Hong Kong – Cross-border insolvency: The law and development in Hong Kong

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This article considers the corporate insolvency laws in Hong Kong to which a creditor might look where it seeks recourse against an insolvent company which is not incorporated in Hong Kong (for convenience, in this article a company incorporated in a place other than Hong Kong is referred to as a “non-Hong Kong company”). A creditor dealing with a non-Hong Kong company may seek to: (i) liquidate, and have an insolvency representative appointed to, the company in its place of incorporation. The insolvency representative might then seek recognition from the Hong Kong Court to enable him to protect and realise assets of the company located in Hong Kong; or (ii) appoint Hong Kong liquidators over the company, either instead of or after the appointment of an insolvency representative in the company’s place of incorporation. This article is principally concerned with the latter option, but starts with a brief review of the former.

Recognition of overseas insolvencies in Hong Kong

Whilst Hong Kong’s statutory corporate insolvency laws do not expressly provide for the recognition of an overseas insolvency, or those administering it, case law suggests that the Hong Kong Court will generally recognise the status of an insolvency representative appointed by an overseas court.

As a result it is not always necessary for a creditor to seek to commence a liquidation in Hong Kong to protect and realise the Hong Kong assets of a non-Hong Kong company. It may suffice for him to obtain a winding-up order in the company’s place of incorporation, and for the insolvency practitioner appointed in the company’s place of incorporation to gain possession of the non-Hong Kong company’s Hong Kong-based assets and, if necessary, seek orders from the Hong Kong Court to secure and realise the same.

But sometimes there is good reason to want to see liquidators appointed in Hong Kong to a non-Hong Kong company. For example, the fact that Hong Kong does not have a comprehensive statutory framework providing for the recognition of overseas insolvencies, and has not enacted the UNCITRAL Model Law on Cross-Border Insolvency (“the Model Law”) (and is unlikely to do so in the foreseeable future), creates uncertainty which is not merely uncomfortable but can result in substantial delay and cost, especially where the company disputes the insolvency representative’s claim for recognition.

Winding-up non-Hong Kong companies in Hong Kong

There may also be other, concrete reasons why the commencement of winding-up proceedings in Hong Kong in relation to a non-Hong Kong company might be beneficial in some circumstances – for example, it might enable a creditor to benefit from certain statutory provisions which apply only when there is a winding-up in Hong Kong, including the automatic stay of legal proceedings against the insolvent company, the avoidance of execution and attachments against the insolvent company and the investigative powers granted to Hong Kong liquidators to enquire into the affairs of an insolvent company by examining its directors and others.

Jurisdiction

The Hong Kong Court has discretionary jurisdiction to wind up “unregistered” companies (which includes non-Hong Kong companies) by virtue of Section 327 of the Companies Ordinance.

Grounds

Section 327(3) lists the circumstances in which a non-Hong Kong company may be wound up in Hong Kong, as follows:

• the company is dissolved, or has ceased to carry on business, or is carrying on business only for the purpose of winding up its affairs;
• the company is unable to pay its debts; or
• the court is of opinion that it is just and equitable that the company be wound up.

One of these three circumstances must be present to enable the Hong Kong Court to exercise its discretionary jurisdiction to wind up a non-Hong Kong company. Most commonly, the ground cited is that the company is unable to pay its debts.

Legal framework

Section 327 provides a statutory exception to the general principle that the law of a company’s place of
incorporation governs its status, and is therefore the appropriate law and system under which to liquidate a non-Hong Kong company. It is recognised that the jurisdiction provided by Section 327 is, in this sense, “exorbitant” such that there must be sufficient connection with Hong Kong to justify the court setting in motion its winding-up procedures over a body which prima facie is beyond the limits of territoriality.

If successful, a petition to wind up a non-Hong Kong company engages the same statutory regime for winding up as that which applies to a Hong Kong incorporated company: there is no qualification or limitation to the application of that regime in the case of a non-Hong Kong company. Potentially, a non-Hong Kong company can be ordered to be wound up by a court in its place of incorporation and, at the same time, by a court in Hong Kong, leading to a potential for conflict between the two separate insolvency regimes in those two countries.

In considering whether to exercise its discretionary jurisdiction to wind up a non-Hong Kong company, the Hong Kong Court must be satisfied that setting in motion this process is justified. The consequences of making a winding-up order informs a consideration of whether or not sufficient connection with Hong Kong has been demonstrated. This issue is addressed in more detail in the next section.

**Requisite jurisdictional connection**

The Companies Ordinance is silent as to the jurisdictional connection that must exist between the non-Hong Kong company and Hong Kong before the Hong Kong Court will agree to liquidate that company. However, the authorities provide clear guidance as to how the Hong Kong Court will approach this issue. In *Re Beauty China Holdings Ltd.*, the Hong Kong Court summarised the three “core requirements” for it to exercise its jurisdiction to wind up a non-Hong Kong company, as follows:

- sufficient connection with Hong Kong (this can, but does not necessarily have to, consist of the presence of assets in Hong Kong);
- reasonable possibility that the winding-up order will benefit those applying for it; and
- the Hong Kong Court is able to exercise jurisdiction over one or more persons interested in the distribution of the company’s assets.

These core requirements have recently been analysed by Harris J of the Hong Kong Companies Court in judgments handed down in two separate, unrelated matters. The most recent of Harris J’s decisions is that in *Re Pioneer Iron and Steel Group Company Ltd.*

In *Pioneer Iron*, the Court noted that the significance of each of these core requirements will vary from case to case, and that an exceptional case may arise in which the connection with Hong Kong is so strong and the benefits of a winding-up order for the creditors of a company are so substantial that the Court will be willing to exercise its jurisdiction despite the third core requirement not being satisfied.

The Court in *Pioneer Iron* also provided helpful guidance on how the three core requirements should be understood and applied.

In relation to the “sufficient connection” requirement, the Court noted that it does not necessarily follow from the fact that a company has not established a place of business in Hong Kong that it does not have substantial connection with Hong Kong. Rather, the fact that the controlling mind of a commercially active company is based in Hong Kong and makes business decisions in Hong Kong about the company constitutes a substantial connection. The fact that the company might also carry out some of its activities elsewhere does not dilute the substance of that connection.

In relation to the “benefit to those applying” requirement, the Court noted that the material question is whether there are any further benefits to be gained from a winding-up order; and that – even if there were – the Court should still not make the order unless it is satisfied that those benefits outweigh the additional costs that would be caused by making the winding-up order. In *Pioneer Iron* the Court decided that the benefits to the company and its creditors derived from the use of the investigation procedures available to Hong Kong liquidators under the Companies Ordinance were such that this requirement was satisfied.

In relation to the third core requirement, the Court noted that, in most cases, the “jurisdictional” requirement will be satisfied by the existence of a creditor who is an individual resident in Hong Kong or a foreign company which is registered under Part XI of the Companies Ordinance or which has a place of business in Hong Kong. Without deciding the question (it was unnecessary in this instance because there existed an individual creditor resident in Hong Kong who asserted a significant claim against the company), the Court stated its view that the authorities from which this requirement emerges intended to require there to exist a person concerned with the proper distribution of assets and over whom the Court can exercise jurisdiction, other than by virtue of him being a creditor of the company.

**Discretion**

Once the Hong Kong Court has determined that the jurisdictional test is met, so that it is empowered to make a winding-up order; the question remains as to whether it ought to exercise its discretion to make that order.
Notwithstanding the fact that one of the circumstances listed in Section 327(3) exists and the three core requirements have been demonstrated, it is still not automatic that a winding-up order will be granted. The making of the winding-up order remains a matter of discretion; the Hong Kong Court may determine that it ought still to refuse to make a winding-up order on the basis of other factors that are put before it (for example, if for some good reason the majority of the creditors object to a winding-up order; the Hong Kong Court may refuse to make the order).

**Relief**

In Hong Kong (where there is no statutory provision providing for co-operation between courts exercising jurisdiction in relation to insolvency unlike, for example, in England and Wales)\(^1\) a liquidator appointed pursuant to the Companies Ordinance to wind up an insolvent non-Hong Kong company is required, whatever the practical position may be, to collect in its assets in Hong Kong and overseas and settle a list of creditors worldwide who submit proofs of debt in accordance with Hong Kong law.

However, if a non-Hong Kong company is already in liquidation in its place of incorporation, a liquidation in Hong Kong will generally be treated as ancillary to it – the functions of the Hong Kong liquidator being framed by Court order accordingly, to provide that he is to collect in the Hong Kong assets, to settle a list of Hong Kong creditors and to transmit the assets and the list to the principal liquidators in the company’s place of incorporation to enable a dividend to be declared and paid.

In the former case, a “concurrent” liquidation, the Hong Kong liquidator is on equal footing with his overseas counterparts and each jurisdiction administers its assets and makes payments to creditors in the separate liquidation. To facilitate cooperation in such cases, the use of protocols as a pragmatic solution to harmonise and co-ordinate concurrent liquidations has become increasingly commonplace, and an accepted part of Hong Kong insolvency law, since many companies operating in Hong Kong are incorporated in other jurisdictions, such as Cayman or the BVI.

In the latter case, the Hong Kong liquidation will be governed and conducted in accordance with Hong Kong insolvency law, but in cooperation with the overseas liquidation process. In such a case, after paying the costs of the Hong Kong liquidation, the Hong Kong court will order the surplus assets to be turned over to the overseas liquidator for pari passu distribution to all creditors of the non-Hong Kong company.

**Conclusion**

Where the requisite connection with Hong Kong exists, a creditor of a non-Hong Kong company should consider whether its interests might best be served by petitioning for the winding-up of that non-Hong Kong company in Hong Kong and having Hong Kong liquidators appointed to the company. The presence of assets within Hong Kong is one, but not the only, reason why such course of action might be advisable.

**Notes:**

Hong Kong law contains provisions enabling a creditor to seek to invoke the jurisdiction of the Hong Kong Court against non-Hong Kong companies outside of the insolvency process in appropriate circumstances. An analysis of these provisions is outside the scope of the present article.

1. In a paper issued on October 31, 2011, the Financial Services and the Treasury Bureau (“FSTB”), noting that 19 jurisdictions including the US, the UK, Australia, Japan, New Zealand and South Africa, had adopted the Model Law, stated that the possibility of adopting the Model Law “involves complex international law issues, and likely requires a standalone piece of legislation separate from the [Companies] Bill” that was then under discussion and was not anticipated to be enacted before mid-2016. The FSTB went on to say that “we can only formulate a timetable after further research and assessment on resources”; nothing further has been issued to date on the matter by the FSTB.

2. Section 183.

3. Section 269.

4. Sections 221 and 222.

5. Section 326: an “unregistered” company is defined to include, a, any company not formed and registered under the Companies Ordinance (and thus, any non-Hong Kong company) including a non-Hong Kong company that is registered under Part XI of the Companies Ordinance.

6. Unless otherwise stated, all references to section numbers in this article are reference to sections of Hong Kong’s Companies Ordinance, Cap. 32.

7. Section 327(3).

8. Section 327(4) provides a detailed regime for when a non-Hong Kong company will be deemed unable to pay its debts.

9. To adopt the words of Moran LJ at paragraph 22 of his judgment in Stocznia Gdanska SA v Latreefers Inc (No 2) [2001] 2 BCLC 116, referencing the equivalent section in England and Wales (s. 221 of the Insolvency Act 1986).

10. This was accepted by Harris J in Pioneer Iron and Steel Group Company Ltd HCCW 322/2010.
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(Unreported, March 6, 2013) (see paragraph 30).

The origins of these requirements, which are adopted in other subsequent cases in Hong Kong, are to be found in the judgment of Knox J in Re Real Estate Development Co [1991] BCLC 210 at 217. See also Re Yung Kee Holdings [2012] 6 HKC 246.

Supra. The earlier of Harris J’s two recent judgments on this subject is that of Re Yung Kee, supra.

Pioneer Iron and Steel Group Company Ltd, ibid, paragraph 28.

Ibid, paragraph 37.

Ibid, paragraph 38.

Ibid, paragraphs 39 and 40.

Ibid, paragraph 41.

Ibid, paragraph 43.


Section 426(4) of the Insolvency Act 1986.

In his decision in Pioneer Iron and Steel Group Company Ltd, ibid, the Judge cited two English cases to support this proposition: Re Bank of Credit and Commerce International SA (No 2) [1992] BCLC 579 and Re Bank of Credit and Commerce International SA (No 3) [1993] BCLC 1490.

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