

Hong Kong Court Recognises PRC Reorganisation for the First Time

The decision raises new questions about whether cross-border insolvency recognition and assistance between mainland China and Hong Kong will be a two-way street.

The Hong Kong court has for the first time recognised the reorganisation proceedings of a company based in mainland China. The order for recognition granted wide-ranging powers to the mainland-appointed administrators to facilitate the preparation of a reorganisation plan encompassing the assets and creditors of the HNA Group based in Hong Kong. This continues a recent trend of the Hong Kong court to accommodate requests for recognition and assistance without the need for reciprocity from the requesting court. Whether this level of cooperation will pave the way for reciprocity from mainland courts with respect to Hong Kong-initiated proceedings remains to be seen. This *Client Alert* considers recent decisions in this area and analyses the implications for future cross-border restructurings.

Background to recognition

The HNA Group is based in Hainan province, where it had applied successfully to the provincial court to seek a bankruptcy reorganisation on the grounds of its insolvency pursuant to Chapter 8 of the People's Republic of China (PRC) Enterprise Bankruptcy Law. The Hainan court appointed a group of administrators with the responsibility of managing the assets and business affairs of the 60-plus member companies of the group. The administrators applied to the Hainan court for it to send a letter of request to the Hong Kong court seeking recognition of the mainland reorganisation in Hong Kong.

The Hong Kong court considered three key issues before acceding to the administrators' request:

- Was the process seeking recognition a collective insolvency process?
- Had the foreign insolvency process been opened in the company's country of incorporation or where it had its centre of main interests (COMI)?
- Did the exclusion of Hainan from the cooperation agreement signed between the Hong Kong Secretary of Justice and the PRC's Supreme People's Court (SPC) on 14 May 2021 (the Cooperation Agreement) preclude recognition on the basis of lack of reciprocity? The Cooperation Agreement covers only the pilot areas of Shanghai, Xiamen, and Shenzhen.

The court swiftly dispensed the first two issues. Despite Hong Kong's lack of a similar rehabilitation procedure, the judge was satisfied that the mainland reorganisation process was a collective insolvency

process because of its inclusion of all as opposed to a subset of the company's creditors. And since HNA was incorporated in the mainland, the second question was not in doubt. Regarding the third issue, although Hainan was not a signatory to the Cooperation Agreement, the court held that reciprocity was not a requirement under the common law for recognition and assistance in Hong Kong.

Scope for mutual recognition?

The Hong Kong court's decision extends the recent line of Hong Kong case law recognising mainland liquidators predating the Cooperation Agreement to reorganisation proceedings (*Re CEFC Shanghai International Group Ltd* [2020] HKCFI 167 and *Re Shenzhen Everich Supply Chain Co Ltd* [2020] HKCFI 965).

Whether the PRC courts would recognise outbound recognition applications from Hong Kong is uncertain. The accompanying opinion to the Cooperation Agreement from the SPC requires the COMI of the relevant debtor to have been located in Hong Kong continuously for six months for the mainland courts to consider an application. The mainland courts' assessment of COMI is based on the place of incorporation of the debtor, but they may consider other factors, including the place of the principal office, the principal place of business, and the place of principal assets of the debtor. The mainland courts therefore reserve the right to form an independent view on a case-by-case basis, which the market will closely watch.

A typical Greater China financing structure might involve a holding company incorporated offshore (for example, in Bermuda, the Cayman Islands, or the British Virgin Islands) that is listed and headquartered in Hong Kong and holds assets and operates both in Hong Kong and the mainland. In the recent case of *Lamtex Holdings* [2021] HKCFI 622, the Hong Kong court made a compulsory winding-up order of a Bermudian company notwithstanding the opposition of the locally appointed provisional liquidators. The court found that the Bermudian officeholders were not promoting a restructuring with sufficient urgency and concluded that it would be more efficient and effective for an insolvency process to be managed out of the location of the debtor's COMI, namely Hong Kong. A winding-up in Hong Kong was also likely better to reflect the commercial reality that the company had little connection with its place of incorporation. By extension, the Hong Kong court might be expected to grant recognition to COMI-based foreign insolvency proceedings commenced outside of the debtor's jurisdiction of incorporation in circumstances in which the officeholder is promoting a genuine restructuring of the debtor's liabilities.

In situations in which debtors have significant assets and/or creditors based in the mainland, it remains to be seen whether the mainland courts would recognise a commencement of insolvency proceedings (and any associated determination of COMI) by Hong Kong and how this uncertainty would affect the "restructuring venue" choices of debtors. Would the mainland courts recognise a Hong Kong scheme of arrangement, particularly if not promoted by liquidators? Conversely, will more PRC-based companies that use the PRC bankruptcy reorganisation proceeding to restructure their debts in the mainland seek recognition of that reorganisation in Hong Kong to address the offshore elements of the restructuring?

Looking forward

An outbound request from Hong Kong-appointed liquidators is currently being tested: in *Re Samson Paper Co Ltd* [2021] HKCFI 2151, the Hong Kong court considered whether to accede to the liquidators' request to issue a recognition letter to the Shenzhen regional court. The court was satisfied that the request was appropriate on account of the assets of the company situated in the mainland, and a request was duly made in July 2021. At the time of writing, the request remains pending before the Shenzhen regional court. The court's response will set the future tone and path of comity between the two jurisdictions.

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