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Hong Kong

RESTRUCTURING & INSOLVENCY

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This country-specific Q&A provides an overview of restructuring & insolvency laws and regulations applicable in Hong Kong.

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HONG KONG RESTRUCTURING & INSOLVENCY



Hong Kong is a leading global financial center that is routinely ranked by the World Bank Group as one of the top three jurisdictions for ease of doing business. The 2020 rankings reflect this commercial reality. Hong Kong is a Special Administrative Region (SAR) of the People's Republic of China.

With the establishment of the Hong Kong SAR in 1997 following its transfer back to the People's Republic of China by the United Kingdom, the "Basic Law" of Hong Kong was enacted by the National People's Congress in accordance with the Constitution of the People's Republic of China and took effect as a mini-constitution for Hong Kong. The Basic Law ensures that Hong Kong, as a special administrative region, will maintain separate governing and economic systems from those of mainland China for 50 years after the establishment of the Hong Kong SAR in accordance with the principle of "one country, two systems". For such period of time, save for any law contravening the Basic Law and subject to any amendment that may be passed by Hong Kong legislature, all laws in force prior to the establishment of the Hong Kong SAR (including common law, rules of equity, ordinances, subordinate legislation and customary law) will be retained and national laws of the People's Republic of China will not be applied in Hong Kong (except for a number of laws relating to defense and foreign affairs). Article 8 of the Basic Law maintains the common law system that has been practiced in Hong Kong for more than 170 years and makes Hong Kong the only common law jurisdiction within China. This legal reality has not changed, and is unlikely to change in the near future.

The restructuring and insolvency legal framework of Hong Kong is principally set out in: (i) the new Companies Ordinance (Cap. 622), which took effect on 12 July 2012 and provides the general framework for the incorporation and operation of companies in Hong Kong; (ii) the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap. 32) (the Winding-Up Ordinance) and subsidiary legislation (including the Companies (Winding-Up) Rules (Cap. 32H)), dealing with corporate insolvency (i.e. the winding up of Hong Kong companies and foreign corporations registered in Hong Kong); (iii) the Bankruptcy Ordinance (Cap. 6) and the Bankruptcy Rules (Cap. 6A) that apply to individual bankruptcy (as opposed to corporate insolvency), although the Winding-Up Ordinance applies by reference to insolvent companies certain provisions of the Bankruptcy Ordinance; (iv) the Rules of the High Court (Cap. 4A) in respect of procedural matters; and (v) the Conveyancing and Property Ordinance (Cap. 219), which regulates the ownership, proof of title, transfer, and mortgaging of properties in Hong Kong.

The Winding-Up Ordinance (as amended in 2016 with effect on 13 February 2017 to increase the protection of creditors against asset depletion) generally reflects the English Companies Acts of 1929 and 1948, but without English insolvency law revisions for administration. It provides for

three types of liquidation: members' voluntary liquidation, creditors' voluntary liquidation and compulsory liquidation. Voluntary administration or "Chapter 11" procedures are not available in Hong Kong. The government may petition for the winding up of a company if considered expedient in the public interest.

The Bankruptcy Ordinance, offers a modern regime of bankruptcy for individuals that was introduced on 1 April 1998 and later amended in 2016 to facilitate the administration of the bankruptcy estate. It contemplates voluntary arrangements for both bankrupts and non-bankrupts.

1. What forms of security can be granted over immovable and movable property? What formalities are required and what is the impact if such formalities are not complied with?

A mortgage is the form of security granted over immovable property. A legal mortgage transfers legal title in the land to the mortgagee, subject to the mortgagor's equity of redemption that is, the right to redeem the mortgaged property on repayment of the debt in question. The security allows the security provider to occupy the land and buildings and covers the land, fixtures, fittings and things permanently attached to the property.

The formalities required to grant security over any interest in land must be made in writing by deed to pass legal title and registered at the Hong Kong Land Registry within one month of the security being created or the priority of the security may be affected. If the mortgagor is a Hong Kong incorporated company or a registered non-Hong Kong companies (under Part 16 of the Companies Ordinance), registration with the Registrar of Companies within one month of the date the security is created is required. Failure to do so may result in the security being voided against a liquidator and any creditor of the company.

Security can be granted over tangible movable property including:

- (i) mortgages, where legal title to the property is transferred to the mortgagee but the mortgagor is allowed to have possession and use of the property (until enforcement);
- (ii) charges, (either in the form of a fixed or floating charge) where legal title to the property remains with the chargor who grants a security interest encumbering the beneficial interest of the property in favor of the chargee. A fixed charge will allow the chargee to control

the charged property and a floating charge would not, instead a crystallization provision would be in place to enable the chargee to restrict chargor from using the charged assets freely on the occurrence of certain pre-agreed events (such a breach or default);

(iii) pledges, where the pledgee will take physical possession of the property or documents of title as security; and

(iv) liens, which is a right to retain property of another party until the debt owed is discharged.

The formalities to grant a mortgage or charge over movable property is similar to that of the registration of an interest in land (see above). Market practice also dictates security over certain assets and will be notified to the appropriate authority, such as the notification of any mortgage created over a Hong Kong registered aircraft to the Director of Civil Aviation. There are also specialist registers for certain classes of movable property, such as ships, where the Marine Department specifies certain marine vessel mortgage registration requirements, and in case of a trade mark, registration with the Intellectual Property Department. There are no formalities to register security interest other than mortgages and charges.

2. What practical issues do secured creditors face in enforcing their security (e.g. timing issues, requirement for court involvement)?

There are no material restrictions or mandatory court approval requirements for secured creditors to enforce their security (such as the absence of mandatory public auction requirements). The precise steps, cost and timing of the process (and the need for consent) will depend on the nature of the security interest and property in question. The success of secured creditors to enforce their security depends on their ability to trace

and obtain control of the asset and the asset's disposal value.

Hong Kong allows an agent or trustee to hold security on behalf of the lenders, in which case an agent or trustee will manage the enforcement process. In other cases where an agent or trustee is not appointed over the security, individual creditors would be free to act independently and in a potentially opportunistic or prejudicial manner to other creditors and the obligors.

3. What is the test for insolvency? Is there any obligation on directors or officers of the debtor to open insolvency procedures upon the debtor becoming distressed or insolvent? Are there any consequences for failure to do so?

Generally speaking, the test of insolvency is aligned with a company that is "unable to pay its debts". There are three broad ways under Hong Kong law in which to establish that a company is "unable to pay its debts":

- (i) failure (for a period of three weeks) to pay, secure or procure payment (to the reasonable satisfaction of the creditor) of a sum equal to or exceeding HK\$10,000 which is then due and which has been the subject of a statutory demand;
- (ii) failure to satisfy (in whole or in part) an execution or other processes issued on a judgment, decree or order of any court in favor of a creditor of the company; or
- (iii) proving to the Court that a company is unable to pay its debts, taking into account the prospective and contingent liabilities of the company by either the "cash flow test" (meaning the company cannot pay its debts as they fall due in the plain sense) or the "balance sheet test" (the company's assets less its contingent and prospective liabilities).

There are generally no obligations on directors or officers to open insolvency procedures upon the debtor becoming distressed or insolvent, unless fraudulent intent can be proven. The recent case of *Moulin Global Eyecare Holdings Limited v Olivia Lee Sin Mei* [2019] HKCFI 1715, directors can be found liable for breaching their duty of care and skill if they fail to properly investigate red flags concerning the solvency of the company. Hong Kong courts have leaned in favor of the liquidators and held that a non-executive director breached her duty of care and was personally liable for the company losses, as she had acquired knowledge that should have caused her serious concern and prompt further investigation; had she done so the fraudulent

conduct of the company would have been revealed.

4. What insolvency procedures are available in the jurisdiction? Does management continue to operate the business and/or is the debtor subject to supervision? What roles do the court and other stakeholders play? How long does the process usually take to complete?

The insolvency procedures available for companies include: (i) scheme of arrangement; (ii) receivership; (iii) members' voluntary liquidation; (iv) creditors' voluntary liquidation; and (v) compulsory liquidation.

Only in the case of a scheme of arrangement, management continue to operate the business and retain control which they ordinarily have prior to the scheme becoming effective and binding.

In the case of a receivership, the director's powers will be suspended to the extent they are inconsistent with the right of the receiver to exercise the powers in connection with his appointment.

Both members' voluntary liquidation and creditors' voluntary liquidations are subject to the court's supervisory jurisdiction, which means that stakeholders such as the liquidator, creditors or shareholders may apply for the court's directions as to the conduct of certain aspects of the liquidation. It is customary that these liquidations can proceed with minimal guidance from the court, particularly where the liquidation is solvent. The court takes a supervisory role in the case of the administration of the compulsory winding up of a company. The court's approval is also required for certain matters, including the appointment of provisional liquidators and liquidators who act as officers of the court in the management of the company during the compulsory liquidation process. The timing for each of these processes will depend on the facts. In a members' voluntary winding up and creditors' voluntary winding up, the company will be permanently dissolved 3 months after the Registrar of Companies registers the final accounts and return filed by the liquidator following the final meeting of creditors and contributories. In the case of a compulsory winding up, the company will be permanently dissolved from the date of the order upon application made by the liquidator.

5. How do creditors and other stakeholders rank on an insolvency of a debtor? Do any

stakeholders enjoy particular priority (e.g. employees, pension liabilities)? Could the claims of any class of creditor be subordinated (e.g. equitable subordination)?

First, creditors secured by a fixed charge or mortgage are paid out of the sale proceeds of the asset subject to that charge or mortgage (less the costs of realization). Fixed charges over the same asset rank for priority in the order in which they were created. After that, preferential creditors (such as employees and the government), floating charge holders and liquidator's costs and remuneration are paid. Once preferential creditors have been paid in full, floating charge holders are paid from the proceeds of sale of the asset subject to that floating charge. Floating charges over the same asset rank for priority in the order in which they were created. After the floating charge holders have been paid in full, any surplus is paid to the unsecured creditors, followed by any claims from post-liquidation interest. Any remaining assets are used to repay the shareholders' capital contributions.

In the event that an employment contract is automatically terminated in a compulsory winding up, that employee becomes a preferential creditor of the company in respect of any unpaid wages and severance payments. If an insolvent company does not have sufficient funds to satisfy all unsecured creditors in full, any available funds will be used to satisfy payments to the preferential creditors in full before any amount is paid to the general pool of unsecured creditors. There is no equitable subordination in Hong Kong.

6. Can a debtor's pre-insolvency transactions be challenged? If so, by whom, when and on what grounds? What is the effect of a successful challenge and how are the rights of third parties impacted?

A debtor's pre-insolvency transaction can be challenged by the liquidator to have the following types of transactions set-aside:

(i) Unfair preferences: that is any action taken by the company, influenced by a desire to prefer, and that puts one creditor in a better position in the event of insolvency than it would otherwise have been in. For the transaction to be set aside, it must have been entered into during the six month period before the company winding up is commenced (as defined as the date of the filing of the winding up petition), but this can be

extended to a two year period if the recipient is a person connected with the company. Transactions involving persons connected with the company are presumed to be an unfair preference unless proven otherwise. Such a connected person means any "associate": in respect of individuals (eg, directors), a person is an associate of another person if that person is a spouse or cohabitant of that other person; in respect of companies, a company is an associate of another company if the same person has control of both companies; and a person can be considered as having control of a company if he is entitled to exercise, or control the exercise of, more than 30 percent of the voting power at any general meeting of the company, or of another company which has control of it.

(ii) "Extortionate" extensions of credit to the company: applies to floating charges granted by the company within: (i) two years before the company's winding-up commenced (if granted in favor of a person who is connected with the company); and (ii) within 12 months before the company's winding-up commenced (if granted in favor of a non-connected person). Transactions made with the intention to defraud creditors or for a fraudulent purpose. For example, a transaction can be set aside if the liquidator establishes that it took place with the aim of placing assets beyond the reach of creditors. If the property disposed of is held by a bona fide third party purchaser for value and without notice of the fraud, then the transaction will not be set aside.

(iii) Onerous contracts: the Hong Kong Court has a discretion to grant leave to Liquidators to disclaim "onerous property" within a 12 month time period (or such extended period as granted by the Court), to give effect a rejection of a contract without obligation to recover amounts paid prior to the insolvency proceedings. The categories of what "onerous property" might be disclaimed includes "unprofitable contracts".

(iv) Transactions at an undervalue: a transaction with a person at an undervalue if (for that transaction) the company receives: no consideration; or consideration which is significantly less than the consideration provided by the company. For the transaction to be set aside, it must have been entered into in the five-year period before the company's winding up is commenced. The transaction will not be set aside if the court is satisfied that the company entered into the transaction in good faith and for the purpose of carrying on its business, and there are reasonable grounds for believing that the transaction would benefit the company.

7. What form of stay or moratorium applies in insolvency proceedings against the continuation of legal proceedings or the enforcement of creditors' claims? Does that stay or moratorium have extraterritorial effect? In what circumstances may creditors benefit from any exceptions to such stay or moratorium?

In a compulsory liquidation, at any time after the presentation of a winding-up petition and before a winding-up order has been made, the company or any creditor or contributory may apply to the court for a stay of proceedings in Hong Kong. Once a winding-up order has been made, no action or proceeding can be commenced in Hong Kong against the company without the leave of the court. In some cases, the Court will make an order allowing a creditor to have an advantage over other creditors (such as an assignment of proceeds of claim) in certain circumstances where that creditor has funded, or given an indemnity, in respect of costs of steps taken to protect the company's assets or achieve recoveries. Creditors' voluntary liquidation and members' voluntary liquidation do not have an automatic stay of proceedings, but application for the Court's directions can be made.

8. What restructuring and rescue procedures are available in the jurisdiction, what are the entry requirements and how is a restructuring plan approved and implemented? Does management continue to operate the business and/or is the debtor subject to supervision? What roles do the court and other stakeholders play?

The only formal ways to reorganize a debtor without realizing its assets and business would be through the use of a scheme of arrangement or the appointment of a provisional liquidator, subject to court approval, although the court has stated that provisional liquidators should not be appointed for the sole purposes of restructuring.

A scheme of arrangement is a statutory arrangement between the company and the requisite majority of its creditors. The procedure is available to companies incorporated in or outside Hong Kong so long as the company has a 'sufficient connection' with Hong Kong. Connecting factors may include having creditors located in Hong Kong, a listing on the Hong Kong Stock Exchange and all or part of the management of the company being based in Hong Kong.

The terms of a scheme become binding on those creditors affected by it (including those creditors who voted against it) when: (i) a simple majority in number, representing at least 75% in value of each class of those creditors entitled to do so, vote in person or by proxy in favor of the terms set out in the scheme of arrangement at a specially convened creditors' meeting; (ii) the Court subsequently makes an order approving the terms of the scheme of arrangement; and (iii) an official copy of the court order sanctioning the scheme of arrangement is delivered to the Companies Registry for registration.

During the entire process of a scheme of arrangement, the persons in control prior to the scheme (whether directors, liquidators or receivers) retain the control which they ordinarily have and the shareholders' rights are modified only to the extent that this is provided for in a binding scheme.

9. Can a debtor in restructuring proceedings obtain new financing and are any special priorities afforded to such financing (if available)?

A company subject to insolvency proceedings can obtain post-petition financing. A liquidator may obtain new financing on the security of the company's assets and priority of such security will be determined under the general rules on creditor claims' priority. In the case where a provisional liquidator is appointed, court direction may be required to obtain post-petition financing, if his/her appointment has not been conferred such powers.

A liquidator also has the power to sell or assign a cause of action to a litigation funder. However, this power of sale only applies to causes of action vested in the company, rather than the liquidator personally.

10. Can a restructuring proceeding release claims against non-debtor parties (e.g. guarantees granted by parent entities, claims against directors of the debtor), and, if so, in what circumstances?

A scheme of arrangement can also effect releases of unsecured claims against non-debtor parties. Such claims against third party guarantors may be released or amended by the scheme if necessary for the successful operation of the scheme of arrangement.

11. Is it common for creditor committees to

be formed in restructuring proceedings and what powers or responsibilities do they have? Are they permitted to retain advisers and, if so, how are they funded?

The committee of inspection is appointed and formed in the case of creditors' voluntary liquidation and compulsory liquidation, at a meeting of creditors and is intended to be representative of the creditors of the company and capable of taking decisions in the interests of all creditors. The primary responsibility is to provide assistance and guidance to the liquidator in the performance of his duties (including appointment of advisers), to approve the exercise of certain powers by the liquidator in accordance with the terms of the Companies Ordinance and to approve the liquidator's remuneration. No creditor committees are required to be formed as part of a scheme of arrangement proceedings.

Ad hoc committees of creditors (usually bank groups, or bondholders groups) are often set up, to coordinate among themselves and the debtor on the implementation of an out of court workout. These ad hoc committees would usually have legal and financial advisers and may be funded by the respective creditors as part of the overall workout plan.

12. How are existing contracts treated in restructuring and insolvency processes? Are the parties obliged to continue to perform their obligations? Will termination, retention of title and set-off provisions in these contracts remain enforceable? Is there any ability for either party to disclaim the contract?

The contracts of a company do not automatically terminate on the commencement of any kind of liquidation, subject to the liquidator's powers to avoid certain transactions (see above) and to disclaim onerous property, which includes unprofitable contracts. The only exception is employment contracts. In a compulsory liquidation all employment contracts will be automatically terminated by the winding-up order, unless ordered otherwise by the court.

13. What conditions apply to the sale of assets / the entire business in a restructuring or insolvency process? Does the purchaser acquire the assets "free and clear" of claims and liabilities? Can

security be released without creditor consent? Is credit bidding permitted? Are pre-packaged sales possible?

There is no specific legal framework (and no administration framework in Hong Kong) for pre-packaged sales of asset/business in Hong Kong and it is possible for asset sales to be incorporated as part of a scheme of arrangement.

A liquidator can sell asset free and clear of claims and liabilities. In cases where a provisional liquidator seeks to sell assets or conduct transactions outside the scope of his appointment, court sanction or directions would normally be obtained. Hong Kong law is not prescriptive on how a liquidator is to dispose of the asset. In general terms, a court-appointed liquidator is required to investigate the affairs of the company in order to get in and realize its assets, before applying those realizations in discharge of the company's liabilities, which will include investigating the conduct of the company's past and present office holders to consider whether any wrongful conduct or criminal offense has been committed against the company.

14. What duties and liabilities should directors and officers be mindful of when managing a distressed debtor? What are the consequences of breach of duty? Is there any scope for other parties (e.g. director, partner, shareholder, lender) to incur liability for the debts of an insolvent debtor?

Fiduciary duties: directors (and shadow directors, a person in accordance with whose directions the directors,) owe fiduciary duties: (i) to act bona fide for the benefit of the company; (ii) to exercise their powers for their proper purpose; and (iii) not to allow any conflict between their duties as directors and their personal interests.

Duty of care and skill: a director need not, in the performance of his duties, exhibit a greater degree of skill than may reasonably be expected from his knowledge and experience, but he will be judged both objectively and subjectively. Such duty applies to a shadow director.

Duties to the company's creditors: the directors must have regard to the interests of the company's creditors where the company is insolvent.

A director can be ordered to repay the company

amounts transferred which is the subject of a successful preference claim, or to compensate the company for its losses by way of damages or equitable compensation. He may also be disqualified if a court considers his conduct makes him unfit for management or otherwise guilty of fraud. Disqualification orders prohibiting a person to be a director in Hong Kong can be made for a period between one and 15 years. If in the course of the winding up it appears that any business has been carried on with fraudulent intent, the court may declare that any persons who were knowingly parties are personally liable for all or any of the company's debts and criminally liable to a fine and imprisonment of up to five years.

With the recent case of *Moulin Global Eyecare Holdings Limited v Olivia Lee Sin Mei* [2019] HKCFI 1715, directors can now be found liable for breaching their duty of care and skill if they fail to properly investigate red flags concerning the solvency of the company. Hong Kong courts have found in favor of the liquidators and held that a non-executive director breached her duty of care and was personally liable for the company losses, as she had acquired knowledge that should have caused her serious concern and prompt further investigation.

A partner will be personally liable for the debts of an insolvent company if they have provided a personal guarantee. A parent company (domestic or foreign) is a separate legal entity and, unless it has provided a guarantee or has been involved in fraudulent conduct, will not be liable for the debts of an insolvent subsidiary.

15. Do restructuring or insolvency proceedings have the effect of releasing directors and other stakeholders from liability for previous actions and decisions?

There is no automatic release for directors or other stakeholders when a company enters an insolvency or restructuring process. In practice, liquidators are required to investigate the conduct of the company's past and present office holders to consider whether any wrongful conduct or criminal offense has been committed against the company and should not be in a position to enter into any arrangement to release directors and other stakeholders from pre-petition liability.

16. Will a local court recognise concurrent foreign restructuring or insolvency proceedings over a local debtor? What is the process and test for achieving such

recognition? Has the UNCITRAL Model Law on Cross Border Insolvency or the UNCITRAL Model Law on Recognition and Enforcement of Insolvency-Related Judgments been adopted or is it under consideration in your country?

There are no statutory provisions dealing with the recognition of foreign restructuring or insolvency proceedings in Hong Kong. However, when a foreign company is in liquidation in its country of incorporation, it may be possible to obtain a winding up order in Hong Kong ancillary to that being conducted abroad. The Hong Kong liquidator will generally be responsible for realizing the Hong Kong based assets and paying over those assets to the principal liquidators abroad pursuant to the court order. Similarly, and under principles of international comity, the Hong Kong courts will, in certain circumstances, recognize insolvency procedures and orders made by foreign courts against a local debtor. Problems often arise in Hong Kong in relation to the insolvency and restructuring of mainland Chinese companies, as there is no formal arrangement for recognition of insolvency procedures between Hong Kong and China (the Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters between the Courts of the Mainland and of the Hong Kong SAR does not apply to insolvency cases).

The UNCITRAL Model Law on Recognition and Enforcement of Insolvency-Related Judgments has not yet been implemented in Hong Kong. However, recently Hong Kong courts granted recognition order in favor of foreign liquidators appointed in an insolvent liquidation commenced by a shareholder resolution and appears willing to provide assistance in appropriate circumstances. It is also understood that the government is considering conducting a standalone consultation on reciprocal enforcement for cross-border insolvency matters between Hong Kong and mainland China.

17. Can debtors incorporated elsewhere enter into restructuring or insolvency proceedings in the jurisdiction?

Notwithstanding the unavailability of the UNCITRAL model law, the court may exercise its discretion to make a winding up order against a foreign company if, amongst other requirements, there is sufficient connection within the jurisdiction of Hong Kong. For a foreign company incorporated outside Hong Kong, whether it is possible to have provisional liquidators appointed in its jurisdiction of incorporation for the purpose of facilitating a corporate restructuring will

depend on the law of that jurisdiction. The Hong Kong court may grant a winding up order against a foreign company if it is satisfied and there are good reasons to exercise discretionary statutory jurisdiction to wind up such company. The three core requirements for exercise of such discretion include (i) sufficient connection with Hong Kong; (ii) reasonable possibility that the winding-up order would benefit those applying for it; and (iii) the court must be able to exercise jurisdiction over one or more person in the distribution of the company's assets. If provisional liquidators are appointed to a foreign company where it was incorporated, and the provisional liquidators would like their appointment to be recognized in Hong Kong, they can obtain a letter of request from the court of the jurisdiction where they were appointed, and then apply to the Hong Kong court for an order to this effect.

18. How are groups of companies treated on the restructuring or insolvency of one of more members of that group? Is there scope for cooperation between office holders?

There is no group company concept in Hong Kong. In a winding up of a group of companies, each company is treated as a separate legal entity. However, a court may permit the same liquidator to take control of insolvent debtors within a group, subject to any conflict of interest.

19. Is it a debtor or creditor friendly jurisdiction?

Hong Kong operates a generally creditor-friendly approach to insolvency but without the benefit of any statutory corporate rescue procedures (such as administration). Recently the government has announced a new round of consultations for the introduction of US Chapter 11 style corporate rescue laws to shield companies from liquidation while they attempt to restructure. (also see response to Question 21 below).

20. Do sociopolitical factors give additional influence to certain stakeholders in restructurings or insolvencies in the jurisdiction (e.g. pressure around employees or pensions)? What role does the state play in relation to a distressed business (e.g. availability of state support)?

Hong Kong serves as a major center for financial services in the North-East Asia region and gateway to mainland China, attracting capital markets activity supported by its geopolitical position and its cross border treaty arrangements with mainland China. Given the number of enterprises wishing to access the equity capital markets in Hong Kong, there is an active market and premium paid for a debtor's listing status, which has been a source of recovery for many distressed debtors listed in Hong Kong. This allows the distressed debtor to issue new shares to a white knight investor and in return, the underlying business revived or cash / asset injected to satisfy re-listing requirements (coupled with a scheme of arrangement). While it is argued that the result of allowing "restructuring" of distressed debtor by allowing a new investor to "acquire" the listing status of a distressed listed debtor and generate a substantial recovery for creditors and shareholders, the regulators have heavily resisted this and adopted strict policy to disallow this practice by claiming this contravene "backdoor listing" principles". The lack of a single unified regulator for listed enterprises in Hong Kong (unlike in the US and Australia) also adds challenges in restructuring distressed listed companies.

21. What are the greatest barriers to efficient and effective restructurings and insolvencies in the jurisdiction? Are there any proposals for reform to counter any such barriers?

In the absence of a voluntary agreement between the company and all of its creditors, a company in Hong Kong only has recourse to a scheme of arrangement or a provisional liquidation. In 2001, the Companies (Corporate Rescue) Bill was introduced into the Legislative Council. The proposals did not proceed, mainly because of the concerns of various stakeholders relating to employment law.

The current proposal to reform the current insolvency law includes (i) statutory provision for insolvent or wrongful trading, making directors and senior management personally liable for the debts of a company which traded while insolvent; and (ii) provisional supervision, a formal turnaround and rescue regime that could be initiated by a company or its directors or provisional liquidators or liquidators, but not the company's creditors. It would give the debtor company a moratorium period during which civil proceedings against the company would be stayed, thus giving valuable time to the provisional supervisor to work towards a possible turnaround of the business, whilst freed up from the threat of creditor action.

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