The Hong Kong Court Reconsiders the Primacy of the Jurisdiction of Incorporation in Cross-Border Insolvency Proceedings

March 19, 2021

In *Re Lamtex Holdings Limited*[1], the Hong Kong Companies Court recently ordered the winding-up of a Bermuda-incorporated Hong Kong-listed company. While the winding-up in Hong Kong of a foreign-incorporated company is not novel, the company in this case—with businesses in Hong Kong and Mainland China—had already been placed into "soft-touch" provisional liquidation in Bermuda, its jurisdiction of incorporation. The Hong Kong winding-up petition therefore raised, in Mr. Justice Harris' words, an "issue of some importance in the development of the principles which guide the Hong Kong Court in dealing with cross-border insolvency and, in particular, cross-border debt restructuring."

The decision, which marks an evolution in the Hong Kong common law principles applicable to cross-border insolvencies, is explored in this update.

The Facts

Lamtex Holdings Limited was a Bermuda-incorporated, Hong Kong-listed company that operated a number of businesses in Mainland China and Hong Kong. The company's center of main interest (COMI) was Hong Kong, and nearly all of Lamtex's creditors were Chinese nationals resident in Mainland China. None of those creditors objected to the Hong Kong winding-up petition.

On July 2, 2020, a creditor of Lamtex presented a winding-up petition in Hong Kong in respect of an undisputed debt. Subsequently, on October 30, 2020, Lamtex presented a winding-up petition in Bermuda and sought the appointment of soft-touch provisional liquidators.

Following their appointment, the provisional liquidators sought recognition and assistance in Hong Kong and an adjournment of the Hong Kong winding-up petition to give the company breathing room to progress a restructuring.

The question for the Hong Kong Companies Court was whether the provisional liquidation in Bermuda (the place of Lamtex's incorporation) should be afforded

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primacy with the result that the Hong Kong winding-up petition should be adjourned so that a restructuring could be pursued under the Bermudan procedure.

The Applicable Legal Framework and the Contest for Primacy

The common law doctrine of "modified universalism" guides the Hong Kong Court when determining cross-border issues arising in transnational insolvencies. As traditionally applied in Hong Kong, the doctrine provides that the place of incorporation of a company should be the system of distribution in an insolvency context and that a winding-up of a foreign company's assets in Hong Kong should be ancillary to that.

The consequence is that local winding-up proceedings in Hong Kong would be stayed in favor of foreign proceedings opened in the company's place of incorporation.

As part of revisiting the rationale for such an approach, the Court gave detailed consideration to the scope of the common law jurisdiction in Hong Kong to recognize and grant assistance to insolvency officeholders appointed outside Hong Kong. Consistent with modified universalism and the position at common law in England, such officeholders recognized to date in Hong Kong have been limited to those appointed in the company's jurisdiction of incorporation.

The Court compared this restrictive approach with the position in other jurisdictions that have adopted the UNCITRAL Model Law on Cross-Border Insolvency (Model Law), as well as Singapore, where the common law had developed in a different direction to England prior to its adoption of the Model Law. In such jurisdictions, officeholders appointed in the location of a company's COMI may be recognized and granted assistance.

The Court questioned whether the restrictive approach in Hong Kong is appropriate having regard to the prevailing commercial reality that many companies in Hong Kong have little connection with their jurisdiction of incorporation, which is typically in the Caribbean or Bermuda. As the Court observed, "What appears to have happened over the course of the last 20 years or so is that many Mainland businesses have been permitted to list in Hong Kong using corporate vehicles incorporated in jurisdictions which have no connection with either Hong Kong or the Mainland."

The Court accepted that it had become desirable, if not essential, for the Hong Kong Court to be able to address recognition of insolvency officeholders in a manner consistent with commercial practice in Hong Kong and Mainland China. Further, there was no doctrinal reason why the common law in Hong Kong could not be adapted to extend to the recognition of insolvencies in places other than a company's jurisdiction of incorporation—a possibility previously mooted, but left undecided, by the Court.[2]

This was tangential to the issue raised in *Re Lamtex*, but it was held that, if COMI is accepted as a basis for recognition, then in a contest for recognition between insolvency proceedings in the jurisdiction of the company's incorporation and its COMI (i.e., the issue in *Re Lamtex*), there would be less reason to give primacy to the place of incorporation.

The Court observed that there would still be many cases where local Hong Kong proceedings should be stayed in favor of foreign proceedings in order to preserve a unitary global insolvency process and distribution, but not where the foreign proceeding comprises a soft-touch provisional liquidation being managed out of Hong

Kong and used to circumvent the problems created by the absence in Hong Kong of a formal insolvency process for reorganization.

The Court also referred to certain factors that could make it appropriate for the place of incorporation to be the primary insolvency jurisdiction. These include a situation where an offshore jurisdiction sitting at the apex of a corporate group whose assets and operations are in the Mainland would be reluctant to recognize a Hong Kong winding-up order. Other factors would include principles of comity and of fairness.

With respect to the latter, Mr. Justice Harris observed that, if the requirements for winding-up a foreign company in Hong Kong are satisfied, as they were in the present case, then, "it is not in my view sufficient for the Company simply to point to insolvency proceedings commenced sometime after the Hong Kong Petition was presented in its place of incorporation and request in the face of objection from local creditors this court simply to defer to that of the place of incorporation. It seems to me unrealistic to expect the court not to have regard to the fact that companies such as the present conduct business in the People's Republic of China which commonly is also the location of a high proportion of their shareholders, creditors and assets."

The Approach to Be Taken in Future Cases

In light of the authorities considered, the Court proposed the following framework to address questions of primacy with respect to insolvency proceedings opened in different jurisdictions:

> "1. Generally, the place of incorporation should be the jurisdiction in which a company should be liquidated; in practice, this means it will be the system for distributions to creditors.
>
> 2. However, if the COMI is elsewhere regard is to be had to other factors:
>
> A. Is the company a holding company and, if so, does the group structure require the place of incorporation to be the primary jurisdiction in order effectively to liquidate or restructure the group.
>
> B. The extent to which giving primacy to the place of incorporation is artificial having regard to the strength of the COMI's connection with its location.
>
> C. The views of creditors."

As the framework suggests, the Court confirmed that an assessment will turn on the circumstances of a particular case and involve giving appropriate weight to the location of a company's COMI. Further, the views of creditors would be a "major consideration."

The Outcome in *Re Lamtex*

On the facts in *Re Lamtex*, the Court declined to adjourn the Hong Kong winding-up petition and instead made its usual winding-up order. The Court observed, among other things, that it was not disputed that the company's COMI was Hong Kong and that the usual test for determining whether to wind-up a foreign company in Hong Kong (comprising the so-called three core requirements) was met in this case. The Court also observed that no creditor had appeared to oppose the petition and that no

good reason had been demonstrated to adjourn the petition (the available information about a restructuring was described as being “scanty in the extreme”).

Observations

The decision in *Re Lamtex* represents an important evolution in cross-border insolvency law and practice in Hong Kong. The focus on a company’s COMI in the context of assessing the primacy of competing insolvency proceedings is likely to have a significant impact in a jurisdiction where many Hong Kong and Mainland Chinese corporate groups are structured under a Hong Kong-listed offshore holding company with little connection to the businesses of the group. The focus on COMI is also pertinent in Hong Kong given that Hong Kong has not yet adopted the Model Law and currently has no statutory framework for dealing with cross-border insolvency matters.

The decision also casts a spotlight on the tactical use in certain cases of soft-touch provisional liquidation. It appeared to the Court that the petition in Bermuda and application to appoint soft-touch provisional liquidators was part of an effort to avoid a winding-up in Hong Kong and “engineer a de facto moratorium, which could not be obtained under Hong Kong law, with a view to then searching for a solution to the Company’s financial problems.”

The Court observed that this was a questionable use of soft-touch provisional liquidation that would encourage the Court to view with care similar applications in the future. The key practical take-away in the words of Mr. Justice Harris was as follows: “Going forward I anticipate that unless the agreement of a petitioner and supporting creditors have been obtained in advance the court will not deal with recognition and assistance applications made by soft-touch provisional liquidators after a winding up petition has been presented in Hong Kong on the papers.”

Indeed, a decision just one day later in *Re Ping An Securities Group (Holdings) Ltd*[3] likewise involved consideration of a Hong Kong winding-up petition where Bermuda-appointed soft-touch provisional liquidators had already been appointed. Mr. Justice Harris referred to his decision in *Re Lamtex* and to the possibility of an immediate winding-up of the relevant Bermuda-incorporated company in Hong Kong, but decided not to make an immediate winding-up order on the facts.

[1] [2021] HKCFI 622.

[2] *Joint Administrators of African Minerals Ltd v Madison Pacific Trust Ltd* [2015] HKEC 641.

[3] [2021] HKCFI 651.

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