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Restructuring & Special Situations

2022 Year in Review

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Key insolvency decisions in Hong Kong and PRC

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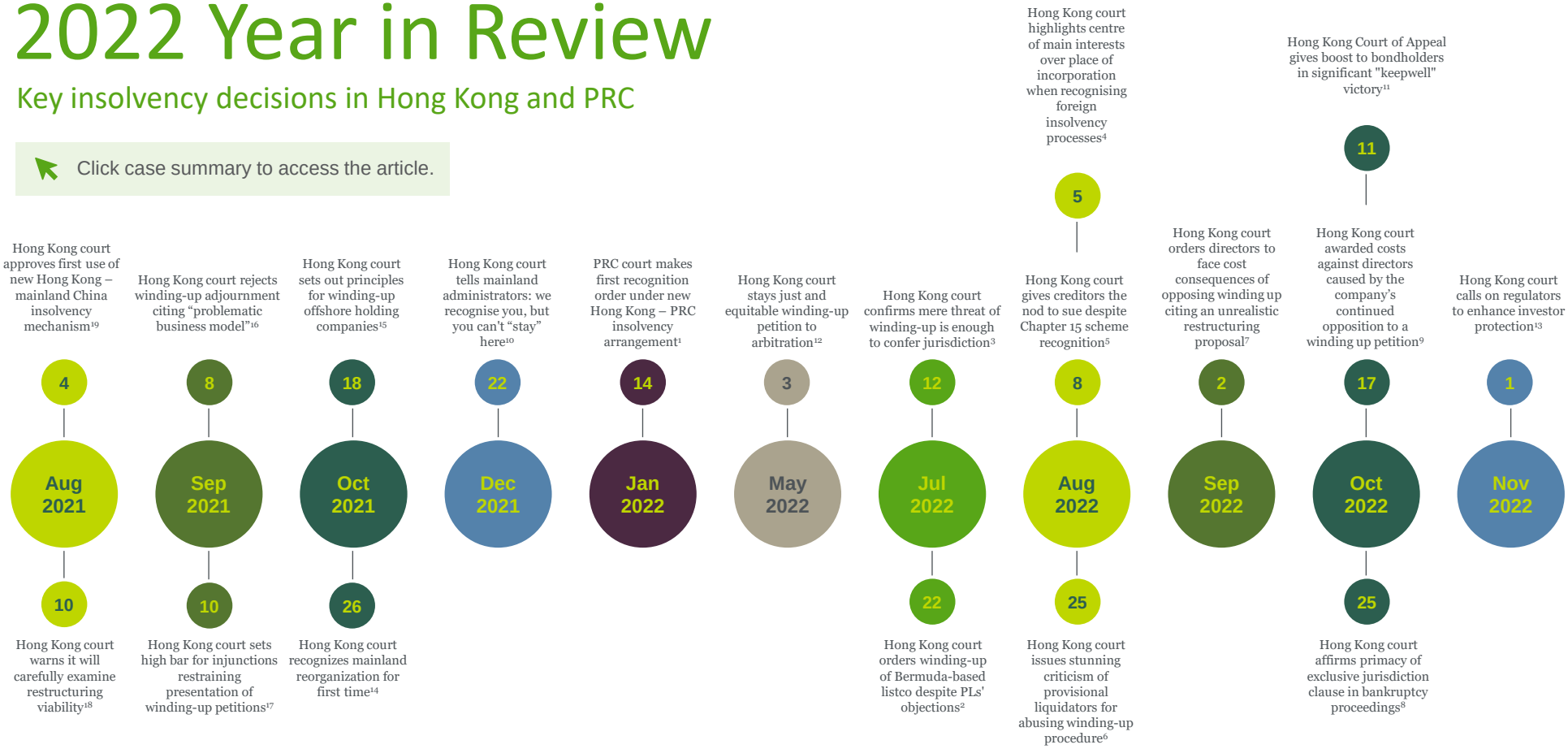

Footnotes

1. (2021) 粤03认港破1号民事裁定书
2. Re Up Energy Development Group Limited [2022] HKCFI 1329
3. Shandong Chenming Paper Holdings Limited v Arjowiggins HKK2 Limited [2022] HKCFA 11
4. Provisional Liquidator of Global Brands Group Holding Limited (in liquidation) v Computershare Hong Kong Trustees Limited and Another [2022] HKCFI 1686
5. Re Rare Earth Magnesium Technology Group Holdings Ltd [2022] HKCFI 1686
6. GTI Holdings Limited [2022] HKCFI 2598
7. Carnival Group International Holdings Limited [2022] HKCFI 2668
8. Re Guy Kwok Hung Lam [2022] HKCA 1297
9. Re Carnival Group International Holdings Ltd [2022] HKCFI 3097, [2022] HKEC 4181
10. HCA 778 of 2021, HCA 778/2021, HCA 798/2021, HCA 1418/2021 and HCA 1442/2021
11. Nuoxi Capital Limited (諾熙資本有限公司) (in liquidation in the British Virgin Islands) v Peking University Founder Group Company Limited (北大方正集團有限公司) [2022] HKCA 1514
12. China Europe International Business School v Chengwei Evergeen Capital LP [2021] HKCFI 3513
13. Securities and Futures Commission v Sound Global Ltd [2022] HKCFI 3025
14. Re Jiang Wenyu [2021] HKCFI 2897
15. Re Grand Peace Group Holdings Limited [2021] HKCFI 2361
16. Re Trinity (Management Services) Ltd [2021] HKCFI 2207
17. Silver Starlight Ltd v China Citic Bank Corp Ltd [2021] HKCA 1248
18. Li Yiqing v. Lamtex Holdings Limited [2021] HKCFI 622, Re Ping An Securities Group (Holdings) Limited [2021] HKCFI 651, Re Joint Provisional Liquidators of China Bozza Development Holdings Ltd. [2021] HKCFI 1235, and Re Joint and Several Provisional Liquidators of Victory City International Holdings Limited [2021] HKCFI 1370
19. Re Lai Kar Yan Derek [2021] HKCFI 2151

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2022 has been a year which has seen significant developments in court-led corporate rescue and insolvency law reform in Hong Kong. In light of the lingering COVID-19 pandemic, it was all the more important that the Hong Kong courts rise to the challenge of enabling companies to address their financial difficulties within the flexible confines of the common law, all against the backdrop of Hong Kong lacking a statutory corporate rescue regime, as is common in most other developed countries around the world.

Cross-border recognition between Hong Kong and mainland China

The Hong Kong court took a significant step forward in developing the law in reciprocal recognition of cross-border insolvency between Hong Kong and mainland China when it granted for the first time an order recognising the bankruptcy reorganisation of a mainland business group and provided recognition and assistance to three individuals representing the mainland-appointed administrator.

The decision in *Re Jiang Wenyu* [2021] HKCFI 2897 (relating to the reorganization of HNA Group Co., Limited) was just weeks after a new co-operation mechanism came into force under which liquidators from Hong Kong may apply to certain mainland courts (currently limited to three pilot cities) for recognition of insolvency proceedings commenced in Hong Kong, whilst bankruptcy administrators from the mainland may apply to the Hong Kong court for recognition of bankruptcy proceedings commenced in the mainland.

For its part, a decision by the Shenzhen Intermediate People's Court in *(2021) 粤03认港破1号民事裁定书* marked the first occasion on which a mainland court had formally recognised and granted assistance to Hong Kong appointed liquidators, expressly granting them powers to deal with assets located in the mainland under the new insolvency co-operation mechanism.

The mechanism opens a new chapter in the cross-border insolvency space between Hong Kong and mainland China and more applications for recognition and assistance can be expected in the future.

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"Soft touch" provisional liquidation – redrawing the boundaries

2022 was also the year where the Hong Kong court saw fit to both clarify and qualify the application of recognition of foreign "soft touch" provisional liquidators, at the same time reining in some of the perceived abuses.

In *GTI Holdings Limited* [2022] HKCFI 2598, the Honourable Madam Justice Linda Chan criticized provisional liquidators appointed in offshore jurisdictions in relation to their "attempt to bypass the creditors' statutory rights" as they had made significant misrepresentations to the offshore courts in view of getting recognition and assistance in Hong Kong. In the end, the court disallowed the right of the provisional liquidators to receive remuneration and to recover costs for making the application.

The decision in *GTI Holdings* followed a line of decisions in which the Hong Kong Companies Court criticised debtor companies for trying to achieve successive adjournments of Hong Kong winding up proceedings by touting unrealistic restructuring schemes (see *Li Yiqing v Lamtex Holdings Limited* [2021] HKCFI 622, *Re Ping An Securities Group (Holdings) Limited* [2021] HKCFI 651, *Re Joint Provisional Liquidators of China Bozza Development Holdings Ltd.* [2021] HKCFI 1235, and *Re Joint and Several Provisional Liquidators of Victory City International Holdings Limited* [2021] HKCFI 1370.)

In *Carnival Group International Holdings Limited* [2022] HKCFI 2668, the Honourable Madam Justice Linda Chan ordered the directors of a Bermuda-incorporated Hong Kong-listed company to be joined as defendants for the purpose of having costs awarded against them for opposing winding up in the absence of a viable restructuring proposal. The court subsequently ordered four of the director respondents to bear costs personally for having caused the company to continue opposing the winding petition.

In the absence of statutory insolvent trading provisions in Hong Kong, the warning given in the *Carnival* decisions serves as a timely reminder to directors, particularly independent non-executive directors, that they must regularly and critically analyse the company's prospects of successfully achieving a restructuring when they chose to continue to trading and actively defend winding up proceedings.

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Importance of COMI

In *Provisional Liquidator of Global Brands Group Holding Limited (in liquidation) v Computershare Hong Kong Trustees Limited and Another* [2022] HKCFI 1789, the Hong Kong court confirmed that recognition and assistance would be given to a foreign insolvency process conducted in a company's centre of main interests and that it will no longer be necessary for the foreign insolvency process to be carried out in a company's place of incorporation.

The judgment set out a practical roadmap for the future of cross-border insolvency in Hong Kong, where listed companies with assets in the mainland and incorporated offshore find themselves in difficulty.

Winding up of foreign incorporated companies

The Court of Final Appeal in *Shandong Chenming Paper Holdings Limited v Arjowiggins HKK2 Limited* [2022] HKCFA 11 expanded on the second of the three core requirements for the winding-up of a foreign company in Hong Kong outlined in the earlier CFA decision *Kam Leung Sui Kwan v Kam Kwan Lai* [2015] 18 HKCFAR 501 and clarified that the "leverage" created by the prospect of winding-up is considered a legitimate form of "benefit" for the purpose of satisfying the second core requirement. This represents a welcome development for creditors who seek the repayment of debts from foreign companies that have a substantial connection to Hong Kong.

This year also saw the Honourable Madam Justice Linda Chan in *Re Up Energy Development Group Limited* [2022] HKCFI 1329 clarify that the fact that a foreign company has been ordered to be wound up by the court in its place of incorporation does not preclude the Hong Kong court from making a winding-up order, provided that the three core requirements stated in *Kam Leung Sui Kwan* are satisfied. On a practical note, the court considered that "if the [foreign company was] not wound up by the court, multiple proceedings would ensue which, in turn, would increase the time and costs for administering the affairs in Hong Kong."

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Pro-arbitration

The Hong Kong courts continued to demonstrate their general "pro-arbitration" approach. The court in *China Europe International Business School v Chengwei Evergeen Capital LP* [2021] HKCFI 3513 stayed a petition presented to wind up a solvent company under the just and equitable ground in favour of arbitration, since the parties had clearly demonstrated their preference for using arbitration as the preferred means of dispute resolution.

Gibbs is alive and well

The Hong Kong courts are willing to sanction schemes of arrangement concerning foreign entities with overseas assets if it is convinced that the proposed restructuring plan is viable. However, 2022 saw the Honourable Mr Justice Harris in *Re Earth Magnesium Technology Group Holdings Ltd* [2022] HKCFI 1686 comment in obiter remarks that "a scheme sanctioned in an offshore jurisdiction and recognized under Chapter 15 in the United States will not be treated by a Hong Kong court as compromising US$ debt". The United States Bankruptcy Court subsequently said it was not convinced of the correctness of the approach.

Exclusive jurisdiction clauses

The Hong Kong Court of Appeal dismissed a challenge to a first instance decision which recognised the Beijing administrators of the commercial arm of the Peking University Group but granted only a limited stay of proceedings. The decision in *Nuoxi Capital Limited (諾熙資本有限公司) (in liquidation in the British Virgin Islands) v Peking University Founder Group Company Limited (北大方正集團有限公司)* [2022] HKCA 1514 means that bondholders and issuers can now be assured of having their contractual rights arising under "keepwell" arrangements determined in the Hong Kong court, rather than the Beijing court. However, it remains to be seen what weight the Beijing court will attach to the Hong Kong judgments on these matters and one awaits to see the trials and other keepwell actions in the early part of 2023.

The year also saw the Court of Appeal confirm in *Re Guy Kwok Hung Lam* [2022] HKCA 1297 that a Hong Kong court should ordinarily respect and give effect to an exclusive jurisdiction clause in bankruptcy proceedings, unless there are persuasive reasons to refrain from doing so. There is no need for a Hong Kong court to first look to the existence of a bona fide dispute before deciding whether to defer to a foreign forum named under the agreement between the parties.

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Investor protection

Finally, the year saw the Honourable Madam Justice Linda Chan calling on regulators to enhance investor protection. In Securities and Futures Commission v Sound Global Ltd [2022] HKCFI 3025, the Securities and Futures Commission was unable to effect service for the purpose of seeking a disqualification order against directors of a listed company. The court specifically expressed the view that regulators should step up when it comes to enforcing investor protection with mainland-based directors of Hong Kong listed companies and it is now up to the regulators to consider putting in place appropriate measures to align with the court's view.

Ahead in 2023

A wide-ranging mechanism allowing for reciprocal enforcement of judgments in mainland China and Hong Kong has come one stage closer with the gazetting of the Mainland Judgments in Civil and Commercial Matters (Reciprocal Enforcement) Ordinance. The Ordinance implements the Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and the Hong Kong Special Administrative Region which was signed on 18 January 2019.

Subject to limited exceptions, the new mechanism allows for registration in Hong Kong of mainland judgments in civil or commercial matters and also for the making of applications to the Hong Kong courts for certified copies of and certificates for Hong Kong judgments in civil or commercial matters for the purpose of facilitating the seeking of recognition and enforcement of Hong Kong judgments in the mainland.

In terms of legislative efforts, it remains unclear whether the updated Companies (Corporate Rescue) Bill will be introduced in 2023. Whilst the Bill has its shortcomings and the proposed provisions lack many of the features that exist in other modern restructuring frameworks, it would no doubt provide some additional tools to assist with achieving a corporate rescue.

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