AN UNCERTAIN FUTURE? ASSESSING THE HONG KONG COURT'S RECEPTION OF CAYMAN INSOLVENCY PROCEEDINGS

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There has been increasing debate among Cayman Islands attorneys and insolvency practitioners about the Hong Kong High Court's (**HK Court**) ongoing preference for a company's Centre of Main Interest (**COMI**) over its place of incorporation when assessing whether and to what extent it should recognise and assist foreign insolvency proceedings. Discussions have ensued on the effect that modified approach will have on the HK Court's recognition of and assistance to Cayman-appointed provisional liquidators and (more significantly for future proceedings) restructuring officers[1].

Several panel sessions at the American Bankruptcy Institute's (**ABI**) Caribbean Insolvency Symposium, hosted in Grand Cayman on 6 and 7 February 2023, raised the HK Court's approach as a point of interest. The approach had been brought into greater focus following comments made by Mr. Justice Harris during an International Insolvency Institute (III) podcast about a week before.

A jurisdiction choosing COMI over the place of incorporation when determining whether to recognise a foreign liquidator and to what extent it should be assisted, is not in itself controversial. It is the criterion employed by jurisdictions signed up to the UNCITRAL Model Law, which includes England and Wales.

However, two factors render the HK Court's repositioning especially relevant for Cayman Islands attorneys and insolvency practitioners.

Firstly, as at June 2022, more than half of the companies listed on the Hong Kong Stock Exchange – approximately 1,195 entities – are incorporated in the Cayman Islands. Even if a modest percentage of these need to restructure their financial obligations, this equates to a significant number of companies that may wish to impose an extraterritorial moratorium on claims being made against them by appointing light-touch provisional liquidators or (more likely) filing for the appointment of a restructuring officer. If the success of a restructuring requires the recognition and assistance of the HK Court, a shift to a COMI-based test, and a more limited approach by the HK Court to the assistance it will provide light-touch liquidators, both cast a degree of uncertainty over the cross-border implementation of that restructuring.

Secondly, it remains to be seen, hopefully in the not too distant future, what treatment a Cayman-appointed restructuring officer will receive from the HK Court in light of recent decisions and the views expressed by members of its judiciary.

The emergence of COMI – from Z-Obee to Global Brands

When considering the HK Court's current approach to recognising foreign insolvency proceedings commenced in the place of incorporation, there is a consistent point of principle which emerges from the recent decisions when the restructuring plans presented to the HK Court are considered through the lens of viability. The relative ubiquity of that point of principle in the decisions between *Z-Obee* and *Global Brands* should give Cayman attorneys and practitioners hope that the outlook is not as negative as they may have initially thought.

The journey begins with what some may, unfairly, now consider the original sin; the case of *Re Z-Obee Holdings Limited*[2], which bequeathed the "Z-Obee technique", whereby companies (invariably incorporated in the BVI, Cayman Islands or Bermuda) would appoint light-touch provisional liquidators in the place of incorporation, then seek recognition and assistance from the HK Court with a view to staving off a winding-up petition brought in Hong Kong and/or implementing a restructuring scheme.

The winds of change began to blow in *Re FDG Electric Vehicles Ltd*[3], when Mr. Justice Harris held that recognition of a Bermudan provisional liquidation would not entail an automatic stay of proceedings in Hong Kong. Furthermore, in *Re China Huiyuan Juice Group Limited*[4], decided only 16 days later, Mr Justice Harris remarked upon the popularity of the Z-Obee technique:

"*Remarkably petitions to wind-up Hong Kong incorporated companies operating domestic businesses are currently a minority. In addition I have received weekly applications for recognition and assistance by soft-touch provisional liquidators of companies incorporated in one of the offshore jurisdictions and listed here intending to use the Z-Obee technique…*"[5]

In March 2021, through *Re Ping An Securities Group (Holdings) Limited*[6](*"I have reached the stage at which I am increasingly concerned about the way soft-touch provisional liquidation, and what is generally referred to as the Z-Obee technique, is being used.*"[7]) and *Re Lamtex Holdings Limited*[8](*"Viewed from a Hong Kong perspective this is a questionable use of soft-touch provisional liquidation…*"[9]) Mr. Justice Harris expressed his concerns that the Z-Obee technique was being abused by offshore-incorporated companies to stave off the threat of liquidation on the basis of unrealistic restructuring proposals.

His concerns were further enunciated just a couple of months later in *Re China Bozza Development Holdings Limited*[10], where he commented that "*…the court needs to supervise closely the use of the Z-Obee technique to avoid it being misused by professionals more concerned with generating fees than the interests of creditors*"[11]. In *China Bozza*, Mr. Justice Harris granted the provisional liquidators recognition on the basis they had been appointed by the courts in the place of the company's incorporation. However, an order for assistance in standard terms was refused and it was reiterated that a winding-up petition in Hong Kong would not be adjourned simply because provisional liquidators had been appointed in the place of incorporation.

Having recognised mainland Chinese reorganisation proceedings based on place of incorporation in *Re HNA Group Co., Limited*[12], the HK Court indicated that it would also have been possible to recognise the proceedings based on the company's COMI, in line with the approach it suggested it would adopt in *Re Lamtex.*

From what started as a concern that the Z-Obee technique was being abused at the expense of those with real economic interests in the subject company, there was, in the case of *Provisional Liquidator of Global Brands Group Holding Ltd v Computershare Hong Kong Trustees Ltd*[13] in June 2022, a sea change in the approach the HK Court said it would take in its common law recognition of foreign insolvency proceedings. Mr. Justice Harris held that COMI should dictate the terms of the HK Court's recognition of the foreign

office-holder in the future, relegating the place of incorporation to a clear runner-up[14].

Global Brands does not mean that seeking the recognition of the HK Court on the basis of place of incorporation will be a forlorn exercise. However, the breadth of the recognition and assistance sought will have to be tailored in the application for it to be granted. Mr. Justice Harris indicated that if the liquidator were appointed in the place of incorporation, then the recognition and assistance will be limited to that to which a liquidator is entitled by virtue of its authority to represent the company – "*managerial assistance*." Should an office-holder seek anything outside that category, it would have to be required "*as a matter of practicality*".

What the foreign-appointed liquidator should not expect as a matter of course is the granting of any powers which extend beyond those arising from the recognition of the liquidator's status and rights resulting from its appointment in the place of incorporation.

A common thread running through most of the decisions that saw the HK Court challenge the use of soft-touch liquidations is the lack of viability in the scheme or restructuring proposal underpinning the application for recognition. In *Re Ping An,* Mr Justice Harris lamented the "*entirely unsatisfactory*"[15] manner in which the restructuring plan, as described to him and relied upon by him in deciding to adjourn the winding-up petition, had been progressed during the adjournment. In *Re Lamtex*, the information regarding the restructuring plan was deemed "*scanty in the extreme*"[16]. In *Re China Bozza,* Mr. Justice Harris found that there was "*no evidence that the Board had anything one could sensibly describe as a plan to restructure the Company's debt or business*"[17].

It appears that, from the HK Court's perspective, the viability of the presented scheme or proposal should influence both the decision whether to recognise the foreign office-holder, and the extent of assistance given, and this reflects the HK Court's focus on safeguarding the interests of stakeholders within its jurisdiction. The more cogent the plans are, the more amenable the HK Court may be to offer practical, rather than managerial, assistance.

The COMI criteria and when they apply

Mr. Justice Harris looked to Judge Glen in *In re Ocean Rig UDW Inc.*[18] for criteria which will factor into a determination on COMI. The criteria are non-exhaustive but include:

- the location of directors and board meetings;
- the location of the company's principal officers;
- notices of relocation to the Cayman Islands;
- the location of operations;
- the location of assets;
- the location of bank accounts;
- the location of books and records; and
- the location in which the restructuring activities took place.

In terms of when those criteria will be considered, Mr. Justice Harris indicated a preference for the date on which the application for recognition is made.

Since Global Brands

The landscape has further developed since *Global Brands* following the decision in *Silver Base Group Holdings Limited*[19], in which Mr. Justice Harris recognised that the liquidators appointed in the Cayman Islands had "*partly*" been influenced by his *Global Brands* decision in their choice to forego applying for recognition and accepting that the company should be wound up in Hong Kong.

Those same liquidators had had in mind an application for the "managerial" type of assistance described in *Global Brands*. Mr. Justice Harris indicated that the HK Court's openness to allow a recognition of that ilk was conditional upon the company not already being in liquidation in Hong Kong. He then posed the following questions which may give liquidators appointed in the place of incorporation cause to pause before seeking the HK Court's assistance in circumstances where the company in question is in liquidation in Hong Kong:

1. "*What, if any, recognition should be granted to a foreign liquidator appointed in the place of incorporation (if it is not the COMI) if the company is wound up in Hong Kong? In such circumstances should the Hong Kong court proceed on the basis that within its jurisdiction only the Hong Kong appointed liquidator is the duly authorised agent of the company*?";
2. "*Should [the fact that a liquidation outside the place of incorporation is treated as ancillary] be the case if the place of incorporation is not the COMI and the reality is, as is commonly the case with letter box jurisdictions, that a company's connection with it is formal and it has no assets, creditors or debtors located there*?"[20]

It remains to be seen what level of assistance foreign office-holders appointed in the place of incorporation could expect from the HK Court where the company's COMI is Hong Kong and there is already a winding up underway in Hong Kong.

In the *Matter of RZ3262019 Limited*[21], notably not a case where there was already a winding up progressing in Hong Kong, the BVI-appointed provisional liquidators were cognisant of the type of recognition and assistance they could seek from the HK Court and applied successfully for the "managerial" variety of assistance and recognition justified by the established principles of private international law.

Conclusion

It is vitally important to the success of the Cayman Islands' restructuring officer regime that there be a semblance of certainty as to whether and to what extent the scheme will be recognised and assisted by courts in jurisdictions integral to the fabric of the debtor company. We hope that it is not long before a restructuring officer has cause to appear before the HK Courts so that Cayman Islands practitioners can gauge what reception future restructuring officers may receive.

There have only been two restructuring officer appointments by the Cayman Islands Court to date – over Oriente Group Limited and Rockley Photonics Holdings Limited. In the former, a creditors' petition to wind up the company has been filed in Hong Kong but has not been heard as yet. Arbitration proceedings against the company have also been commenced. We must wait and see if the winding up petition is advanced and if so, how the HK Court proceeds as a result.

In the case of *Rockley Photonics*[22], the application for appointment of the restructuring officers states an intention to present the

restructuring plan to creditors for approval pursuant to the United States Bankruptcy Code. This means that it may not be long before we read of the U.S. Court's reaction to an application for recognition of a restructuring officer and the restructuring plan.

There is optimism within the Cayman Islands legal and insolvency community that recognition of and assistance to a restructuring officer will be forthcoming from the HK Court. The first of the two-pronged test for a foreign insolvency proceeding to be recognised – that it must be a "collective insolvency proceeding" – should be surmountable. It then comes down to whether the second prong – formerly that the collective insolvency proceeding be commenced in the company's place of incorporation – has been altered and to what extent that alteration will affect the level of assistance to be given, including the treatment of the moratorium.

As has been amply demonstrated in the cases referred to above addressing offshore provisional liquidations, we expect the HK Court to be no less vigilant on the viability of a scheme of arrangement proposed by a restructuring officer than it has been when considering the plans and schemes proposed by soft-touch provisional liquidators.

Just as we would advise in the context of a provisional liquidator seeking recognition and assistance in Hong Kong, we would recommend that a restructuring officer be armed with as comprehensive and viable a scheme or proposal as possible when making its application.

[1] A reference to the regime introduced by amendments to the Companies Act permitting the appointment of restructuring officers, further details of which can be found here.

[2] [2018] 1 HKLRD 165]

[3] [2020] HKCFI 2931

[4] [2020] HKCFI 2940

[5] *China Huiyan Juice* at [55]

[6] [2021] HKCFI 651

[7] *Re Ping An* at [5]

[8] [2021] HKCFI 622

[9] *Lamtex* at [42]

[10] [2021] HKCFI 1235

[11] *China Bozza* at [22]

[12] [2021] HKCFI 2897

[13] [2022] HKCFI 1789

[14] See also here our article on the role that the Global Brands decision may play in the context of a scheme seeking recognition in jurisdictions other than Hong Kong, for example the United States.

[15] *Re Ping An* at [4]

[16] *Lamtex* at [42]

[17] *China Bozza* at [6]

[18] 570 B.R. 687 (Bankr. S.D.N.Y. 2017)

[19] [2022] HKCFI 2386

[20] *Silver Base* at [3]

[21] [2022] HKCFI 3602

[22] FSD 16 of 2023

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