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ARTICLE

An Era of Cooperation: Notable Judicial Assistance by the Hong Kong Courts in Recent Cross-Border Insolvency and Restructuring Cases

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Synopsis

Hong Kong is one of the leading capital markets in the world. Billions of dollars are raised on a day to day basis, from all parts of the world, through a wide range of capital and financing activities, particularly Initial Public Offerings ('IPOs'). The Cayman Islands is a popular jurisdiction for setting up listing vehicles in Hong Kong IPOs as it offers corporate flexibility, a well-established English law based legal system and tax neutrality. Of all the listed companies in Hong Kong, slightly more than half of them are incorporated in the Cayman Islands.

It is imperative that an effective cross-border insolvency and restructuring regime is in place to accommodate potential complex insolvency and restructuring scenarios involving these valuable public companies. However, one significant hurdle is that Hong Kong has been slow in introducing comprehensive legislation for the purposes of corporate rescue and restructuring. It is hoped that such legislation will be on its way. For now, the burden falls on the judiciary and the legal practitioners to develop innovative and practical solutions within the existing legal framework.

This article discusses some recent cases in Hong Kong which demonstrates how the Hong Kong Companies Court has successfully formulated innovative and practical judicial solutions to complex cross-border insolvency and restructuring issues.

Recent approach of the Hong Kong Court on cross-border restructuring

The general approach of the Hong Kong Companies Judge, The Honourable Mr. Justice Harris, can be helpfully summarised in his own words during an interview by The Hong Kong Lawyer in May 2017. In reflecting his current role at the bench he said:

> 'one of the things that I appreciate the longer I do this job is that what I find most satisfying is solving problems. Advocacy doesn't involve solving problems – rather you are taking part in an intellectual competition. Whilst that was stimulating when I was younger, as I have gotten older, I have become more interested in identifying efficient and effective ways to solve the types of commercial problems companies' activities give rise to and corporate insolvency, in particular. The corporate insolvency and restructuring field is about helping parties solve practical commercial issues.'

His Lordship's pragmatic and effective approach is reflected in his landmark decisions handed down in recent years after he was appointed to the Hong Kong Companies Court. The common themes of these decisions are: (i) upholding the strong presumption at common law in favour of the place of incorporation being the appropriate jurisdiction for presenting winding up petition; and (ii) recognising and assisting foreign liquidators (appointed by the courts of the place of incorporation of the company) as long as it is within the court's powers, so as to ensure proper discharge of their duties and/or overcome the limitations of the Hong Kong law as regards corporate restructuring/rescue.

By way of background, in *Re Legend Int'l Resorts Ltd* [2006] 2 HKLRD 192, the Hong Kong Court of Appeal held that the statutory power to appoint provisional liquidators under the relevant legislation in Hong Kong to restructure a company's debt was not permissible. This is to be contrasted with the position in the Cayman Islands (and also Bermuda), where provisional liquidation can be used expressly for restructuring (so called a 'soft touch provisional liquidation'). The Hong Kong common law position post *Re Legend* was unhelpful to corporate restructuring/rescue given the absence of statutory tools to create a moratorium preventing creditors taking enforcement action of their own.

The Hong Kong court's decision in *Re Z-Obee Holdings Ltd* (2016: No. 183) provided a pragmatic way forward: in *Re Z-Obee*, His Lordship adjourned a winding up petition filed with the Hong Kong Court against a Bermuda company to allow a window for the Hong Kong provisional liquidators to apply to the Bermuda court

for their appointment as restructuring provisional liquidators (permissible in Bermuda as discussed). The Bermuda court appointed the Hong Kong provisional liquidators as joint provisional liquidators of the company expressly for the purpose of restructuring. Then, the Hong Kong provisional liquidators applied to be discharged in Hong Kong, and the Bermuda court appointed joint provisional liquidators who subsequently sought recognition in Hong Kong and introduced a parallel scheme in order to effect the intended restructuring both in Hong Kong and Bermuda.

Re Z-Obee is *the* pioneer case in which the Hong Kong court applied judicial recognition and assistance techniques to mitigate/overcome the effect of *Re Legend* in a restructuring of an offshore incorporated, Hong Kong listed company.

Very recently, in *Re China Solar Energy Holdings [2018] HKCFI 555*, His Lordship has further clarified the position in *Re Legend*: notwithstanding that under the current statutory regime, the provisional liquidators need to be appointed on conventional grounds such as asset preservation and investigation, where the circumstances warrant, they can be given restructuring powers and can exercise such powers following completion of the tasks for which the appointment was made (such as asset preservation). On that basis, the Companies Judge dismissed an application to remove the provisional liquidators on the ground that their remaining role can only relate to restructuring – which appeared not to be permissible pursuant to *Re Legend*. The Learned Judge rightly decided that terminating the provisional liquidators just because their remaining role concerns restructuring would be detrimental to the creditors' overall interest. This would be inconsistent with the legislative purpose underlying appointment of provisional liquidators. This decision should be welcomed as it serves to mitigate the hardship arose out of *Re Legend*, and is very helpful in the context of cross-border restructuring.

Place of incorporation: natural forum for liquidation proceedings

His Lordship's approach on upholding the place of incorporation as being the natural and appropriate forum for winding up and appointment of provisional liquidators can be seen in *Re G Limited [2016] 1 HKLRD 167*. Here the Court dismissed an application for appointment of provisional liquidators in Hong Kong over a Cayman company listed on the Hong Kong Stock Exchange. The petitioner in *Re G Limited* sought to wind up the company on the grounds of insolvency and to appoint provisional liquidators in Hong Kong. At the first hearing, it emerged that the company had also brought winding up proceedings in the Cayman Islands together with an application for appointment of provisional liquidators which would be heard in a matter of days. The Hong Kong Judge took the view that unless there were demonstrable pressing needs for immediate appointment in Hong Kong, the matter should be left to the Cayman Court being the court of place of incorporation. The Judge affirmed that in the conventional case an insolvent company should be wound up in its place of incorporation and then it is a matter for the liquidators to decide whether recognition or assistance is required from the court in Hong Kong. The Court considered that the most straightforward way to proceed in these circumstances would be to obtain a letter of request from the court of place of incorporation.

Notable recent examples of assistance provided by Hong Kong Court

In *Re Centaur Litigation SPC [2016] HKEC576*, pursuant to a letter of request issued by the Cayman Court, the Hong Kong Court was asked to grant a recognition order which was a more extensive order than what had previously been granted in Hong Kong, containing a provision requiring any person wishing to commence proceedings in Hong Kong against companies in liquidation to first obtain the court's leave. This was consistent with the 'automatic stay' provisions in section 186 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance of Hong Kong and also section 97 of the Cayman Companies Law. The Court was initially concerned that it might seem unfair to Hong Kong based creditors to incur costs in commencing legal action only to find, with no fault on their part, that the proceedings were subject to an automatic stay, but, on balance, granted the order sought.

A further notable example for Hong Kong Court granting an order recognising foreign liquidators is *Re BJB Career Education Co Ltd [2017] 1 HKLRD 113*. In that case, pursuant to a letter of request issued by the Cayman Court, the Hong Kong Court was asked to make an order requiring a former chairman and director to produce documents, answer interrogatories and attend an oral examination. The former chairman sought to argue that an oral examination order could not be made against an officer of a foreign company as such an order would infringe Article 96 of the Basic Law. Article 96 provides 'With the assistance or authorization of the Central People's Government, the Government of the Hong Kong Special Administrative Region may make appropriate arrangements with foreign states for reciprocal judicial assistance'. The former chairman's argument appears to be that such assistance to the foreign court cannot be provided in the absence of assistance or authorisation of the Central People's Government. Such argument was dismissed. The Court affirmed that the common law power of assistance extended to an order for oral examination if such a power existed in both the jurisdiction of liquidation (here, the

Cayman Islands) and the assisting jurisdiction (here, Hong Kong). It further affirmed that reciprocity was not a necessary component of recognition of and assistance to foreign liquidators. It was held that the Basic Law was not contravened as the common law position was clearly part of the laws in Hong Kong prior to 1997.

More recently, the Hong Kong Court clarified (and reaffirmed) its view on powers of foreign insolvency officeholders in *Re China Lumena New Materials Corp [2018] HKCFI 276*.

In *Re China Lumena*, the provisional liquidators appointed by the Cayman Court encountered difficulties in taking control of the Company's bank accounts in Hong Kong because some local banks require to see a Hong Kong Court order before they are prepared to comply with a provisional liquidators' request for a transfer of the Company's credit balances. Citing his Judgment in *Bay Capital Asia Fund, LP v DBS*, his Lordship confirmed that, the ability of foreign insolvency officeholders appointed by the Court in the country of incorporation of the company to obtain documents relating to the Company's bank account in Hong Kong is generally not dependent on obtaining a prior Hong Kong Court order:

> '[I]f a bank receives a request from liquidators of a company which has an account with them, once it is satisfied, which should be straightforward, that the liquidators have been properly appointed by the court of the place of the company's incorporation they will hand over documents to which the directors of the company would have been entitled.'

In *Bay Capital*, Harris J. explained that if foreign insolvency officeholders would like to deal with assets located in Hong Kong (as opposed to merely obtain documents/information), they should apply for a Hong Kong order authorising the transfer of such assets.

Here the provisional liquidators had argued that on the basis that they are entitled to information from the banks without a Hong Kong order (akin to the information right enjoyed by directors of the Company), it logically follows that the Cayman appointed provisional liquidators could also request the Hong Kong banks to transfer the credit balances without a Hong Kong order.

The Hong Kong Judge considered that 'this would be going too far' and would go even further than international insolvency standards envisaged in Article 21 of the UNCITRAL Model Law on Cross-Border Insolvency.

In order to strike a balance between the foreign insolvency officeholders' need for convenience and the local court supervision which may be expected by the creditors, his Lordship maintained his view that foreign insolvency officeholders appointed by the place of incorporation are entitled to information without a prior Hong Kong recognition order; but that it would be appropriate to seek recognition in Hong Kong in order to take possession of or deal with the assets in Hong Kong. The Learned Judge particularly reminded practitioners about the standard practice for applying recognition orders and such orders may be granted very quickly, pursuant to the standard practice.

This decision is of significance to Hong Kong insolvency law practitioners and in-house lawyers, particularly those working for financial institutions. It used to be standard local practice to require sight of a 'local order' before acting on any request from foreign insolvency officeholders. Based on the Court's repeated emphasis in this case and *Bay Capital*, it would be incorrect for practitioners to insist on seeing a 'local order' before complying with an information request from a foreign insolvency officeholders (appointed by country of incorporation) in respect of the affairs and assets of the company. If such incorrect approach is adopted in the future, it is likely to attract judicial criticism and may lead to penalty in terms of costs.

Conclusion

The recent judicial approach of the Hong Kong Court reinforces the modern notion of cross-border insolvency cooperation between international courts and should certainly be welcomed.

Legal practitioners should be mindful that the country of incorporation is the natural jurisdiction to commence insolvency proceedings at common law. Commencing insolvency proceedings in the place of incorporation would ensure that, if the court so orders, the liquidation or provisional liquidation status is globally applicable.

We have seen a number of cases whereby insolvency officeholders appointed in Hong Kong over offshore companies were unable to carry out their work effectively in the absence of parallel proceedings in the place of incorporation. As discussed above, given the limitation of the Hong Kong statutory regime for corporate restructuring/rescue at present, commencing liquidation (and an application for appointment of provisional liquidators) in the place of incorporation would enhance flexibility of potential restructuring down the road.

In light of the Hong Kong Court's expressed readiness in providing assistance to offshore insolvency proceedings, there appears to be no reason for practitioners and their clients to be concerned about the foreign liquidators' ability to perform their duties in Hong Kong in an efficient manner.

Conyers Dill & Pearman advises on the laws of Bermuda, BVI and Cayman. Conyers Dill & Pearman does not *advise on the law of Hong Kong.*

International Corporate Rescue

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