The company must have been 'influenced by a desire' to improve the beneficiaries position in the event it being wound up. The liquidator must show a positive intention to improve the creditor or guarantor's position. This is often hard to evidence, but the courts have on occasion being willing to find a desire to prefer existed where there were no other grounds for the relevant transaction (see *Re MC Bacon* [1990] BCLC 324).

**Commented [RD(DWH16):** Presumption of insolvency applies only to transactions at an undervalue, not unfair preferences (s266B(3))

**Commented [RD(DWH17):** Rebuttable presumption of desire to prefer where beneficiary is a connected person.

As a matter of principle, a liquidator will want to unwind a preference transaction as it runs contrary to the pari passu principle (i.e. that creditors of the same class should share equally in available assets).

Practically, a liquidator will want to take action to obtain further assets and ultimately realisations for the liquidation estate. It will do this by obtaining the relief applicable to preference transactions under section 266 of the CWUMPO, which includes (i) vesting the property subject to the preference in the liquidator, (ii) releasing or discharging security given by the company as a preference, (iii) directly any person to pay the liquidator the benefit received from the preference, (iv) reviving an obligation that was released or discharged in preference, and (v) requiring a person to provide security for any obligation imposed under an order seeking to restore the position to as it was pre-preference.

### 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.

**Commented [RD(DWH18):** (3 marks) Should mention some of the main elements that are needed to use the new mechanism as is not a wholesale provision (e.g. COMI for 6 months in Hong Kong, appointments made in Hong Kong only, need for letter of request)

Could also have referred to the pre-existing tools (e.g. s.327 and common law developments such as CEFC Shanghai)

The first part of this statement is correct: Hong Kong does have limited formal arrangements to deal with cross-border insolvency, having not: (i) adopted the UNCITRAL Model Law, (ii) entered any international treaties that deal with cross-border insolvency and (iii) entered into any bilateral agreements with other countries. It has, however, consistently adopted common law principles of recognition and has traditionally been keen to rely on these principles to assist foreign insolvency representatives.

The second part of the statement does stand correct as regards to PRC: it does have limited formal arrangements to deal with cross-border insolvency. However, this is not because Hong Kong and Mainland are one country. Hong Kong is a 'Special Administrative Region of the PRC', which means it is stated to have a high degree of autonomy in many areas of law and policy. One of these areas in which Hong Kong has autonomy is its legal system. Exercising this autonomy, Hong Kong cooperates a legal system which retains a British common law approach, therefore differing from the PRC legal system considerably.

In May 2021, Hong Kong and certain areas of the Mainland (namely Shanghai Municipality, Xiamen Municipality of Fujian Province and Shenzhen Municipality of Guangdong Province) piloted a new cooperation mechanism between Hong Kong and each respective area in the Mainland. This system sets out a mechanism for office holders in Hong Kong and those areas of the Mainland to obtain recognition and assistance in the other. However, the Mainland and Hong Kong are one country, this cannot be said to be a cross-border



arrangement, but rather a specific arrangement to deal with the autonomy Hong Kong exercises over its insolvency regime.

**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 is a statutory mechanism contained in Part 13, Division 2 of the Companies Ordinance which allows companies to enter into a court sanctioned binding agreement which compromises or makes other arrangements with each of their creditors and/or members collectively.

The arrangement may include terms adjusting or compromising the debts owed to creditors or reducing the level of share capital for each members.

Schemes of arrangement are subject to the sanction of the court. At a high level, the process for obtaining approval of a scheme is therefore (i) the court grants sanction to convene a scheme meeting (i.e. a meeting of relevant creditors and members) and gives relevant directions, (ii) the scheme meeting is held and at least 75% of voting creditors (with the percentage assessed by value of their claims) must approve it and (iii) the court must sanction the scheme.

Provided the threshold for votes is met and the scheme is sanctioned by the court, non-consenting creditors will still be bound by the terms of the scheme.

The pros of schemes of arrangements are:

1. Schemes are flexible and can be on bespoke terms to address the specific distress facing a debtor company – for example, they can include negotiating entirely new financial instruments.
2. Negotiating with creditors collectively and having a binding arrangement at the end of the process creates certainty for the company that will be vital if it is to navigate its way out of financial distress.
3. The threshold of 75% prevents minority creditors / shareholders exerting excess leverage over a company in distress and means feasible restructuring plans can be implemented without their consent.
4. Despite the above, the need for court sanction means there is a safeguard to ensure that classes of creditors are treated fairly and equitably.

The cons of schemes of arrangements are:

1. They are very costly and therefore have limited use for to small-medium sized enterprises.
2. Schemes only bind creditors if the relevant debt is governed by Hong Kong law or if the creditor agrees to participate in the scheme. For cross-border insolvencies, there may therefore be a need to get the scheme recognized (or implemented a fresh) in other jurisdictions. Again, this increases costs.

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

**Question 4.1 [maximum 4 marks]**

**Commented [RD(DWH19)]:** (3 marks) A clear and concise answer but the majorities needed are wrongly stated. Should also mention that a main disadvantage is no 'built-in' moratorium whilst the restructuring progresses  
Also, as classes are important, should state that scheme governed by classes and outline requirements (similarity of legal rights, not interests)

**Commented [RD(DWH20)]:** Need majority in number representing 75% in value. (So one (or a few) big creditor(s) cannot pass the vote alone)

**Commented [RD(DWH21)]:** (2.5 marks) Good answer but should also address possibility of MVL. More importantly:

Should also advise that if company is insolvent owes duties to creditors ahead of the company  
should also advise Mr. Chan that Liquidators should be neutral and carry out their duties (including investigation of how the company has been run/conduct of directors) irrespective of who appoints/nominates them

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.

This answer assumes that Mountainview Limited (the *Company*) is insolvent on either a cash flow or balance sheet basis.

As an alternative to winding up the company, Mr Chan could seek advice as to whether the company’s circumstances could be addressed by a scheme of arrangement. This is method, if successful, will allow the Company to continue trading but requires sufficient support from the Company’s creditors to proceed. It is also an expensive process. It’s appropriateness will therefore be dependent on many factors, including (i) the Company’s level of debt, (ii) it’s ongoing business prospects and (iii) re-financing options and (iv) creditor engagement.

If a scheme of arrangement cannot be pursued and Mr Chan considers the Company ought to enter liquidation, he can instigate the process for commencing a creditors’ voluntary liquidation (*CVL*). CVL is an insolvent liquidation. It is instigated by the Company’s directors convening a shareholders meeting whereby the members will be invited to pass a special resolution (requiring 75% votes) to wind the company up and to appoint a specific liquidator. This means Mr Chan would be able to recommend an initial liquidator, albeit the choice of liquidator will ultimately be a matter, at that stage, for the shareholders. If passed, the CVL will commence on the date of the resolution. The initial liquidator appointed will have limited powers, one of which will be to convene a meeting of creditors within 14 days of the shareholders meeting. At this meeting the creditors will then nominate a liquidator. This is a quicker and more cost efficient option than proceeding with an application to court to wind up the Company.

Mr Chan may also be able to instigate an emergency CVL pursuant to s.228A CWUMP. This allows him, as sole director, to pass a resolution immediately placing the Company into CVL without requiring the approval of shareholders. To do so, he will need to certify that (i) the Company cannot by reason of its liabilities continue its business, (ii) the Company needs to be wound up and that it is not just and reasonable for it to be wound up under any other section of the CWUMPO; and (iii) a meeting of creditors will be convened in 28 days. Considering limb (ii), this process should be used cautiously by directors as there are penalties for commencing an emergency CVL when it is inappropriate to do so. Again, under this process Mr Chan would have the initial choice of liquidator, but they would have limited powers and could be replaced by the creditors at the first meeting of creditors.

Finally, if for some reason Mr Chan considers a court ordered liquidation is preferable, he can call a shareholders’ meeting and invite the shareholders to pass a special resolution to cause the Company to petition for its own winding up. Mr Chan cannot instigate this process unilaterally in his capacity as director. In this scenario, the Official Receiver will be immediately appointed on the making of a winding up order. Depending on the value of the liquidation, the Official Receiver will then either outsource the liquidation or, if over HKD 200,000, convene a creditors meeting whereby a resolution will be passed to appoint a liquidator.

**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.

If the receiver has been validly appointed in respect of the receivables pursuant to an unimpeachable charge, the liquidator will not have any entitlement to the proceeds of the receivables as these will be ringfenced for GFL pursuant to the terms of its charge. However, here there are multiple ways for the liquidators to challenge the purported charge created over the Kite's receivables, all of which would undermine the receivership and leave the liquidator in control of the receivables and/or their proceeds:

1. The purported charge in favour of GFL was stated to be a fixed charge. However, in order to create a valid fixed charge, the charger must exercise control over the charged assets (see *Re Spectrum Plus Limited* [2005] 2 AC 680). Here, Kite continued to operate the account into that received the receivables without intervention GFL. GFL therefore did not have control and as such, did not create a fixed charge. (Note, there is insufficient information in the question to determine whether grounds for crystallisation of the floating charge arose and whether GFL exercise their right to do so prior to appointing a receiver. If crystallization had not occurred, the receiver would not have been properly appointed under the terms of a fixed charge and therefore would not have the power to control the receivables. This remainder of this answer will assume the floating charge was not crystallised.)
2. Provided the charge instrument was otherwise validly executed and properly registered at the Companies Registry in accordance with section 334, the charge may still be valid as against the liquidator as a floating charge. In which case, subject to paragraph 3 below, the liquidator would be entitled to the receivables and/or their proceeds in order to ensure that prior ranking expenses and claims (e.g. preferential creditor claims) prior to a distribution being made to GFL under its floating charge.

**Commented [RD(DWH22)]:** (3.5 marks) Broadly correct, but also need to consider why likely a floating charge (Spectrum); perhaps unfair preference;

**Commented [RD(DWH23)]:** Good point

**Commented [RD(DWH24)]:** Yes, but would ordinarily be the other way round: receiver would collect and then remit to L an amount sufficient to pay prefs

3. However, the floating charge is likely to be wholly invalid pursuant to section 267 of CWUMPO because:

Commented [RD(DWH25)]: Bit strong

- a. The charge appears to have been created within the period 12 months prior to commencement of the Kite's liquidation (measured from the date of presentation of the relevant petition). As it falls within this 12-month period, there is no need to consider whether GFL is connected to Kite.
- b. It was created at a time when Kite was in financial distress and therefore appears to have been unable to pay its debts as they fall due.
- c. No 'new money' or credit was advanced to the Kite in consideration for it purporting to grant the charge over its assets. Had 'new money' been advanced, the charge would have been valid to the value of that amount.

Accordingly, the liquidator should seek a declaration that the security granted in favour of GFL and, consequently, the appointment of receivers invalid so that she may deal with the receivables as an unsecured asset of Kite in the liquidation.

#### Question 4.3 [maximum 6 marks]

Commented [RD(DWH26)]: (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;
- (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.

Taking each of the issues presented to the BVI liquidator in turn:

**(A) Standing of Mr Xu**

The clause of the FA cited at (a) is governed by Hong Kong law and constitutes an agreement between Mr Xu and Mr Qi. It is unclear whether SPL is also a party to the FA.

If SPL is in fact a party, the clause cited at (a) will fall foul of the anti-deprivation principle as it is a clause designed to give one party (Mr Qi) an advantage in the event of another (SPL's) insolvency. Given the wide ranging comments of the Court of Appeal in *Peregrine Investments Holdings Ltd v Asian Infrastructures Fund Management Co Ltd* [2004] 1 HLRD 598) it is arguable that, even if SPL is not a party to the FA, the anti-deprivation principle will still render the agreement void as it is clearly intended to constitute a “fraud on insolvency laws’ which create gives one party and advantage at the expense of others.

Notwithstanding the above, as the winding order has already been made by the court and presumably the contractual terms of Mr Xu’s petitioning debt litigated and ruled upon, the liquidator need not be concerned about Mr Xu’s standing. It would be for Mr Qi to successfully appeal to the winding up order.

**(B) Information gathering from Mr Zhang and/or Mr Wong**

Mr Zhang and Mr Wong are likely to have information relating to the assets and affairs of SPL. It will be beneficial for the liquidator to obtain this information. Considering their continued non-cooperation, the liquidator should consider seeking a recognition order in Hong Kong with a view to then seeking an order for the production of documents and/ examination from the Hong Kong court (noting Mr Zhang and/or Mr Wong will be subject to that court’s jurisdiction).

To do so, the liquidator will need to make an application to the BVI court seeking that it issue a letter of request to the Hong Kong court requesting that it assist the liquidator. The Hong Kong court will then carefully consider the request from the BVI court. The Hong Kong court will only grant recognition and assistance to the extent that an equivalent type of relief would be available from the Hong Kong court.

If recognition is granted, the liquidator will then only be entitled to seek such assistance from the Hong Kong court as he would be entitled to under both Hong Kong and BVI law. If BVI insolvency law has more restrictive provisions in respect of a liquidator’s power to obtain information and examine relevant parties, the liquidator may prefer to consider whether it is preferable to seek a new winding up order against SFL in Hong Kong as an unregistered company pursuant to the Part X of CWUMPO.

Assuming, however, BVI legislation contains similar investigative powers, once recognized the liquidator can make an application to the Hong Kong court to compel Mr Zhang and Mr

Wong to produce relevant documents (see, for example, BJB Career Education Co Ltd [10§7] 1 HKLRD and *Re Centaur Litigation SPC* (Unreported, HCMP 3389/2015).

#### (C) Bank Account in Hong Kong

The liquidator should not need to obtain recognition of the Hong Kong court to obtain information in respect of SPL's Hong Kong bank accounts as, pursuant to *Bay Capital Asia Fund LP (in Liquidation) v DBS Bank (Hong Kong)* Unreported, HCMP 3104/2015, 2 November 2016, banks in Hong Kong should readily assist foreign representatives by providing documents without them having to first seek recognition.

However, to take control of the bank account and the assets contained therein, the liquidator will need to seek recognition. The liquidator could make an application for a recognition order for this specific purpose (*Re China Lumena New Materials Corp (in Provisional Liquidation)* [2018] HKCFI 276), which would be shorter and cheaper than a full recognition application (referred to above).

#### (D) Claims against Mr Xi

As it appears there could be potential claims against Mr Xi, either held by SPL or the liquidator, Mr Xi's residence will be relevant to determining where claims should be brought against him and where service should be effected.

The impact this will have on the liquidator will depend on the nature of the claims identified.

The Hong Kong court has long recognized a foreign liquidators ability to bring proceeding in the name of the company of which they are appointed without obtaining recognition. Therefore, if the liquidator wishes to cause SPL to pursue a claim against Mr Xi (e.g. a breach of fiduciary duty claim), he could do so without seeking recognition.

If the liquidator wishes to bring a claim in Hong Kong pursuant to powers under the Hong Kong insolvency regime (e.g. a fraudulent trading claim) he will first need to obtain recognition of his appointment in Hong Kong through the method set out above.

#### (E) Assets in the Mainland

The BVI liquidator will only be able to obtain recognition of his appointment (pursuant to the BVI court order) in PRC if reciprocity exists.

There is no automatic recognition or cooperation framework system in place between the Mainland (as a whole) and Hong Kong. However, certain areas of the Mainland (namely Shanghai Municipality, Xiamen Municipality of Fujian Province and Shenzhen Municipality of Guangdong Province) are piloting a new cooperation mechanism between Hong Kong and each respective area in the Mainland. That pilot provides a framework for Hong Kong liquidators to have their appointment recognized and seek assistance from the PRC Courts in those areas.

If the BVI liquidator has his appointment recognized in Hong Kong or is appointed as liquidator in an ancillary liquidation in Hong Kong, he may be able to rely on the pilot as providing a mechanism for the liquidator obtaining recognition and assistance from the PRC court's in the relevant areas. To do so:

1. SPL's centre of main interest must be in Hong Kong. We do not have sufficient information to determine if that is the case.

Commented [RD(DWH27)]: Qi?

Commented [RD(DWH28)]: Query whether recognition is enough. I would say no.

2. SPL must have assets in one of the areas included in the pilot, or a representative office in that area.
3. The Hong Kong court must issue a letter of request to the relevant court in the relevant area.

**\* End of Assessment \***

**TOTAL MARKS: 41.5 out of 50**

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