

Further clarification on the impact of foreign insolvency proceedings

July 13, 2021

A 2020 decision of Mr Justice Harris¹ concerned FDG Electric Vehicles Limited (the **Company**), a company which has been put into provisional liquidation in Bermuda, where it was incorporated. The Joint and Several Provisional Liquidators (the **Provisional Liquidators**) applied to the Hong Kong court for an order of recognition and assistance (the **Application**).

In considering the Application, the court identified two issues which required further consideration:

- Should the order contain a paragraph, which on its face gives the Provisional Liquidators the power to take control of all directly and indirectly owned subsidiaries of the Company?
- What, if any, stay should be ordered in respect of existing or prospective proceedings against the Company in Hong Kong?

Limitation of control of the Provisional Liquidators

Generally, when the court recognises foreign insolvency proceedings, it may permit the provisional liquidator to take control of a company's assets in Hong Kong. Pursuant to a decision of Mr Justice Harris earlier this year², this would also include allowing liquidators to present a winding-up petition against a Hong Kong company, as a claim against a Hong Kong incorporated debtor should be regarded as an asset in Hong Kong, and an action to realise the value of such asset will generally be properly commenced in Hong Kong.

However, in this case the Provisional Liquidators were seeking the power to take control of subsidiaries of the Company incorporated in jurisdictions other than Hong Kong.

It was ultimately accepted by the Provisional Liquidators that the power to take control of subsidiaries should be limited to those which are incorporated in Hong Kong and held either directly or, if indirectly, through intermediate subsidiaries incorporated in Hong Kong. Whether the provisional liquidators are able to obtain control of subsidiaries in other jurisdictions would be a question of law in that jurisdiction, not Hong Kong law.

No automatic stay of proceedings in Hong Kong

The court has a power at common law to assist a foreign liquidation by ordering a stay of proceedings within its jurisdiction. The underlying rationale for such power is modified universalism, which requires the court to, so far as is consistent with justice and public policy, co-operate with the courts in the country of the principal liquidation to ensure that all of the company's assets are distributed to its creditors under a single system of distribution.

Recognition orders normally contain a paragraph which provides that, where a company remains in liquidation in

foreign insolvency proceedings, no action or proceedings shall proceed or commence in the jurisdiction of Hong Kong except with leave of the Hong Kong court.

The court commented that such a provision is intended to ensure that action would not take place in Hong Kong without the relevant parties being aware of the foreign insolvency proceedings and, if appropriate, a stay granted. Such a provision would not impose an automatic stay, for example, on proceedings already under way in Hong Kong or unidentified prospective proceedings. Rather, an application would need to be made and heard before the judge granting the recognition order.

As such, Mr Justice Harris therefore granted an order in line with a recent recognition and assistance decision in the Cayman Islands, whereby liquidators must apply for a stay instead.

The court noted that many of the previous applications have not been made by liquidators to assist collective insolvency processes and to ensure that a company's assets are distributed to its creditors under a single system of distribution. Rather, many of them have been made by provisional liquidators appointed in the place of incorporation on a soft-touch basis with a view to facilitating a restructuring of a company's debt using a scheme of arrangement introduced in both the jurisdiction of incorporation and Hong Kong.

The fact that the courts have found that the common law principles support assisting a soft-touch provisional liquidation does not mean that the courts have accepted that a foreign soft-touch provisional liquidation is for all purposes to be treated as a collective insolvency process. It is therefore not clear, if the foreign proceedings have a different character, whether a stay can be justified, where such stay is arguably not granted in aid of collective insolvency processes.

As the court was not required to consider this on this occasion, we await further clarification.

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1. *FDG Electric Vehicles Ltd* [2020] HKCFI 2931↔
 2. *Re Joint Liquidators of Nuoxi Capital Ltd* [2021] HKCFI 572↔

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