INSOL INTERNATIONAL
FOUNDATION CERTIFICATE
IN INTERNATIONAL INSOLVENCY LAW

SUMMATIVE (FORMAL) ASSESSMENT: MODULE 8C

HONG KONG

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

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

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

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

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.

2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way**. **DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.

3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).

4. You must save this document using the following format: **[studentID.assessment8C]**. An example would be something along the following lines: 202122-336.assessment8C. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words "studentID" with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked**.

5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6. The final submission date for this assessment is **31 July 2022**. The assessment submission portal will close at **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.

7. Prior to being populated with your answers, this assessment consists of **8 pages**.

ANSWER ALL THE QUESTIONS

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

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

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

Question 1.1

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

A receiver can be appointed –

(a) only pursuant to a charge over shares.

(b) only by the court.

(c) only pursuant to a legal mortgage over land.

(d) any of the above.

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

Question 1.2

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

(a) It depends on whether the person with whom the bankrupt transacted is an associate of his or not.

(b) Two (2) years before the date of the bankruptcy order.

(c) Five (5) years before the date of the petition on which the bankruptcy order was made.

(d) Five (5) years before the date of the bankruptcy order.

Commented [RD(DWH2]: Incorrect (0 marks) - 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 (see 6.2.2 of text) and s.51(1)(a) Bankruptcy Ordinance

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.

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.

(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.

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.

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.

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

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]: Incorrect (0 marks) – see rule 84 CWUR and section 5.5 of text: can vote but only for unsecured portion of its debt

Question 1.9

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

(a) A 1995 decision of the English House of Lords is binding.

(b) A 1993 decision of the UK Privy Council on an appeal from Hong Kong is binding.

(c) A 1996 decision of the UK Privy Council on an appeal from the Cayman Islands is binding.

(d) None of the above because they all pre-date the Handover in 1997.

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

Question 1.10

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

(a) He must make an application to the High Court of Hong Kong using the provisions of the UNCITRAL Model Law.

(b) He must first seek permission from the Ministry of Justice in Beijing.

(c) No recognition is possible.

(d) None of the above.

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

QUESTION 2 (direct questions) [10 marks]

Question 2.1 [maximum 3 marks]

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

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 jurisdictional requirements are that the debtor must be:

(a) An individual
(b) Be domiciled in Hong Kong
(c) Be personally present in Hong Kong on the day on which the petition is presented or
(d) At the time in the period of 3 years ending at that day (i) have been ordinarily resident or have had place of resident in Hong Kong or (ii) have carried on business in Hong Kong.

Question 2.2 [maximum 3 marks]

Commented [RD(DWH12]: (3 marks). Would have been preferable to include source (CFA's decision in Yung Kee)

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

There are 3 core requirements:

(a) A sufficient connection with Hong Kong. This is not necessarily the presence of assets within the jurisdiction;
(b) A reasonable possibility that the winding up order would benefit the applicant; and
(c) The court would be able to exercise its jurisdiction over one or more persons interested in the distribution of the company's assets.

The jurisdiction to wind up a non- Hong Kong will remain even after the matters giving rise to the original connection cease to exist.

Question 2.3 [maximum 4 marks]

Commented [RD(DWH13]: (2.5 marks). See note below, plus would be better to mention need for urgency, and that powers are as prescribed by the court. Should also mention the Legend Resorts 'restriction' that PL cannot be appointed solely for restructuring

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

In technical terms, a 'provisional liquidation' does not exist in Hong Kong law. However, the term 'provisional liquidation' is used where provisional liquidators have been appointed under section 193 of the CWUMPO.

A provisional liquidator would be appointed in circumstances where there is a need to preserve assets during the period between the presentation of the petition and the making of a winding up order. There is generally no requirement for the provisional liquidator to realise those assets, unless it is necessary to preserve their value.

The application to appoint a provisional liquidator can be made any time after the petition has been presented. In some cases, depending on the urgency, it may be made at the same time as the presentation pf the petition. The court will not appoint a private provisional

liquidator even if the application is made immediately prior to winding up. The court may, however, appoint provisional liquidators despite the appointment of any voluntary liquidator.

Commented [RD(DWH14]: This confuses another issue - namely that the court will not (usually) allow a petitioner to apply to appoint a PL 'at the last minute' just before a winding up order is made in order to avoid the statutory mechanism of the Official Receiver being appointed and a creditors' meeting being called

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

Question 3.1 [maximum 5 marks]

Commented [RD(DWH15]: (3.5 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.

I believe a liquidator will be able to challenge a transaction that is unfairly preferential on the basis that the person receiving the benefit took advantage of the company while it was in or near insolvent. A person connected to the company would be able to have information as to the company's woes and could have used that to his/her advantage. It is fair for the liquidator to seek to unwind those transactions.

Commented [RD(DWH16]: Correct but not quite the right way round. The recipient of the preference may well not know - it is the company desiring to prefer IT

A liquidator of a company can make an application to set aside unfairly preferential transactions in voluntary or compulsory winding ups. This includes transactions that occur when the insolvent company acts to place a creditor or guarantor in a better position than it would have been upon the company's insolvency. The liquidator may take such an action in relation transactions entered during the 6 months prior to the commencement of winding up or 2 years where the beneficiary under the unfair transaction was a person connected to the company. These transactions include where there was for example a granting of a security as well as payment during that period.

The liquidator will need to show that

(i) At the time the asserted unfair preference was given/ entered into, the insolvent company was unable to pay its debts or became unable to pay its debts as a result of same. This requirement will be presumed where a person connected with the company is on the other side of the transaction – that is, an associate of a director or shadow director of the company;

Commented [RD(DWH17]: Presumption of insolvency applies only to transactions at an undervalue, not unfair preferences (s266B(3))

(j) The company was influenced by a desire to improve that person's position in the event of the company going into liquidation. This is difficult to prove, and the transaction will not be set aside unless the company positively wished to improve the creditor's positon in the event of its own insolvent liquidation and the person does not desire all the necessary consequences of his actions.

Commented [RD(DWH18]: Rebuttable presumption of desire to prefer where beneficiary is a connected person.

Question 3.2 [maximum 5 marks]

Commented [RD(DWH19]: (4 marks) Could also have referred to the pre-existing tools (e.g. s.327 and common law developments such as CEFC Shanghai)

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.

Although Hong Kong is a part of the PRC, it retains a level of autonomy as a Special Administrative Region of the PRC. Laws in force as at 30 June 1997 continued to apply in Hong Kong after the Handover from the UK to the PRC. Therefore, although it is one country, different rules may apply in some areas of the law.

Hong Kong has no formal requirements for cross-border insolvency, save for provisions for winding up of non-Hog Kong companies. In May 2021, however, Hong Kong and certain areas of the Mainland entered into a new arrangement, which provide mechanisms for Hong

Kong insolvency officeholders to obtain recognition and assistance in certain areas in Mainland, and for insolvency office holders in the Mainland to obtain recognition and assistance in Hong Kong.

The new arrangement originated from a meeting between representatives of the Supreme Court in the Mainland and the Hong Kong government. At the meeting, both sides sought to further the objective of Article 95 of the Basic Law through the mutual recognition of and assistance to bankruptcy proceedings between Hong Kong and the Mainland. The record of the meeting indicates that there was an agreement to allow Hong Kong appointed liquidators and provisional liquidators to apply for recognition in Mainland and for administrators appointed in Mainland to apply for recognition in Hong Kong.

In a subsequent opinion from the Supreme Court, it was made clear that

(i) the applicable Mainland designated areas under the agreement were Shanghai Municipality, Xiamen Municipality of Fujian Province and Shenzhen Municipality of Guangdong Province (the ***pilot area***)
(j) the definition of what would constitute a Hong Kong insolvency proceeding would be any collective insolvency proceeding commenced under the CWMPO or the CO and would include compulsory liquidations, creditors' voluntary liquidations and schemes of arrangements which are promoted by the provisional liquidator/liquidator;
(k) the applicable COMI for the purposes of recognition would be Hong Kong. The place of incorporation is presumptive of this, but the court will consider other factors such as whether Hong Kong was the principal office, the principal place of business or the place of principal assets of the debit. Additionally, the COMI should have been in Hong Kong for at least 6 months prior to the application for recognition.
(l) Where the debtor's principal assets are in the pilot area of the Mainland, then the Hong Kong administrator could apply for recognition / assistance in Mainland. A letter of request from the Hong Kong court would not be necessary.

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 scheme provided for by Part 13, Division 2 of the Companies Ordinance and O.102 r 2 and r 5 of the RHC by which the insolvent company enters a binding compromise / arrangement with the members and creditors. It includes plans for an adjustment of debts owed to the creditor and reduction of share capital. The arrangement will need to be approved by a stipulated majority of the creditors (75% by value of the creditors present and voting in proxy or in person) and sanctioned by the court.

The benefits of a scheme of arrangement includes:

1. It is a court sanctioned arrangement which binds all creditors of the relevant class;

2. It can be used to cancel existing instruments and replace them with new instruments

3. it enables the company and the creditors to adjust debts in circumstances where there are many creditors, divergent views and a difficulty in obtaining 100% agreement on contractually varying the debt of the company. Without a scheme of arrangement the company would need to get the 100% of creditors (as opposed to a stipulated majority) to contractually vary the debt. The scheme would therefore have

Commented [RD(DWH20]: (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(DWH21]: Need majority in number representing 75% in value. (So one (or a few) big creditor(s) cannot pass the vote alone)

much utility where there ''are hold-out creditors seeking an unfair advantage against a substantial majority of similarly ranked creditors.''

4. Additionally, the scheme will be binding on non-consenting / hold-out creditors so long as they are in the category of creditors where the stipulated majority of the creditors have approved the scheme.

5. The scheme of arrangement is also a good alternative to winding up the company. It would allow the company the possibility of continuing to trade following implementation of the scheme.

6. Another benefit is that the scheme may be recognized in other relevant jurisdictions, including in Mainland PRC.

Commented [RD(DWH22]: Recognition is not automatic; although you are right to say that a scheme (if promulgated by a liquidator) falls within the new mutual recognition mechanism between Hong Kong and the Mainland (but only pilot areas remember)

The cons are:

1. A scheme of arrangement implemented and sanctioned in Hong Kong, in accordance with the Gibbs principle does not have the effect of discharging a debt which is governed by a foreign law (unless the relevant creditor takes part in the scheme)

2. The creditors must be in the same class or the court will have no jurisdiction to sanction the scheme

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

Question 4.1 [maximum 4 marks]

Commented [RD(DWH23]: (0.5 mark) some marks for thinking of scheme, but rest a bid jumbled and shows misunderstanding. IVA is for individuals only.

Answer should discuss voluntary liquidation

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

Mr Chan should be advised that since the company is unlikely to be able to carry out business he should consider the options available under Hong Kong law for the structured dissolution of the company, corporate rescue and reorganization of debts. Mr Chan has a fiduciary duty to the company and must consider these options in acting in the best interest of the company.

Commented [RD(DWH24]: Creditors when insolvent

His friend is correct that the company may be wound up. However, that is not the only option. The company may present a winding up petition followed by an appointment of provisional liquidators to promulgate a restricting, which is generally by using a scheme of arrangement. The option of appointing provisional liquidators for the purpose of assisting with restructuring continues in Hong Kong to some extent, despite the decision in Re Legend International Resorts Ltd.

Commented [RD(DWH25]: The friend says "must"

Hong Kong law provides for the option of a scheme of arrangement which a statutory scheme by which the company enters a binding compromise / arrangement with the members and creditors. If the plan were to be agreed, it would enable the company and the creditors to adjust debts, which could rescue the company.

Contrary to what the friend said, the provisional liquidator will need to investigate the affairs of the company closely if there is to be any good restructuring plan.

Save for schemes of arrangement, there is no legislation in Hong Kong that specifically deals with corporate rescue as an alternative to winding up. There are however informal 'work-out's that are quite common in Hong Kong, for example the practice among banks to re-schedule debts through the London Approach. Mr Chan may also consider the guidelines set out in the Hong Kong approach to Corporate Difficulties, which sets out formal but non-statutory recommendations to restructuring.

The company may also make an application for an individual voluntary arrangement (***IVA***) on the basis that the company (as debtor) has problems with debt repayment. The first step in applying for an IVA is that Mountainview will need to must find a Nomine, as oppose to a liquidator. Mountainview must prepare a proposal for the Nominee setting out how the company intends to repay its creditors. Mountainview would also need to submit an up to date Statement of affairs to the Nominee. The company would then make an application for an Interim Order implementing the IVA. The Nominee would then file a report stating whether in his opinion a meeting of the creditors must be fixed to consider the IVA. This means that he must carry out some investigations in relation to the company's affairs. A creditors' meeting would thereafter be held to decide whether or not to approve the IVA. The IVA would have to be approved by a majority in excess of 75% by value of the creditors present and voting (in person or proxy). The chairman would then report to the court and the Official Receiver the details of the IVA.

Commented [RD(DWH26]: Applies only to individuals

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.

HK law recognises a security arrangement like the one entered into by Kite and GFL whereby the financier (GFL) buys the right to be paid receivables from the business of the company (from the sales in Europe etc). The security is expressed to be a fixed charge. Fixed charges will attach at the date of its creation (date unknown in this case), and GFL

Commented [RD(DWH27]: (2 marks) Good mention of the possibility of unfair preference, but thrust should be to consider nature of charge. Is it a floating charge instead? (Noting error below when dealing with it as if it is a fixed charge)

An outline is

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

Commented [RD(DWH28]: It is not stated to be a receivables purchase - not really relevant here

would be considered a secured creditor. The enforcement of fixed charges stands wholly outside the liquidation.

The security agreement also permitted GFL to appoint the receiver, which is also permitted under Hong Kong law. Generally, the subsequent appointment of a liquidator will not affect the receiver's right to hold and/sell the property or asset that was the subject of the charge (the receivables). Any realisations made by the receiver out of those assets are generally not available to the liquidator for payment of liquidation expenses. The assets, must however, be used to meet the claims of preferential creditors, provided there is insufficient assets to meet those claims from the uncharged assets available to the liquidator (in this case, the only asset is the receivables).

Commented [RD(DWH29]: Only floating charge

However, the security agreement / fixed charge may be voidable against a liquidator if it was an unfair preferential transaction entered within a certain time before the commencement of liquidation (except as to new money lent). An unfair preference occurs where Kite acted so as to place GFL in a better position than it would have been upon Kite being put in liquidation. The transaction must have been entered into during the 6 months prior to commencement of winding up or 2 years where the beneficiary under the transaction was a person connected to Kite. In this case, there was nothing to suggest GFL was connected to Kite so the relevant period is 6 months prior to liquidation.

It is unclear when liquidation commenced and when Kite and GFL entered into the agreement, but provided that the agreement was entered within the 6 months period, the liquidator may void the agreement. The liquidator must show that:

a. At the time of the transaction the company was unable to pay its debt / became unable to pay its debt due to the transaction concerned. Here, there is no dispute that Kite had difficulty paying its debts
b. The company was influenced by a desire to improve GFL's position in the event of a liquidation. It has been held that where a company gives a financer a charge over an asset and there is no good grounds for doing so save that the company was under the threat of insolvency, then the security agreement is liable to be set aside on the grounds that it was an unfair preference (Re Sweetmark v Garment Works). This is especially so if no new money was given in exchange for the charge. Here, GFL instated on the fixed charge and there is nothing suggesting that it gave Kite more funds. There is therefore evidence that the company positively wished to improve GFL's position in the event of its own insolvent liquidation.

The liquidator may therefore seek an order setting aside the fixed charge on the basis that it was an unfair preference and seek orders pursuant to section 266 of the CWUMPO:

(a) Vesting the liquidator with the property subject to the unfair preference (the receivables);
(b) Releasing or discharging the security (fixed charge) given by Kite to GFL;
(c) Directing GFL to pay to the liquidators any benefit received from the company (including any realisations);

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;

(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.

Based on Hong Kong common law, the BVI liquidator has a right to bring an action in Hong Kong to recognize the BVI insolvency of SPL. The Hong Kong court will assist the BVI liquidator as a foreign representative by relying on common law principles.

The Hong Kong court may also grant ancillary winding up orders in Hong Kong, which will provide the liquidator with powers exercisable under CWUMPO and CWUR.

Commented [RD(DWH30]: (4 marks)

Outline of elements should be included is as follows (not all would be needed for full marks):
Question asks that advice be given to L; answer should be written accordingly
The FA clause that all provisions (including repayment to Xu) are void if SPL insolvent is almost certainly void due to the anti-deprivation principle
Whether L is properly appointed would be a matter for BVI law
L will be able to take certain steps in Hong Kong without a formal recognition order
Obtain documents from the company's bank (Bay Capital)
Bring an action against Mr. Qi (perhaps for breach of fiduciary duty) (Irish Shipping – but see recent decision of Nuoxi Capital which creates some uncertainty)
IF can find him; also query if has assets (litigation worthwhile?). Need to investigate
L should obtain a recognition order to take other steps that 'belong' to an office-holder as opposed to the company itself (e.g. examination of individuals):
The Hong Kong court is receptive to such applications from legal systems similar to Hong Kong (BVI is one)
The Hong Kong court will need the originating court (BVI) to make a letter of request
The powers that the liquidator can then exercise in Hong Kong must be powers that he has as a liquidator in the home (i.e. BVI) jurisdiction and that he would have if appointed as a liquidator here in Hong Kong (the Singularis principle)
Note that although the jurisdiction to examine in Hong Kong's legislation is a broad one (s.286B), some jurisdictions restrict the power to examine to officers or closely related parties, so this should be checked carefully, certainly as regards Mr. Wong (no suggestion he is an officer). Need to check with BVI lawyers. [nb, some development in more recent cases re basis on which examination powers are exercised]
Re **possible assets in the Mainland** and the new "co-operation mechanism":
- 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
- 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).
- 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.
- 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].

(a) The FA clause in the FA

The FA is governed by Hong Kong law. Therefore the liquidator may seek certain declarations from the court in respect of the FA's clauses.

Generally, in Hong Kong a contractual clause that provides for the determination or modification of the contract upon the insolvency of the counter party will be upheld, though there are limits to this. For example, and in accordance with the 'anti-deprivation principle', the Hong Kong court will not uphold a term in the agreement which results in general creditors being deprived of an asset that would, in the absence of such a clause, be used to satisfy their debts.

Here, Mr Xu is a general creditor of SPL. There was no security agreement between him and SPL in respect of the investment. He is therefore entitled to the benefit of the 'anti-deprivation principle'.

The clause in the FA puts shareholder who provided loans to Mr Qi in a better position than Mr Xu. Those shareholders are also presumed to be general creditors. Therefore the clause in the FA breaches the anti-deprivation rule. The BVI liquidators may seek the Hong Court declaration to that effect.

(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**;

In the recent cases of *Re BJB Career Education Co Ltd* and *Re Centaur Litigation SPC*, it was held that the Hong Kong court may grant recognition orders to permit a foreign office holder (here, the BVI liquidator) to seek the production of documents and the examination of individuals in Hong Kong.

In this respect, the BVI liquidator may seek orders for Mr Wong to produce the books of SPL and for examination of both Mr Zhang and Mr Wong. These are Hong Kong based persons with information relevant to the BVI liquidation. The powers of document production and examination exists in both BVI and Hong Kong so the Singularis principle would be satisfied.

(c) SPL has a bank account at a bank in Hong Kong;

The BVI liquidator will need to apply for a specific order to deal with any assets in Hong Kong (*Re China Lumena New Materials Corp*). This is because, the court will need to balance the BVI liquidator;s need for convenience of access to the assets with the need for court supervision which creditors may expect.

The Hong Kong bank account /funds therein are assets of SPL. The BVI liquidator must therefore specifically request an order in respect of dealing with the account 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.**

Recognition in Hong Kong would not equate recognition in the PRC Mainland. The new co-operation mechanism established in May 2021 between Hong Kong and certain areas of the Mainland entered into a new arrangement, provide mechanisms for Hong Kong insolvency officeholders to obtain recognition and assistance in certain areas in Mainland.

The mechanism only applies to Shanghai Municipality, Xiamen Municipality of Fujian Province and Shenzhen Municipality of Guangdong Province (the ***pilot area***).

Additionally, it only applies to a Hong Kong collective insolvency proceeding commenced under the CWMPO or the Company Ordinance and would include compulsory liquidations, creditors' voluntary liquidations and schemes of arrangements which are promoted by the provisional liquidator/liquidator.

Since the proceedings here were commenced under the common law, there is an argument to be made that the new mechanism does not apply.

Commented [RD(DWH31]: Ancillary liquidation

Additionally SPL's COMI must be Hong Kong. Since SPL was incorporated in the BVI then BVI is presumed the COMI. However, the court may be persuaded by evidence of the location of the company's principal place of business or principal place of assets that the COMI is Hong. There is evidence of assets in Hong Kong and so that might assist with determining the COMI.

There would also need to be evidence that SPL's principal assets are in the pilot area of the Mainland. The liquidator would have to make the necessary checks.

*** End of Assessment ***

TOTAL MARKS: 33 out of 50

Formatted: Left