I. EFFECT OF WINDING-UP AND RECEIVERSHIPS ON DIRECTORS

Compulsory Winding-Up

Powers of Directors

General

The presentation of a petition for the winding-up of the company by the court does not in itself affect the powers or position of the directors who may continue to operate the business of the company.[1] However, the directors would need to ensure that they do not engage in fraudulent trading,[2] and in addition, should be aware that if a winding-up order is made, any disposition of the company's property and any alteration in the status of the members of the company after the date of the petition would be void unless validated by the court.[3] Where a provisional liquidator is appointed before the hearing of the petition, the directors' powers would cease.[4] The board has some residuary powers though, such as opposing the petition on behalf of the company or in appealing against the order for the appointment of the provisional liquidator.[5] The scope of the board's residuary powers can generally be tested by considering whether the power the board is said to have lost is one which can be said to have been assumed by the liquidator; if it has not been assumed, then the board would still retain the power.[6] In addition, there may be some powers which can be exercised by both the provisional liquidator and the directors, such as the right of inspection of the company's accounting records under the Companies Ordinance (Cap.622), s.374(1)(b). In *Re Gold Pleasure Industrial Co Ltd*,[7] the court held that there is no inconsistency for both the directors and provisional liquidators to exercise this right of inspection, so long as the directors do not exercise the right in such a way as to jeopardise or adversely affect the provisional liquidators' functions. Where a provisional liquidator had not been appointed before the winding-up order, the directors' management powers and control over the company would cease upon the making of the winding-up order whereupon the Official Receiver becomes the provisional liquidator in accordance with the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.194.[8] However, the directors could act for the company to appeal the wind- **1.001**

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1 *Re Oriental Bank Corp, ex p Guillemin* (1884) 28 Ch D 634; *Mersey Steel and Iron Co v Naylor Benzon & Co* (1882) 9 QBD 648.

2 Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.275.

3 Cap.32, ss.182, 184.

4 *Re Oriental Bank Corp, ex p Guillemin* (1884) 28 Ch D 634; *Fowler v Broad's Patent Night Light Co* [1893] 1 Ch 724; *Gosling v Gaskell* [1897] AC 575; *Re Mawcon Ltd* [1969] 1 All ER 188, at 192, [1969] 1 WLR 78, at 82; *Re Union Accident Insurance Co Ltd* [1972] 1 All ER 1105, at 1113, [1972] 1 WLR 640, [1972] 1 Lloyd's Rep 297, *per* Plowman J.

5 *Re Perak Pioneer Ltd (No 3)* [1984] HKC 505; *Re Union Accident Insurance Co Ltd* [1972] 1 All ER 1105, at 1113, [1972] 1 WLR 640, [1972] 1 Lloyd's Rep 297, *per* Plowman J.

6 *Re Union Accident Insurance Co Ltd* [1972] 1 All ER 1105, at 1113, [1972] 1 WLR 640, [1972] 1 Lloyd's Rep 297, *per* Plowman J.

7 [2006] 4 HKC 398. On the directors' rights of inspection generally, see also *Re Alvarez & Marsal Asia Ltd* [2009] 4 HKLRD 727; *Re Fook Lam Moon Restaurant Ltd* [2011] 1 HKLRD 964; *Lam Sit King v Chungshan Commercial Association Hong Kong* [2011] 3 HKLRD 323.

8 *Madrid Bank v Bayley* (1866) LR 2 QB 37, at 40; *Re Oriental Inland Steam Co* (1874) 9 Ch App 557, at 560; *Re Ebsworth & Tidy's Contract* (1889) 42 Ch D 23, at 43; *Fowler v Broad's Patent Night Light Co* [1893] 1 Ch 724; *Measure Bros Ltd v Measures* [1910] 2 Ch 248; *Re Farrow's Bank Ltd* [1921] 2 Ch 164, at 174; *Re Mawcon Ltd* [1969] 1 All ER 188; [1969] 1 WLR 78; *Re Union Accident Insurance Co Ltd* [1972] 1 All ER 1105; [1972] 1 WLR 640; [1972] 1 Lloyd's Rep 297.

ing-up order.[9] A director might also be appointed as a special manager with such powers as determined by the court on application by the Official Receiver where the Official Receiver is liquidator of the company.[10]

Effect of Acting Outside of Powers

1.002 Where the directors act outside of their powers, the act will not be binding on the company.[11] There may be a possibility that a third party who deals with the company without knowledge of the appointment of the provisional liquidator or the winding-up could rely on the directors' ostensible authority,[12] although ostensible authority would not be applicable where notice of the order for the appointment of the provisional liquidator or for the winding-up has been advertised in accordance with Companies (Winding-Up) Rules, r 36.[13] The liquidator could, however, adopt and ratify the acts of the directors.[14]

Directors Engaged as Employees

1.003 Employees are dismissed from the date of publication of the order for winding-up, and accordingly a director employed under a service contract[15] would be dismissed from his position as employee[16] and may claim in the winding-up for any entitlements due in such capacity as employee.[17] As to the rights of such directors to claim compensation for termination of their engagement as employees, see para.1.008 below. The liquidator may however allow the employment of some or all the company's employees to continue if the liquidator carries on the business of the company.[18]

Whether Directors Cease to Hold Office

1.004 Although the directors may lose their powers and executive directors are dismissed as employees, it is not entirely clear whether the directors actually cease to hold office as directors. There are indications in the English Court of Appeal decision of *Measures Brothers Ltd v Measures*[19] that the office of director is vacated automatically upon the winding-up, although it does not appear that the decision actually turned on that

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9 *Re Diamond Fuel Co* (1879) 13 Ch D 400, at 404–405; *Re Union Accident Insurance Co Ltd* [1972] 1 WLR 640; *Re Reprographic Exports (Euromat) Ltd* (1978) 122 SJ 400.

10 Cap.32, s.216.

11 *Bolognesi's Case* (1870) 5 Ch App 567.

12 *Cf, Re a company (No 006341 of 1992), ex p B Ltd* [1994] 1 BCLC 225, at 230.

13 *Re Mawcon Ltd* [1969] 1 All ER 188; [1969] 1 WLR 78.

14 *Re Mawcon Ltd* [1969] 1 All ER 188; [1969] 1 WLR 78.

15 See *Re Beeton & Co Ltd* [1913] 2 Ch 279.

16 *Re General Rolling Stock Co* (1866) LR 1 Eq 346 (advertisement of the winding-up order is to be treated as notice by the liquidator of termination of the employment); *Re Oriental Bank Corp, ex p Guillemin* (1884) 28 Ch D 634; *Golsing v Gaskell* [1897] AC 575, HL; *Fowler v Commercial Timber Co* [1930] 2 KB 1; *Re Standard Salt & Alkali Ltd* [1934] SASR 168; *Re Mawcon Ltd* [1969] 1 All ER 188, [1969] 1 WLR 78; *Re Peck Winch & Tod Ltd* (1979) 130 NLJ 116.

17 *Re Beeton & Co Ltd* [1913] 2 Ch 279 (director who was also engaged as employee entitled to claim preferential payments due to employees under Companies (Consolidation) Act 1908 s.209 (cf Cap.32 s.265)).

18 *Re English Joint Stock Bank, ex p Harding* (1867) 3 Eq 341; *Re Herald Newspaper of Otago* (1889) 7 NZLR 484; *Re Associated Dominions Assurance Society Ltd* (1962) 109 CLR 516; *Re Oriental Bank Corp* (1886) 32 Ch D 366; *Reid v Explosives Ltd* (1887) 19 QBD 265.

19 [1910] 2 Ch 248. See also *McAteer v Mullen* [2008] NI Ch 12; *Park Associated Developments Ltd (in liq) v Kinnear* [2013] EWHC 3617 (Ch) at [2].

issue.[20] That approach however was accepted in a South African decision,[21] and in addition, Canadian cases have held that, following the appointment of the liquidator, the directors are not under fiduciary duties so that they are free to purchase the company's property from the liquidator.[22] However, in the earlier case of *Madrid Bank Ltd v Bayley*,[23] Blackburn J (with whom Shee J agreed) had held that on a winding-up, although the directors no longer have control over the management of the company, nothing in the companies legislation required the directors to cease to be officers of the company, and accordingly the directors in that case were required to answer interrogatories under relevant statutory provisions requiring "officers" of a body corporate to answer interrogatories in an action to which the body corporate is a party. Australian courts have, upon reviewing the various English and overseas decisions, subsequently held that the weight of authority supports the view that the directors are not automatically removed from office upon a winding-up, but simply have their powers suspended.[24] In *Austral Brick Co Pty Ltd v Falgat Constructions Pty Ltd*,[25] Young J stated that the Canadian cases do not proceed on the basis that the directors have ceased to hold office, and can be explained on the basis that, because the company is adequately protected by an independent liquidator on a winding-up, it is not necessary to impose on the directors all the usual fiduciary obligations when dealing with the liquidator. In *McAusland v Deputy Commissioner of Taxation*,[26] French J had also held that the legislative scheme (in relevant respects comparable to the Hong Kong legislation) requires nothing more than a cessation of the powers of the directors on a winding-up, and further that the legislation, in allowing for a stay or termination of the winding-up, would be consistent with a mere suspension of power rather than an automatic vacation of office, as this militates against the unnecessary inconvenience of having to reappoint the directors should the winding-up proceedings be stayed or terminated.

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20 The issue before the Court of Appeal was whether the company in liquidation could by injunction enforce a restraint of trade covenant against the director, in circumstances where the employment of the director ceased upon winding-up. Buckley LJ, in dissent, had held that as the director vacated office upon the winding-up, then in accordance with the contract, the director would be restrained from competing against the company for a seven-year period following vacation from office (see especially [1910] 2 Ch 248 at 256). The majority had held against the company, but the ratio of the majority was simply that the company would be denied equitable relief because it was unable to perform its side of the bargain by continuing the employment of the director. Of the majority judges, Cozens-Hardy MR did not comment on whether the director vacated office, but Kennedy LJ did state that the director was displaced from his office. Whether the director actually ceased office was not an issue though (as noted by Joyce J in the first instance decision in *Measures Brothers v Measures* [1910] 1 Ch 336 at 345) and it appears that the analysis in the Court of Appeal judgments would not have depended on whether the winding-up automatically led to the office of director being vacated or simply led to the director's employment under the contract being automatically terminated.

21 *Attorney General v Blumenthal* [1961] 4 Sth Af LR 313.

22 *Re Mabou Coal and Gypsum Co* [1894] 27 NSR 305, which affirmed *Chatam National Bank v McKeen* (1895) 24 SCR 348; *Holmstead v Annable* (1914) 18 DLR 3.

23 (1866) LR 2 QB 37.

24 *Austral Brick Co Pty Ltd v Falgat Constructions Pty Ltd* (1990) 8 ACLC 1011; 2 ACSR 766; *Lord Corporation Pty Ltd v Green* (1991) 22 NSWLR 532 at 541–3; *McAusland v Deputy Commissioner of Taxation* (1994) 12 ACLC 78; 12 ACSR 432.

25 *Austral Brick Co Pty Ltd v Falgat Constructions Pty Ltd* (1990) 8 ACLC 1011, 2 ACSR 766 at 768.

26 *McAusland v Deputy Commissioner of Taxation* (1994) 12 ACLC 78; 12 ACSR 432 at 449. Gummow J (with whom Sheppard J agreed on this issue) decided the relevant issue on a different basis, but was willing to assume that the "suspension of powers" approach to be correct for the purposes of that case.

Assistance in the Liquidation and Examination of Directors

Assistance in the Liquidation

1.005 Upon a provisional liquidator being appointed or upon a winding-up order being made, the directors must allow the provisional liquidator or liquidator to take custody and control of all the property of the company.[27] Directors or former directors, if required by the provisional liquidator or liquidator, must within 28 days of the appointment of the provisional liquidator or the date of the winding-up order (as the case may be) submit to the provisional liquidator or liquidator a verified statement of the company's affairs in accordance with Cap.32, s.190. After a winding-up order is made, the liquidator may order officers of the company to deliver, convey, surrender or transfer any money, property or books and papers in their hands to which the company is *prima facie* entitled.[28] The directors may also need to attend on the Official Receiver, provisional liquidator or liquidator to answer questions and to give information both before and after the submission of the statement of affairs.[29] Where required, the directors might also be summoned before the court under s.221 of Cap.32 to be examined in relation to the promotion, formation, trade, dealings, affairs or property of the company, or to produce any books and papers in their custody or power relating to the company.[30] Failure to deliver the company's property and books to the liquidator or for concealing or providing false information about the company may lead to criminal liability.[31]

Public Examinations

1.006 Directors might also be required to be publicly examined before the court under s.222 of Cap.32, where the Official Receiver or liquidator has made a report under s.191 stating that in his opinion the director has committed a fraud in the promotion or formation of the company or in relation to the company since its formation. In addition, under s.168IA, where the Official Receiver has made a report that in his opinion a *prima facie* case exists against a director that would render him liable to a disqualification order under Part IVA,[32] the court may, on application by the Official Receiver, require the director to attend before the court to be publicly examined as to the conduct of the business of the company or as to his conduct and dealings as a director.

Fiduciary Duties

Scope of Application of Duties: Effect of Winding-Up

1.007 As discussed above, it is not entirely clear whether directors vacate office upon a winding-up or merely have their powers suspended. However, even if the directors have not vacated office, it is clear that the directors would not be subject to any duties to act bona fide in the interests of the company or to act for proper purposes or to

[27] Cap.32, s.197.

[28] The liquidator is delegated with the court's power to require delivery of property under Cap.32, s.211; see also Cap.32, s.226(c) and Companies (Winding-Up) Rules, r 67.

[29] Companies (Winding-Up) Rules, rr 39(2) and 41.

[30] Section 221 is discussed in more detail in Chapter 6.

[31] Under Cap.32, ss.271, 272.

[32] See "Disqualification of directors" at para.1.065, below.

act with due care, skill and diligence, for the reason that the directors can no longer exercise powers on behalf of the company. In addition, the directors may purchase the company's assets from the liquidator without being subject to restrictions arising from any fiduciary duties.[33] But it is also clear that, whether or not the directors are treated as having vacated office, they would not be able to use information properly regarded as trade secrets belonging to the company, since such a restriction applies even after a director has left office.[34] So, for example, in *Measures Brothers Ltd v Measures*,[35] where, at a time when winding-up of the company was imminent, the director had made copies of lists of the company's customers for later use in his own business after the winding-up order was made, Joyce J held that the director's actions in taking the lists amounted to a breach of duty to the company and ordered the director to deliver back those lists to the company.[36]

In non-winding-up cases, the courts have accepted that the corporate opportunity doctrine still applies where a director has resigned from the company, where the resignation may fairly be said to have been prompted or influenced by a wish to acquire for himself the opportunity sought by the company or where it was his position with the company rather than a fresh initiative that led him to the opportunity which he later acquired.[37] It is not clear how far this principle applies in the winding-up situation though. There is a New Zealand authority which indicates that a company cannot prevent a director from exploiting a corporate opportunity where the company had terminated the director's employment.[38] On this analysis, and if the winding-up has led to the director vacating office, then it could be said that the company has terminated the director's position and thus the directors are entitled to exploit the corporate opportunity and it matters not whether the company had acted voluntarily or involuntarily in the termination.[39] In any event, the continuing fiduciary obligations of directors who have left office do not go so far as to prevent a director from using his own accumulated knowledge, skill and experience for his own profit, nor from preventing the director from cultivating his own commercial relationships with the company's suppliers and customers,[40] provided that the use of the company's contacts does not involve taking away confidential customer lists or committing to memory of such information.[41]

[33] *Re Mabou Coal and Gypsum Co* [1894] 27 NSR 305, which affirmed *Chatam National Bank v McKeen* (1895) 24 SCR 348; *Holmested v Annable* (1914) 18 DLR 3; *Lord Corporation Pty Ltd v Green* (1991) 22 NSWLR 532.

[34] See *Kishimoto Sangyo Co Ltd v Akihiro Oba* [1996] 2 HKC 260, CA; *Measure Bros Ltd v Measures* [1910] 1 Ch 336; *Lord Corporation Pty Ltd v Green* (1991) 22 NSWLR 532.

[35] *Measure Bros Ltd v Measures* [1910] 1 Ch 336. See also *Austral Brick Co Pty Ltd v Falgat Constructions Pty Ltd* (1990) 8 ACLC 1011; 2 ACSR 766, at 768.

[36] This aspect of the decision of Joyce J at first instance was not challenged on appeal.

[37] *Canadian Aero Service Ltd v O'Malley* (1973) 40 DLR (3d) 371; *Industrial Development Consultants Ltd v Cooley* [1972] 2 All ER 162; *Kishimoto Sangyo Co Ltd v Akihiro Oba* [1996] 2 HKC 260, CA.

[38] *Plateau Equipment Ltd v Marsden* (1991) 5 NZCLC 67,096.

[39] See *Measure Bros Ltd v Measures* [1910] 2 Ch 248. But *cf Lord Corporation Pty Ltd v Green* (1991) 22 NSWLR 532, at 543–544.

[40] *Kishimoto Sangyo Co Ltd v Akihiro Oba* [1996] 2 HKC 260, CA; *Kao Lee and Yip v Koo Hoi Yan Donald* [2003] 2 HKC 113.

[41] *Measure Bros Ltd v Measures* [1910] 1 Ch 336; *Robb v Green* [1895] 2 QB 315, CA (Eng); *Sanders v Parry* [1967] 2 All ER 803; [1967] 1 WLR 753; *Roger Bullivant Ltd v Ellis* [1987] ICR 464, [1987] IRLR 491, CA (Eng).

If the directors are not treated as having vacated office though, the conceptual analysis as to the scope of application of the corporate opportunity doctrine would be different from the above. *Prima facie*, if the directors are still in office, in principle it would appear that they would still be subject to the general duties preventing them from exploiting corporate opportunities belonging to the company, at least where the liquidator is carrying on, or may still carry on, the company's business. Ordinarily, it seems that where a corporate opportunity has come to the directors by reason of their position as directors, they are restrained from diverting corporate opportunities to themselves on the basis that they have acquired or became aware of the opportunity as representatives of the company and accordingly the opportunity belongs in equity to the company.[42] This rationale would equally be applicable in the period during winding-up where the liquidator may still pursue the corporate opportunity for the benefit of the company's creditors and shareholders, since the opportunity can be said to belong to the company. On this approach then, the director cannot exploit a corporate opportunity which came to the director by reason of and in the course of the position of director.[43]

However, it is submitted that the directors would not be precluded from exploiting a business opportunity which came to the director in a "private" capacity following the commencement of winding-up or from otherwise competing with the company during the winding-up.[44] Even before winding-up, there is no absolute duty on directors preventing them from competing with the company,[45] and in the period when the company is being wound up, there is arguably no conflict of interest at all where the directors no longer exercise any powers over the company and where they are no longer responsible for the company's assets or business. Furthermore, although cases such as *Industrial Development Consultants Ltd v Cooley*[46] indicate that ordinarily a director is not permitted to exploit any opportunity which is of concern and relevance to the company, notwithstanding that the director only became aware of the opportunity in a private capacity, it may be that this principle is not applicable in the winding-up context. It appears that the rationale for that principle is that the directors are under duties of good faith to act in the interests of the company and thus are under an obligation to pass on the information about the business opportunity which may be of relevance to the company.[47] However, it could be argued that this rationale is not applicable during a winding-up, since the directors are no longer under any obligations to manage the company's business and to act in the interests of the company.

Voluntary Winding-Up

Powers of Directors and Position of Directors Engaged as Employees

1.008 The passing of a resolution[48] for the voluntary winding-up of the company does not in itself affect the powers of directors, however, pursuant to Cap.32, those powers

[42] See *Cook v Deeks* [1916] 1 AC 554.
[43] *Cf Lord Corporation Pty Ltd v Green* (1991) 22 NSWLR 532, at 543–544.
[44] *Cf Measure Bros Ltd v Measures* [1910] 2 Ch 248.
[45] *London & Mashonaland Exploration Co v New Mashonaland Exploration Co* [1891] WN 165; *Bell v Lever Bros* [1932] AC 161, at 195, HL.
[46] [1972] 2 All ER 162. See also *SEA Food International Pty Ltd v Lam* (1998) 16 ACLC 552.
[47] [1972] 2 All ER 162, at 173–174.
[48] Under Cap.32, s.228.

would cease upon the appointment of the liquidator.[49] The directors' powers can continue though if sanctioned, in a voluntary winding-up, by the company in general meeting or the liquidator[50] or in a creditor's voluntary winding-up, by the committee of inspection or the creditors if there is no such committee.[51] Where the directors have acted outside their powers, the transaction would ordinarily be invalid,[52] however, it may be that where the resolution for winding-up was neither registered nor advertised, a third party dealing with the directors could rely on the directors' ostensible authority in binding the company if the third party did not know and had no means of knowing that the resolution had been passed.[53] Where the directors have acted without authority, it is always possible for the liquidator to adopt and ratify the directors' acts.[54]

It appears that although the directors' powers may cease upon the appointment of the liquidator, the directors nonetheless still remain in office.[55]

As to whether executive directors are automatically dismissed from their position as employee, the law is not entirely settled. In *Re Imperial Wine Co; Shireff's Case*,[56] Lord Romilly MR stated that the resolution to wind up the company puts to an end the employment of the company's manager. However, in *Midland Counties Bank v Attwood*,[57] Warrington J considered that the *Shireff's Case* was not binding authority for that principle on the basis that it was *obiter* only and held instead that the voluntary liquidation does not in itself result in the dismissal of the company's employees. Voluntary winding-up was treated as being different from compulsory winding-up in that in the former the liquidator simply acts as an officer of the company, while in the latter, there is a change in the personality of the employer in the sense that the liquidator in control of the company is an officer of the court.[58] In the later case of *Fowler v Commercial Timber Co Ltd*,[59] Greer LJ of the English Court of Appeal suggested though, in *obiter*, that where the company is insolvent, the resolution for voluntary winding-up would, just as much as a compulsory winding-up, automatically put to an end the employment of the company's managers and other employees. It has been suggested that the resolution for winding-up can be treated as resulting in the employee's dismissal in such a situation, and possibly in other situations as well, where the resolution and the surrounding circumstances indicate that the company is unable or unwilling to carry out its obligations under the employment contract.[60]

[49] Cap.32, s.235(2) (members' voluntary winding-up) and s.244(2) (creditors' voluntary winding-up).
[50] Cap.32, s.235(2).
[51] Cap.32, s.244(2).
[52] *Bolognesi's Case* (1870) 5 Ch App 567.
[53] *Re A Company (No 006341 of 1992); ex p B Ltd* [1994] 1 BCLC 225, at 230.
[54] *Re Mawcon Ltd* [1969] 1 All ER 188; [1969] 1 WLR 78.
[55] *Midland Counties District Bank Ltd v Attwood* [1905] 1 Ch 357; see also Andrew R Keay, *McPherson's Law of Company Liquidation* (London: Sweet and Maxwell, 2001), para.7.33.
[56] (1872) 14 Eq 417.
[57] [1905] 1 Ch 357. See also *McEvoy v Incat Tasmania Pty Ltd* (2003) 130 FCR 503; 46 ACSR 392 at [7].
[58] This position is criticised in Andrew R Keay, *McPherson's Law of Company Liquidation*, (London: Sweet and Maxwell, 2001), p 312; But *cf* Robert Pennington, *Pennington's Corporate Insolvency Law*, 2nd edn (London: Butterworths, 1997), p 102.
[59] [1930] 2 KB 1.
[60] See *Re T N Farrer Ltd* [1937] Ch 352; Andrew R Keay, *McPherson's Law of Company Liquidation* (London: Sweet and Maxwell, 2001), pp.312–313; Keith J Bennetts, "Unfair Dismissal Proceedings in Company Liquidation and Receivership" (1990) 8 *C&SLJ* 158, p 162.

Where there is a dismissal of the director-cum-employee, whether the director is entitled to compensation for early termination depends on the proper construction of the terms of the employment contract. Where the contract between the director and the company is constituted by the articles only, then there is an implied term that the employment is conditional on the continued existence of the company and accordingly the director is not entitled to damages for the termination following winding-up. However, where, apart altogether from the articles, the company and the director have entered into an independent agreement, such a term will not usually be implied into the contract, and the director would be entitled to claim for breach of contract if there has been early termination (such as where the period of service was for a fixed term that has not yet expired).[61]

Role and Assistance in the Liquidation

1.009 Where a members' voluntary winding-up is proposed, the directors must issue a certificate of solvency in accordance with Cap.32, s.233 within the five weeks immediately preceding the date of the passing of the resolution for winding-up or on that date but before the passing of the resolution. Where a creditors' winding-up is proposed, a meeting of creditors must be arranged for the day on which there is to be held the members' general meeting (at which the resolution for winding-up is to be proposed) or for the following day and the creditors' meeting must be properly advertised in accordance with Cap.32, s.241. The directors must cause a statement of the affairs of the company together with a list of the creditors and their claims to be laid before the creditors' meeting, and one of the directors must be appointed by the board to preside at that meeting.[62]

A copy of the resolution for winding-up must be forwarded to the Registrar within 15 days after the passing of the resolution,[63] and notice of the resolution must be advertised in the Gazette within 14 days of the resolution.[64] If there is a breach of either of these requirements, the company and responsible officers are liable to a fine.[65]

The liquidator would be entitled to take control of the company's assets in accordance with the liquidator's powers and functions[66] and accordingly the directors would need to deliver up to the liquidator the property and books of the company in their custody or control. The provisions in sections 271 and 272 of Cap.32 imposing criminal liability for failure to do so or for providing false information to the liquidator are applicable, being provisions which apply to every type of winding-up.[67]

Fiduciary Duties

1.010 The directors' usual fiduciary duties will continue to the extent that the directors continue to have management powers, but even where the directors no longer exercise any management

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61 *Re N T Farrer Ltd* [1937] Ch 352; see also *Fowler v Commercial Timber Co Ltd* [1930] 2 KB 1.

62 Cap.32, s.241.

63 Cap.622, s.622.

64 Cap.32, s.229(2).

65 For contraventions of Cap.622, s.622, "responsible persons" (as defined in Cap.622, s.3) would be liable. For contraventions of Cap.32, s.229(2), "officers in default" (as defined in Cap.32, s.351(2)) would be liable.

66 See Cap.32, ss.199 and 251.

67 See Cap.32, ss.271 and 272.

powers, they might still be subject to certain fiduciary duties: see the discussion above of the directors' fiduciary duties in the context of compulsory winding-up.

Receivership

General

The appointment of a receiver does not result in the directors ceasing to hold office.[68] 1.011
The directors would still be required to comply with their statutory duties, for example their statutory obligation[69] to prepare financial statements,[70] as well as their fiduciary duties under the general law, although those duties will be qualified by reason and to the extent of the receiver's control of the company.[71] For example, a director could not be called to account for a failure to pursue an asset which was in the possession and control of the receiver with the same diligence as the director would, where the company is not in receivership.[72] As the directors remain in office, they can do what the receiver requires them to do as such holders of office.[73]

The appointment of the receiver would also have an impact on the powers of the directors, which are reduced in inverse proportion to the powers of the receiver.[74] To ascertain the scope of the directors' powers, it is accordingly necessary to first identify the extent of the powers of the receiver from the court order or charge instrument under which the receiver was appointed. Where the receiver was appointed by the court to collect, get in and receive the whole of the assets of the company, it has been held that the appointment of the receiver effectively deprives the directors of all powers of management.[75] Where the receiver was appointed privately pursuant to a charge, the receiver would have power as a receiver or as a receiver and manager over the assets that are subject to the charge, in accordance with the terms of the debenture or charge instrument, and such powers can be exercised by the receiver without the concurrence of the directors.[76] Thus, the directors will generally have no role to play in relation to the charged assets.

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68 *Newhart Developments Ltd v Co-operative Commercial Bank Ltd* [1978] QB 814, at 819, [1978] 2 All ER 896; [1978] 1 WLR 636, CA (Eng); *Li Lai Fun v Centro-Sound Ltd* [1986] 1 HKC 541; *McDonald v Golden Dynasty Enterprises Ltd* [2008] 5 HKLRD 569; and see also *Hawkesbury Development Co Ltd v Landmark Finance Pty Ltd* (1969) 92 WN(NSW) 199, at 209; [1969] 2 NSWLR 782, at 790.

69 See Cap.622, s.379.

70 See *Gomba Holdings UK Ltd v Homan* [1986] 1 WLR 1301; [1986] 3 All ER 94, [1986] BCLC 331, [1986] BCC 99.

71 See *Re Geneva Finance Ltd* (1992) 7 ACSR 415, at 420; *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638, at [1328].

72 *Re Geneva Finance Ltd* (1992) 7 ACSR 415, at 421.

73 *McDonald v Golden Dynasty Enterprises Ltd* [2008] 5 HKLRD 569. In that case, the court made orders, on application by the receivers, for the directors to pass board resolutions for the execution of powers of attorney giving the receivers power to take action for and on behalf of the company to identify and preserve the assets of the company and to investigate dispositions of the company's assets during the receivership period. The receivers considered that it was necessary for the directors to take such action as it would otherwise be difficult for them to act for and on behalf of the company in the PRC due to complexities in obtaining recognition of their authority as receivers under PRC law.

74 See, e.g. *Hawkesbury Development Co Ltd v Landmark Finance Pty Ltd* (1969) 92 WN(NSW) 199, at 209, [1969] 2 NSWLR 782, at 790.

75 *McDonald v Golden Dynasty Enterprises Ltd* [2008] 5 HKLRD 569; see also *Australian Industry Development Corp v Co-operative Farmers and Graziers Direct Meat Supply Ltd* (1978) 3 ACLR 543; *Moss Steamship Company Ltd v Whinney* [1912] AC 254, at 260.

76 *M Wheeler & Co Ltd v Warren* [1928] Ch 840; *Re Scottish Properties Pty Ltd* (1977) 2 ACLR 264.

I. INTRODUCTION

5.001 The (new) Companies Ordinance (Cap.622) made wide-sweeping changes to Hong Kong companies law. However, these changes did not affect the winding-up process. The relevant provisions affecting winding-up remained alive in the old Companies Ordinance (unrepealed) and this Ordinance has been re-titled the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32). That said, an amendment bill to the insolvency regime is currently under debate. This can be reviewed at: Companies (Winding Up and Miscellaneous Provisions) (Amendment) Bill 2015 (http://www.legco.gov.hk/yr15-16/english/bills/b201510021.pdf) currently under debate http://www.info.gov.hk/gia/general/201510/02/P201510020248.htm.

Where a company is solvent and its members wish to put it into liquidation, they may do so by way of a members' voluntary winding-up.

As the company is solvent, the creditors will be paid in full and therefore they have no financial interest in the outcome of the liquidation. The members will therefore have control of the conduct of the winding-up of the company. Accordingly, the members will appoint the liquidator, determine his remuneration and exercise a general power of supervision over the performance of his duties.

II. PREREQUISITE FOR MEMBERS VOLUNTARY WINDING-UP CERTIFICATE OF SOLVENCY

5.002 Before a company can be placed in members' voluntary winding-up, the directors of the company (or if there are more than two, the majority of the directors) must issue a certificate of solvency.[1] The certificate of solvency is normally issued at a directors' meeting. However, it may be issued other than at a directors' meeting if, but only if, before such certificate is issued, the directors have passed a resolution authorising the certificate to be issued.[2]

In the case of a private company having only one director, the sole director may issue a certificate of solvency by recording the certificate and signing the record of it in the minute book of the company.[3]

The certificate of solvency must be in the specified form.[4] It must state that:

(a) The directors have made full enquiry into the company's affairs; and

(b) They have formed the opinion that the company will be able to pay its debts in full within such period not exceeding 12 months from the commencement of the winding-up as may be specified in the certificate of solvency.[5]

The certificate of solvency must also fulfill the following requirements to be effective:

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1 Section 233 of Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32).
2 Section 233(1A) of Cap.32.
3 Section 233(6) of Cap.32.
4 See Form NW1 of the Companies Registry Specified Forms.
5 Section 233(1) of Cap.32.

(1) It must be issued within five weeks immediately preceding the date of the passing of the resolution for winding-up or on that date but before the passing of the resolution; and

(2) It must be filed with the Registrar of Companies not later than the date of the filing with the Registrar a copy of the resolution for voluntary winding-up[6] (i.e. within 15 days of the making of the resolution for voluntary winding-up).[7]

The certificate of solvency must contain a statement of the company's assets and liabilities at the latest practicable date before the issuing of the certificate.[8]

Most members' voluntary liquidations are used to wind-up inactive or dormant companies which have minimal assets and liabilities. Provided the company is solvent, issuing a certificate of solvency under such circumstances should be a straightforward matter.

More care should be exercised for active companies with significant assets and liabilities. In such circumstances, the directors of the company may wish to seek advice from a reputable firm of accountants and request such firm to provide written advice on whether the company is indeed solvent and able to discharge all its liabilities within a period of 12 months or less. They may also wish to discuss the proposed certificate of solvency with the proposed liquidator. In considering whether a certificate of insolvency may be issued, the directors should also bear in mind future or contingent liabilities under contracts, guarantees and other instruments and circumstances.

The proper issuance and filing of the certificate of solvency will result in the winding-up being a members' voluntary winding-up. Otherwise it will be a creditors' voluntary winding-up.[9]

In the matter *Re Pacific Gain Technologies Ltd* [2015] HKEC 1643, Harris J at para.3 stated that:

> "If the company files the certificate of solvency out of time, after the passing of a special resolution to put the company to liquidation, the company will be put automatically into creditors' voluntary winding-up. A court order will [then] be required to stay the creditors' voluntary winding-up and a order that the members' voluntary winding-up procedure can be recommenced."

A director who signs a certificate of solvency without reasonable grounds for the opinion that the company will be able to pay its debts in full within the period specified in the certificate may be convicted and be liable to a fine[10] and imprisonment for six months.[11]

If the company is unable to pay or provide for its debts in full within the period of five weeks after the issuing of the certificate, the directors are presumed not to have had reasonable grounds for their belief in the solvency of the company until the contrary is shown.[12]

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6 Section 233(2)(a) of Cap.32.
7 Section 622 of the Companies Ordinance (Cap.622) which came into force on 3rd March 2014.
8 Section 233(2)(b) of Cap.32.
9 Section 233(4) of Cap.32.
10 The maximum punishment is a fine at level 5 (currently HK$50,000).
11 Section 351 and Twelfth Schedule of Cap.32.
12 Section 233(3) of Cap.32.

III. PROCEDURE

Passing of Special Resolution

A members' voluntary winding-up is deemed to commence at the time of passing by the members of the company of a resolution placing the company into voluntary liquidation.[13] **5.003**

Generally, a special resolution is required.[14] However, in rare circumstances where there is a period fixed for the duration of the company by the articles and this has expired or where the event on the occurrence of which the memorandum of articles provide that the company is to be dissolved has happened, an ordinary resolution will suffice.[15]

For a special resolution, the following requirements must be satisfied:[16]

(a) Not less than 14 clear days notice[17] must be given of the meeting at which a special resolution is proposed. This requirement may be waived by 95% in nominal value of those shareholders having the right to attend and vote;

(b) Notice of the meeting must include the text of the resolution and specify the intention to propose the resolution as a special resolution;[18]

(c) 75% of those attending and voting must vote in favour of the special resolution;

(d) Voting can occur in person or by proxy; and

(e) Voting is initially on a show of hands although a poll vote may be demanded.[19]

A chairman's declaration that the resolution is carried shall, unless a poll is demanded, be conclusive evidence of the fact without proof of the number or proportion of the votes recorded in favour of or against the resolution.[20]

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13 Section 230 of Cap.32.
14 Section 228(1)(b) of Cap.32.
15 Section 228(1)(a) of Cap.32.
16 See also Sections 564 of the Cap.622.
17 See *Securities and Futures Commission v Stock Exchange of Hong Kong Ltd* [1992] 1 HKLR 135, where it was held that the words "not less than 21 days' notice" meant at least 21 clear days excluding the day of giving the notice, the day of deemed receipt and the day of the meeting itself. Note also that under Section 571(1)(b) of Cap.622, the minimum notice period for all general meetings (regardless whether it is an ordinary resolution or a special resolution) has now been reduced from 21 days to 14 clear days (for a limited liability company) and 7 clear days (for unlimited liability company), subject to any longer period of notice required by the company's articles. See also s.571(2) of Cap.622.
18 Sections 564(4)(a) and 564(4)(b) of the Cap.622. See also *Re Moorgate Mercantile Holdings Ltd* [1980] 1 All ER 40, [1980] 1 WLR 227, where it was held that the substance between the notice and the terms of the resolution passed must be identical, though corrections of clerical or grammatical errors are allowed, applied in *Re Hong Kong Pharmaceutical Holdings Ltd* [2006] HKCU 1931 (decision under the predecessor Companies Ordinance (CO) before the new Cap.622 came into force on 3rd March 2014); see also *Re Peninsular and Oriental Steam Navigator Co* [2006] All ER (D) 36.
19 There are some new provisions under Cap.622 with regard to the right to demand a poll. For example, the threshold for members is reduced from 10% to 5% of total voting rights and the threshold based on one-tenth of the paid up capital is removed (s.591 of Cap.622). There are also new provisions to clarify the rights and obligations of proxies (ss.596–605 of Cap.622).
20 Section 590 of Cap.622; see also *Re Hadliegh Castle Gold Mines* [1900] 2 Ch 419.

The length of notice may be abridged if it is so agreed by a majority of members having the right to attend and vote at the meeting, being a majority together representing at least 95% of the total voting rights at the meeting of all the members.[21]

Under section 548 of the Companies Ordinance (Cap.622),[22] anything that may be done by a resolution passed at a general meeting or a class meeting may be done, without a meeting and without any previous notice being required, by a written resolution of the members or of that class of members of the company (as the case may be).

Under the (new) Companies Ordinance (Cap.622), there are new provisions for proposing, passing and circulating written resolutions.[23]

The date of the resolution should be the date on which the last member or representative signs the written resolution.[24]

A copy of the special resolution must be filed with the Registrar of Companies within 15 days after the passing thereof.[25] If the company fails to register the special resolution within 15 days, the company and every responsible person (which includes a liquidator or provisional liquidator) commits an offence[26] and shall be liable to a fine and, for a continued default, to a daily default fine.[27]

Within 14 days[28] after the passing of the special resolution for voluntary winding-up, the company must give notice of the passing of the resolution by advertisement in the

[21] Section 571(3)(b) of the Cap.622.

[22] This section restates sections 116B(1), 116B(3) to 116B(6), and 116B(11) of the predecessor CO.

[23] For example, Cap.622 provides that: (a) either the directors or a member of a company may propose a written resolution (s.549 of Cap.622); (b) member(s) of the company who proposed the written resolution may require the company to circulate with the resolution a statement of not more than 1,000 words on the subject matter of the resolution (s.551(2) of the Cap.622); (c) the company must circulate the written resolution if it was proposed by the directors or by members of a company representing not less than 5% or a lower percentage specified for that purpose in the company's articles (ss.550 & 552(2) of Cap.622); (d) the proposed written resolution may be circulated, and member(s) may signify their agreement to it, by electronic means (ss.553(2)(a) & 556(3)(a) of Cap.622); (e) the company must circulate the resolution to every member within 21 days after it has received the proposed written resolution, it must also send the proposed written resolution to its auditor on or before the circulation date to members (ss.553 & 555 of Cap.622); (f) the period for agreeing to the proposed written resolution is 28 days or such period as specified in the company's articles (s.558 of Cap.622); and (g) if a resolution is passed as a written resolution, the company must send a notice of that fact to every member and the auditor of the company within 15 days (s.559 of Cap.622).

[24] Sections 548(4) and 556 of Cap.622.

[25] Sections 622(1) and 622(2) of Cap.622.

[26] Sections 622(7) and 622(9) of the Cap.622. The (new) Companies Ordinance (Cap.622) now introduces a new formulation of "responsible person" to replace "Officer who is in default" in the predecessor CO. "Responsible person" includes an officer or a shadow director of a company as well as an officer or a shadow director of a corporate officer of the company; see s.3 of Cap.622. The threshold for committing an offence under Cap.622 has been lowered by removing the element of "knowingly and willfully" from the provision to cover, *inter alia*, reckless acts or omissions.

[27] Section 622(7) of Cap.622. The maximum punishment is a fine at level 3 (currently HK$10,000) and a daily default fine of HK$300.

[28] Section 229(1) of Cap.32. Balancing the need for the notice to be given promptly and the practical difficulty faced by a company under the present requirement for publication in the Gazette, it is proposed in the Improvement of Corporate Insolvency Law Legislative Proposals Consultation Document published in April 2013 by the Financial Services and the Treasury Bureau (the "Consultation Document") to extend the time limit from 14 days to 15 days. Presumably, this is also to align the notice period with the period within which a copy of the special resolution for voluntary winding-up must be filed with the Registrar of Companies under sections 622(1) and 622(2) of Cap.622. (Note that the government has received a total of 36 written submissions during the consultation periodand has published a paper entitled "Improvement of Corporate Insolvency Law Legislative Proposals Consultation Conclusions" (the "Consultation Conclusions") in this reagrds. Such paper is available at http://www.fstb.gov.hk/fsb/ppr/consult/impcill.htm.)

Gazette. Otherwise, the company and its officers who are in default[29] will become liable to a fine and, for a continued default, to a daily default fine.[30]

Appointment of Liquidator

In addition to passing a special resolution, the company will, in practice, pass one or more of the following resolutions[31] as appropriate: **5.004**

(a) an ordinary resolution to appoint a liquidator;[32]

(b) an ordinary resolution to fix the remuneration of the liquidator;[33]

(c) a special resolution to authorise the liquidator to exercise particular powers set out in s.199 of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32) including the following:

  (1) to pay any class of creditors in full;

  (2) to make compromises or arrangements with creditors or persons claiming to be creditors, or having or alleging themselves to have any claim against the company; and

  (3) to compromise claims by the company against debtors, potential debtors, and contributories;[34]

(d) an ordinary resolution to dispense with the requirement to audit the liquidators' statement of receipt and payment; and[35]

(e) an ordinary/special resolution to authorize the liquidator to divide amongst the members of the company *in specie* or in kind the whole or any part of the assets of the company.[36]

The appointment of the liquidator is made,[37] in practice, at the same meeting at which the resolution to wind-up the company voluntarily is passed.[38]

[29] The definition of an "Officer who is in default" means any officer or shadow director of the company who knowingly and willfully authorises or permits the default, refusal or contravention. See s.351(2) of Cap.32. For the purposes of section 229(1) of Cap.32, the liquidator of the company shall be deemed to be an officer of the company (s.229(2) of Cap.32). The new formulation of "Responsible person" was introduced in Cap.622 to replace "Officer who is in default" as listed in the predecessor CO referred to in n 26 does not appear to apply to the term "Officer who is in default" in Cap.32. It is submitted that the said formulation should also apply to Cap.32 for consistency.

[30] Section 229(2) of Cap.32. The maximum punishment is fine at level 3 (currently HK$10,000) and a daily default fine of HK$300; see s.351(1A) and the Twelfth Schedule of Cap.32.

[31] See Smart and Booth (Eds), *Hong Kong Corporate Insolvency Manual* (2002), at p.16.

[32] Section 235(1) of Cap.32.

[33] Section 235(1) of Cap.32.

[34] These powers may be exercised if sanction is obtained in a members' voluntary winding-up by special resolution of the company in a general meeting. See s.251(1)(a) of Cap.32.

[35] Section 255A of Cap.32.

[36] Special resolution is required by Cap.622, Schedule 1, Article 105 (for public companies) and Schedule 2, Article 84 (for private companies) of the model articles made by the Financial Secretary under section 78(1) of Cap.622.

[37] An ordinary resolution would suffice. Section 235(1) of Cap.32.

[38] Section 235(1) of Cap.32.

The Liquidator must file notice of his appointment with the Registrar of Companies and also publish the same in the Gazette within 21 days of his appointment.[39] Any person in default will be liable to a fine and, for continued default, to a daily fine.[40]

In the event that the members of the company are unable to agree on the identity of the liquidator, the court may appoint a liquidator.[41]

IV. IF COMPANY IS FOUND TO BE INSOLVENT

5.005 If, at any time, the liquidator is of the opinion that the company will not be able to pay its debts in full within the period specified in the certificate of solvency, he shall immediately summon a meeting of the creditors.[42] If the liquidator fails to do so, he shall be liable to a fine.[43]

At this meeting convened by the liquidator, the liquidator shall lay before the creditors a statement of the assets and liabilities of the company.[44] The creditors may decide either to proceed as a creditors' voluntary winding-up or one or more of them may petition for the compulsory winding-up of the company. The creditors may appoint another liquidator and fix the remuneration of the liquidator so appointed. In addition, the creditors may also appoint a committee of inspection.[45]

V. STAY/RESCISSION OF MEMBERS' VOLUNTARY WINDING-UP

Stay of the Winding-Up Proceedings

5.006 In a members' voluntary winding-up, the court may stay the winding-up proceedings either altogether or for a limited period of time, and on such terms and conditions as the court thinks fit, upon the application of the liquidator, the Official Receiver or any creditor or contributory.[46] The company itself has no right to apply for a stay.[47]

The court has a discretion whether to grant a stay of the winding-up proceedings. The burden is on the applicant to make out a sufficient case for a stay that carries

[39] Section 253(1) of Cap.32. It is proposed in the Consultation Document that the notice period be shortened to 15 days to align with: (i) the requirement of section 117(1) of the predecessor CO (now repealed) (*cf* section 622(2) of the new Cap.622); and (ii) proposed changes to section 229 of Cap.32 referred to in n 28 above.

[40] The maximum punishment is a level 3 fine and a daily default fine of HK$300: see s.351(1A) & Twelfth Schedule of Cap.32.

[41] Section 252 of Cap.32.

[42] (n 44), below.

[43] Section 237A(3) of Cap.32.

[44] Section 237A(1) of Cap.32. However, this section does not specify: (a) the time limit for the liquidator to summon the meeting of creditors, (b) the manner in which notice should be given to the creditors, or (c) the details of the statement of assets and liabilities. The Consultation Document proposes inclusion of new provisions to address these issues so that when the winding-up is to proceed as a creditors' voluntary winding-up, the creditors would be involved and duly informed at the earliest possible instance, and the obligations of the liquidator to engage the creditors would be clearly set out.

[45] Section 237A(2) of Cap.32.

[46] Sections 209 and 255 of Cap.32.

[47] See *King Pacific International Holdings Ltd* [2002] 3 HKLRD 474.

conviction[48] so that it is not merely sufficient for the applicant to establish that a stay is reasonable in the circumstances.[49] The court has to be satisfied that it is right to stay the winding-up proceedings, and, if there be matters as to which the court has doubts, it should not order a stay.[50] The factors that a court would take into account in exercising such discretion will include:[51]

(a) whether there are sufficient assets to pay the creditors and the expenses of the liquidation;

(b) whether the stay is in the interest of the creditors, the liquidator and the members and whether they consent to the stay;

(c) whether there is a genuine commercial reason for the stay; and

(d) whether the stay is conducive or detrimental to commercial morality and the public at large including whether there is any irregularity in the affairs of the company.

Once a permanent stay of the winding-up procedure is granted, the liquidation is for all practical purposes at an end. The liquidator may be discharged, control of the company reverts to the directors and the company may resume its business.[52]

Rescission of Members' Voluntary Winding-Up

5.007 It has been held in Hong Kong that the members of a company may, by special resolution, rescind the earlier special resolution placing the company in Members' Voluntary Liquidation.[53]

The above decision has been the subject of criticism,[54] as being contrary to dicta of Megarry J in *Re Calgary and Edmonton Land Co Ltd*[55] to the effect that a voluntary liquidation may not be terminated by the members of the company passing a resolution to that effect. It has also been argued, *inter alia*, that if such rescission were to be allowed, there would be no necessity to apply to court to permanently stay a members' voluntary winding-up.[56]

Conversion from Voluntary Winding-Up to Compulsory Winding-Up

5.008 A members' voluntary winding-up of a company shall not bar the right of any creditor or contributory to apply to have the company wound up by the court, but in the case of an application by a contributory, the court must be satisfied that the rights of the contributories will be prejudiced by a voluntary winding-up.[57]

[48] *Re Calgary and Edmonton Land Co Ltd (in liquidation)* [1975] 1 WLR 355, at 358–359 cited in *Re Outboard Marine Corp Asia Ltd* [2003] 1 HKLRD 585, at 588, CFI.

[49] *Re Outboard Marine Corp*.

[50] *Re Lowston Ltd* [1991] BCLC 570.

[51] See *Outboard Marine Corp*; see also *Re Calgary and Edmonton Land*.

[52] *Palmer's Company Law*, para.15.164.

[53] See *Re Keon Trading Co Ltd* (unrep., HCMP 3674 of 1997, 6 Feb 1998).

[54] See *Smart and Booth, op cit*, at pp.11 and 12.

[55] *Ibid.*

[56] *Ibid.*

[57] Section 257 of Cap.32.

In *Re Goldcone Properties Ltd (in creditors' voluntary winding-up)*[58] Ribeiro J laid down, *inter alia*, the following principles relevant to determining whether the court should order a compulsory winding-up where the company is already in voluntary liquidation:

(a) The court has unfettered discretion to be exercised judicially taking into account all material factors, including whether the class remedy of liquidation would be better satisfied by the continuation of the voluntary liquidation or better served by being superseded by a compulsory liquidation;

(b) The court should consider whether the majority of the creditors in value supported the petition. If so, unless there are contrary reasons, the court would be inclined towards making a compulsory order;

(c) In weighing the views of creditors a qualitative as opposed to a purely quantitative approach should be used. In this regard, it would be relevant if the creditors opposing the petition had a personal interest in the opposition;

(d) Where the petitioner required the issues concerning the company's liquidation to be further investigated, the question was whether there was prima facie evidence that the matters which the petitioner required investigation were questions which rational creditors could think of that required investigation and further action and the outcome of which might be financially favorable to them; and

(e) Whether the liquidators are acting and seen to be acting independently and impartially particularly where possible wrongdoing by the directors had to be investigated and possibly pursued in litigation.

In considering whether it should exercise its discretion to grant an order that the company be wound up by the court in circumstances where the company is already being wound up voluntarily, the court should consider whether there are transactions which require investigation or whether the circumstances call for the exercise of powers which the court has in a compulsory winding-up.

The Official Receiver may also petition for a compulsory winding-up where a company is being wound up voluntarily. If the court is to make an order for compulsory winding-up, it must be satisfied that the voluntary winding-up cannot be continued with due regard to the interests of the creditors and contributories.[59]

Where a voluntary winding-up is converted to a compulsory winding-up, the winding-up of the company shall be deemed to have commenced at the time of the passing of the resolution and all proceedings taken in the voluntary winding-up are deemed to have been validly taken unless the court, on proof of fraud or mistake, thinks fit otherwise to direct.[60]

[58] [2000] 2 HKLRD 16. This was applied in *Re Fullbright Co Ltd* [2009] 2 HKLRD 584.
[59] Section 179(2) of Cap.32.
[60] Section 184(1) of Cap.32.

VI. CONSEQUENCES OF A MEMBERS VOLUNTARY WINDING-UP

5.009 Upon the commencement of the winding-up, the company shall cease to carry on its business except so far as may be required for the beneficial winding-up thereof.[61]

On the appointment of a liquidator, all the powers of the directors of the company shall cease except so far as sanctioned by the company in general meeting or by the liquidator.[62] It appears, however, that directors and employees are not automatically dismissed upon the voluntary winding-up.[63]

VII. THE LIQUIDATORS: DUTIES, POWERS, VACANCY IN OFFICE, REMOVAL BY THE COURT, REMOVAL OF LIQUIDATOR BY THE COMPANY AND CREDITORS, RESIGNATION AND VACATION OF OFFICE

Duties

5.010 In the event of the members' voluntary winding-up continuing for more than one year, the liquidator must summon a general meeting of the company at the end of the first year from the commencement of the winding-up, and of each succeeding year, or the first convenient date within three months from the end of the year or such longer period as the Official Receiver may allow. The liquidator must lay before the meeting an account of his acts and dealings and of the conduct of the winding-up during the preceding year.[64] Failure to comply with this provision results in a summary conviction or a fine.[65] The duty of the liquidator to call a general meeting is to ensure that he accounts to the members of the company in relation to the liquidation.

The liquidator must pay the debts of the company and must adjust the rights of contributories amongst themselves.[66]

Although there is no formal requirement to do so, the liquidator will often advertise for creditors to provide the liquidator with full particulars of their debts and claims.

The liquidator or any contributory or creditor may apply to the court to determine any question in the winding-up of a company, or to exercise all or any powers which the court might exercise if the company were being wound up by the court as respects the enforcing of calls, or any other matter.[67] If the court is satisfied that the determination of the question or the required exercise of power will be just and beneficial, it may

[61] Section 231 of Cap.32.
[62] Section 235(2) of Cap.32.
[63] See *Fowler v Commercial Timber Co Ltd* [1930] 2 KB 1.
[64] Section 238(1) of Cap.32.
[65] Section 238(2) of Cap.32. The maximum punishment is a fine at level 3. See s.351(1A) and Twelfth Schedule of Cap.32.
[66] Section 251(2) of Cap.32.
[67] Section 255(1) of Cap.32.

I. INTRODUCTION

Clawing Back, Pre and Post Petition

One of the principles underlying insolvency law is to ensure the *pari passu* doctrine, so that all unsecured creditors are treated equally. 9.001

This chapter deals with the payments made prior to the filing of the winding-up petition (unfair preferences) and those made post petition (unvalidated transactions). Whilst the operating principles which apply in these two scenarios vary; it will be seen that the law strives to strike a balance between ensuring that unsecured creditors are treated equally whilst at the same time preventing the claw back of assets where it would be inequitable to do so. It is the operation of this uneasy exercise which sometimes causes a degree of confusion when ascertaining whether some transfers should be avoided.

Introduction

The law is borrowed from the provisions set out in the Bankruptcy Ordinance (Cap.6). The relevant statutory provisions are ss.50, 51, 51A and 51B of the Bankruptcy Ordinance (Cap.6). These are modeled on ss.340, 341, 342 and 435 of the UK Insolvency Act 1986. 9.002

The law in so far as it concerns unfair preferences in the corporate insolvency context is problematic. The source of the problem lies largely in there being no enacted legislation for unfair preferences in the corporate context. Rather, the legislature has simply adopted the provisions contained in the Bankruptcy Ordinance (Cap.6) and deemed these to be part of s.266B of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32).[1] This has caused some difficulties as a result of the wholesale importation of sections of the Bankruptcy Ordinance. This is so in particular, where the analogy between a personal and corporate debtor breaks down. As will be seen below there are specific difficulties, in defining an "Associate". Many subsections in s.51B of the Bankruptcy Ordinance (Cap.6) deal with "blood" relatives of a personal debtor. This obviously has no equivalent for a corporate debtor.

The law on the matter has changed for winding-up proceedings which have commenced after 1 April 1998. Whilst it will no doubt be the case that the "old law" (for winding-up proceedings commencing before 1 April 1998) will be progressively less relevant, since it would be increasingly improbable that an action for unfair preference would still not have been dealt with by now, nevertheless, for the sake of completeness, it will be briefly be touched upon here.

Old Law

The "old law" is conveniently set out in the decision of Deputy High Court Judge S. Kwan (as she then was) in *Re Hoi Sing Construction Company Ltd*:[2] 9.003

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[1] Section 266B (1)(a) of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32) states that "a reference in s.266 or s.266A of this Ordinance to a fraudulent preference shall be deemed to be a reference to an unfair preference as provided for in s.50 of the Bankruptcy Ordinance".

[2] [2001] 2 HKC 325 at 328–330.

"The statutory provisions

43. Section 266(1) of the Companies Ordinance (now renamed the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32)) is as follows:

> 'Any conveyance, mortgage, delivery of goods, payment, execution or other act relating to property made or done by or against a company within six months before the commencement of its winding-up which, had it been made or done by or against an individual within six months before the presentation of a bankruptcy petition on which he is adjudged bankrupt, would be deemed in his bankruptcy a fraudulent preference, shall in the event of the company being wound up be deemed a fraudulent preference of its creditors and be invalid accordingly …'

44. As the commencement of the winding-up in this case was before the Bankruptcy (Amendment) Ordinance, No. 76 of 1996, came into operation on 1 April 1998, the old section 49(1) of the Bankruptcy Ordinance (Cap.6) is applicable. This section, which has been repealed, provided as follows:

> 'Every conveyance or transfer of property, or charge thereon made, every payment made, every obligation incurred and every judicial proceeding taken or suffered by any person unable to pay his debts as they become due from his own money in favour of any creditor or of any person in trust for any creditor, with a view to giving such creditor, or any surety or guarantor for the debt due to such creditor, a preference over the other creditors, shall, if the person making, taking, paying or suffering the same is adjudged bankrupt on a bankruptcy petition presented within six months … after the date of making, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy'.

The case law

46. The relevant propositions of law extracted from the cases may be set out as follows:

(1) The debtor's state of mind is the paramount consideration. The intention or view to prefer, as the immediate cause of the debtor's conduct, is the cardinal point round which the whole question turns. This is a question of fact to be derived from a review of all the circumstances of the case (*Peat v Gresham Trust Ltd* [1934] AC 252 at 262; *Banque Nationale de Paris v Sam Wah Hing Garment Factory Ltd* [1985] 2 HKC 499 at 506I; *Halsbury's Laws of England,* 4th edn, Vol 3, para.918).

(2) A limited company cannot have a view except so far as the views of the agents by which it acts. In this context, the state of mind of those in control of the company has to be examined as it is only through such persons that any view can be attributed to the debtor company (*Peat v Gresham Trust Ltd*, supra. at 261).

(3) The onus is on the person alleging a fraudulent preference to prove to the satisfaction of the court that the payment impugned was made by the debtor "with a view of" preferring the payee over his other creditors. In other words, he must prove the debtor's intention to prefer. This burden does not shift, even where it is shown that a voluntary payment has been made which in fact gives a creditor preference (*In Re Cutts* [1956] 1 WLR 728 at 733; *BNP v Sam Wah Hing Garment Factory Ltd*, supra at 506D).

(4) It is competent for the court to draw the inference of intention to prefer from all the facts of the case, particularly when there is no direct evidence of intention. But the inference should not be drawn, having regard to the situation of the onus of proof, unless such inference is the true and proper inference from the facts proved. Thus, it will not be drawn, if the inference from the facts is equivocal and, in particular, it will not be drawn from the mere circumstance that the creditor paid was in fact 'preferred', in the sense that he was paid when other creditors were not (*In Re Cutts*, supra at 733, 739).

(5) The intention to prefer, which must be proved, is the principal or dominant intention. It is recognised that there may be more than one intention involved. There may also be a valid distinction for present purposes between a view or intention to prefer and the reasons for forming and executing that intention, i.e., motive (*In Re Cutts*, supra at 734, 740, 750).

(6) The time at which the intention is adjudged is the time of payment. The section is not looking to future events in this respect (*In Re Matthews Ltd* [1982] 1 Ch 257 at 264B to D).

(7) Fraudulent preference does not necessarily involve an element of dishonesty. Nevertheless, it must be remembered that the inference to be drawn is of something which has about it, at the least, a taint of dishonesty, and, in extreme cases, much more than a mere taint of dishonesty. The court is not in the habit of drawing inferences which involve dishonesty or something approaching dishonesty unless there are solid grounds for drawing them (*BNP v Sam Wah Hing Garment Factory Ltd*, supra. at 506B; *In Re Kushler Ltd* [1943] 1 Ch 248 at 252; *Re Wing Hong Woo Co Ltd* [2000] 4 HKC 186 at 201A to C).

(8) The word 'preference' imports in it the voluntary act of a person who can do either the one thing or the other as he prefers. In as much as preference implies selection and selection implies freedom of choice, a payment must in order to constitute a preference be voluntarily made, and that a payment made under pressure, e.g., in the shape of proceedings actual or threatened by the creditor concerned, or fear of such proceedings, is not for this purpose a voluntary payment (*Butcher v Stead* (1875) LR 7 HL 839 at 846; *Sharp v Jackson* [1899] AC 419 at 423, 425, 427; *In re Cutts*, supra at 740; *BNP v Sam Wah Hing Garment Factory Ltd*, supra at 507H to I; Halsbury's Laws of England, 4th edn, Vol 3, para.914)".

Old Law v New Law

9.004 It is fundamental to understand that the "old law" has very little relevance now; and hence considerable caution should be exercised before placing any reliance on precedents based on the "old law".

In *Re MC Bacon Ltd*,[3] Millett J (as he then was) held that:

> "… [the Old law] has been replaced and its language has been entirely recast. Every word of significance, whether in the form of statutory definition or in its judicial exposition, has been jettisoned. 'View', 'dominant', 'intention' and even 'to prefer' have all been discarded. These are replaced by 'influenced', 'desire' and 'to produce in relation to that person the effect mentioned in s(4)(b). I therefore emphatically protest against the citation of cases decided under the old law. They cannot be of any assistance when the language of the statute has been so completely and deliberately changed. It may be that many of the cases which will come before the courts in future will be decided in the same way that they would have been decided under the old law. That may be so, but the grounds of decision will be different. What the court has to do is to interpret the language of the statute and apply it. It will no longer inquire whether there was 'a dominant intention to prefer' the creditor, but whether the company's decision was 'influenced by a desire to produce the effect mentioned in sub-s (4)(b)'. This is a completely different test".

His Lordship considered that there were:

> "… at least two radical departures from the old law. It is no longer necessary to establish a dominant intention to prefer. It is sufficient that the decision was influenced by the requisite desire. That is the first change. The second is that it is no longer sufficient to establish an intention to prefer. There must be a desire to produce the effect mentioned in the subsection".

In *Re Stanley Hau Po Man*,[4] Lam J adopted what Millet J had to say in *Re MC Bacon Ltd* and held that:[5]

> "His Lordship highlighted some differences between the old law and the new law and explained the requirements under the new law. In contrasting the distinction between the concept of *desire* under the new law and that of *intention* under the old law, Millett J made the following points:
>
> (a) Intention is objective, desire is subjective. A man can choose the lesser of two evils without desiring either (p.87G).
>
> (b) The relevant desire is a desire to produce the effect of putting a creditor/ surety/guarantor into a position which, in the event of the company going into insolvent liquidation, will be better than the position he would otherwise have been in (p.87H).
>
> (c) A man is not to be taken as desiring all the necessary consequences of his actions (p.87H).
>
> (d) "Some consequences may be of advantage to him and be desired by him; others may not affect him and be matters of indifference to him and while still others may be positively disadvantageous to him and not be desired by him, but be regarded by him as the unavoidable price of obtaining the desired advantages".
>
> (e) A transaction will not be set aside unless the debtor *positively* wished to improve the creditor's position in the event of his/ its own insolvent liquidation (p.88A).
>
> (f) Mere presence of the requisite desire is not sufficient. The desire must have influenced the decision to enter into the transaction. That requirement is satisfied if it was one of the factors which operated on the minds of those who made the decision. It need not be the only factor nor a decisive one (p.88B to C)".

[3] [1990] BCLC 325, at 335.

[4] [2004] 3 HKC 461. Note that while the Court of Appeal reversed part of the decision, the reasoning of his Lordship was not challenged by the Court. Both *Re MC Bacon Ltd* and *Re Stanley Hau Po Man* were applied by Kwan J in *The Official Receiver v James Conrad Louey* (unrep., HCMP 2770/2003), 2006 WL 3378766 (CFI). [2006] HKEC 2233; *Re Phantom Records Ltd* (unrep., 7 December 2006).

[5] [1990] BCC 78.

II. SUMMARY

9.005 These are the basic elements which must be in existence in order to constitute an unfair preference:

(a) a preference within the meaning of s.50(3) of the Bankruptcy Ordinance (Cap.6) was given by the bankrupt at the relevant time; this is a matter of fact. There must therefore be an antecedent debt as well as a transaction giving rise to preferential effect;

(b) the bankrupt was influenced by the requisite desire as defined in s.50(4) of the Bankruptcy Ordinance (Cap.6) when he gave the preference; where the company gives a factual preference to a connected party, this gives rise to certain presumptions; and

(c) the bankrupt was insolvent at the time of the transaction or he became insolvent in consequence of that transaction.[6]

If these requirements are met, then the Court will make such order as is necessary in order to restore the parties back to where they would be had the transaction giving rise to an "unfair preference" never taken place.[7] As will be explained below, the Court has wide discretion to make such order as appropriate. This discretion is subject to caveats; essentially that the Court should not make such orders in so far as these would injure the interests of 'innocent' third parties.[8]

[6] Section 51(2) of the Bankruptcy Ordinance (Cap.6).

[7] Section 50(2) of the Bankruptcy Ordinance (Cap.6).

[8] Section 51A(2) of the Bankruptcy Ordinance (Cap.6).

Given the fact sensitive nature (ie was the company influenced by a desire to prefer, was the company insolvent at the time of the transaction, etc) of applications to set aside transactions on the grounds of unfair preference, it will be a rare case where such proceedings can be struck out. See *Re Cheung Siu Kin* (per Poon J., 10th April 2013)

III. REQUIREMENTS

Antecedent Debt

9.006 This requirement is laid down in s.50(3)(a) of the Bankruptcy Ordinance (Cap.6). A debtor can only be preferred if he or she "is one of the debtor's creditors or a surety or guarantor for any of his debts or other liabilities".

Therefore, the starting point is that there must be a *pre existing* debtor/lender or debtor/guarantor relationship (which arose before the "relevant time"). Hence, if at the "relevant time" a company purchases goods or services and pays for these, there can be no unfair preference. This is so because the liability to pay arises at the same time as goods or services are given to the company. That relationship must be a direct one. In one case, where a billiard saloon was operating from premises leased from its directors and the company paid the rent directly to the landlord, the Court held there could be no unfair preference as there was no pre-existing borrower/lender relationship.[9]

Preferential Effect

Improving the Position

9.007 Morritt J in relation to the English equivalent of s.50(3)(b) of the Bankruptcy Ordinance (Cap.6) in *Re Ledingham-Smith*[10] had this to say:

> "The phrase 'will be better' in relation to the event of the individual's bankruptcy used in section 340(3)(b) envisages a bankruptcy after the doing of the thing in question. It also predicates that the position will be better, not may be".

The effect of the preference is thus measured as if the liquidation occurred immediately after the doing of the thing rather than when the liquidation actually occurs. This means that the creditor's position is improved by reference to a hypothetical liquidation which would arise immediately after the transaction rather than the actual liquidation when it occurs.

On the facts of that case, the court held that there was no preference because *at the time when the payment was made*, it could not be said that the payee would inevitably be benefited by the payment since further service were to be provided by the payee after the payment. There was no evidence to show that when such payment

[9] See *Re Beacon Leisure* [1992] BCLC 565. Note that there, Mr. Wright QC left open the possibility that the directors had been preferred (567h).

[10] [1993] BCLC 635.

was made, it would definitely be in excess of payment for services to be rendered in the immediate future. The evidence was that if the payment had not been made, the subsequent services would not have been rendered.

Third Party Funds

9.008 When a company is in financial difficulties, it sometimes happens that the people behind the company (often shareholders) will use their own funds to reduce the company's indebtedness. These monies paid for and on behalf of the company would in the ordinary course be construed as unsecured loans to the company. Such advances have a neutral effect on the company's overall financial position. On the one hand, one debt is extinguished, on the other there is an increase in the company's liabilities. There is at least one strong argument why s.266B of Cap.32 should not be triggered. Payments by these backers cannot be equated with the company doing "anything by itself or suffers anything to be done". These payments have, strictly speaking, nothing to do with the company.

In addition, it is arguable that nothing which has happened, offends the spirit behind the legislation, which is intended to ensure that the other creditors are not worse off.[11]

Secured and Partly Secured Creditors

9.009 It goes without saying that a secured creditor (to the extent of his security) cannot be preferred since he cannot be said to be worse off when the company goes into liquidation. If monies are repaid at the "relevant time" to a *partly* secured creditor, the preferential effect will be measured as being the amount of payment made minus the value of the security at *the time of the payment* (hence being equivalent to the unsecured amount). Hence the applicant will normally need to adduce evidence of the value of the security at the time of the transaction.

Guaranteed Debts of the Company

9.010 In a liquidation, a guarantor becomes effectively a contingent creditor. This is so, as the creditor generally has the right to sue either or both guarantor and creditor company.

When a company repays at the "relevant time", a debt which is guaranteed (by a third party), this might well improve both the creditor and the guarantor's position.[12] Whilst the guarantor might claim against the company if he has an indemnity, he will only recover a dividend upon the liquidation as an unsecured creditor; hence he is preferred to the extent that the debt guaranteed by him is paid by the company.

[11] In *James v Common Wealth Bank of Australia* [1995] 13 ACLC 1604, Young J at 1607 held that "if one can see that the position of the general creditors after the transaction was no worse than it was before the transaction then the transaction does not have the effect of giving a preference to one creditor over the others". Note however that Young J was dealing there with s.122(1) of the Bankruptcy Act 1966 which focuses on "the effect of giving that creditor a preference, priority or advantage over other creditors" whereas under Hong Kong law, the focus is simply on whether the creditor is better off than if the transaction had not been entered into. In other words, in Australia the focus in on the effect on other creditors whereas in Hong Kong, one looks at the improvement.

[12] This would be on the assumption that the debt is secured, or if it is partially secured, the preferential effect would be restricted to the unsecured part.

In short, to the extent that the debt guaranteed by the guarantor has been repaid; this will reduce the guarantor's loss on a liquidation of the company.

The applicant could in principle pursue unfair preference claims against both the creditor (say A) and the guarantor (say B) for the amounts repaid.[13] This is so as both could be said to have been put in a better position; however in practice it may well be that the applicant would have difficulties in establishing that the company desired to prefer both rather than one. As will be seen below, it is often difficult to ascertain (as there is often no direct evidence) whether the company desired to prefer A and B or whether it simply desired to prefer A with the incidental but necessary effect that it would benefit B.[14]

Common Preferences

9.011 In the Cork Report,[15] three specific examples are given as to what would constitute an act of preference: (1) payment to a creditor of his debts (in whole or in part) (2) providing security for indebtedness which arose before the 'relevant time' (3) return of goods which had been delivered but not been paid for.

Payments

9.012 Payments are the most common and straightforward form of improving a creditor's position vis-à-vis another. This clearly "has the effect of putting that person into a position" which would be better in the even of the company being declared insolvent. Obviously, when the payment is in part, the preference will extend to the extent of the payment. It is to be noted that the legislation does not require the act of preference to be narrowed to cash payments. Therefore, a transfer of an asset of the company to satisfy the payment of a debt would also be caught.[16]

Security for Indebtedness Arising Prior to the Relevant Time

9.013 When a company grants security for a previously unsecured loan, it does something which improves the unsecured creditor's position by giving him priority over the other unsecured creditors.[17]

Return of Goods

9.014 This deals with the return of goods supplied on credit. This proposition is a commonsensical one: assuming that the title to the goods has passed to the purchasing

[13] The creditor would in those circumstances be well advised to join the guarantor as a party, so that should he have to repay the Company to the extent of the preference, he could recoup it against the guarantor. Note that the Court has the power under s.51A(1)(e)–51A(1)(f) of the Bankruptcy Ordinance (Cap.6) to revive the obligations of the guarantor to the creditor, to the extent that these had originally been extinguished as a result of the preferential payment; upon the Court ordering the creditor to repay the applicant.

[14] *Re Agriplant Services Ltd* [1997] 2 BCLC 599 illustrates the difficulties involved in ascertaining whom the company desired to prefer.

[15] Para 1208 of the Cork Report.

[16] In *Weisgard v Pilkington* [1995] BCLC 1108 at 1113c, Judge Maddocks held that the transfer of leases owned by the Company to some of its directors in repayment of unsecured loans was an act of preference.

[17] For example in *Re MC Bacon* [1990] BCLC 324 the granting of a debenture to secure a previously unsecured debt was regarded as an act of preference. In *Re Mistral Finance (in liquidation)* [2001] BCLC 27 at 33 *per* Peter Smith QC, where there had been a first mortgage for the purchase of a yacht but it was void for failure of registration, and thus a second one was created during the "relevant time". That was held to be an unfair preference.

company; then the only recourse of the vendor/creditor is a claim *in personam* for monies due and owing. The vendor/creditor will only receive a dividend in the liquidation on a pari passu basis. However by having the goods supplied to it returned, it obviously becomes better off. By allowing the vendor/creditor to act as if the transaction had never been entered into, the company would be effectively releasing the vendor/creditor from its strict contractual obligations.

Court Orders

Section 50(6) of the Bankruptcy Ordinance (Cap.6) provides that: **9.015**

> "the fact that something has been done in pursuance of the order of a court, does not, without more, prevent the doing or suffering of that thing from constituting the giving of an unfair preference".

This provision is no doubt targeting at transactions disguised in Court Orders which are designed to prefer a creditor. This might be done by having a Court "sanction" it, for example by way of a consent order which is endorsed by the Court.[18] However, it goes without saying that if the Court order was obtained after a contested hearing, it may be that the requirement of "desire to prefer" could not be met.

Series of Dealings between the Parties

9.016 One can envisage a situation whereby a trading company would owe a certain amount of money to a supplier/creditor at the start of the "relevant time". During this pre-liquidation period there could be repayments for trade debts owed to the supplier/creditor and at the same time, the latter would supply the trading company with goods. If the trading company was paying for the goods freshly supplied, there would obviously be no preference issue since there would be no "antecedent debt".[19] However a problem might arise where the trading company during the "relevant time" settles debts for goods previously supplied, in order to ensure future deliveries on credit. It could be argued that there is an element of unfair preference, if one isolates that repayment as an independent transaction. It could be said that the company paid for antecedent debts and as a matter of strict law got nothing for it.

The problem is compounded for the supplier/creditor if it is repaid for "antecedent debts" on more than one occasion and supplies fresh goods to the company. That supplier/creditor could be potentially liable to repay all of the sums it received as settlement of antecedent debts. In reality, it may be that, had the supplier/creditor not been paid for its previous supplies, the company would be worse off since it would not have supplied the company which in turn might have suffered great losses as a result.

In Australia, the Courts have devised a principle whereby, the Court could, when assessing whether a creditor had been preferred; look at the broad picture of the trading relationship between the supplier/creditor and the company; rather than look at it on a

[18] For example, a Bankrupt could try to transfer valuable property to his wife by way of a consent order in a artificial divorce proceeding where the property would be transferred as part of the ancillary relief. Another example would be where a company is sued by a "friendly" creditor and makes a consent order so as to use this as an excuse to pay that creditor to the detriment of the general body of creditors.

[19] See paragraphs on antecedent debt in para.9.006.

transaction by transaction basis. This principle operates in such a way that if the other creditors are not worse off, because the supplier/creditor has supplied goods of equal or superior value to the amounts paid by the company in settlement of old debts so as to induce the creditor supplier to continue supplying it, the Court will consider that there would be no preference.[20]

It is unlikely that the Hong Kong courts will feel the need to develop a similar principle. It must be noted that in Australia:

> "… the effect of a payment on the other creditors of a debtor is determined objectively. If the payment has the effect of giving a creditor a preference over the other creditors, it does not matter that neither the creditor nor the debtor intended to give the creditor preferential treatment".[21]

The Australian legislation looks to the effect of the transaction and not to the intent, or state of mind, of the debtor.[22] As such, where the company settles old debts in order to induce the creditor supplier to supply it with fresh goods, that transaction would normally be caught by the Australian legislation; even where the other creditors in fact benefited from a series of transactions at the "relevant time" because the value of goods supplied exceed the amount settled for past deliveries. In Hong Kong however, the state of mind of the company when making payments is of crucial importance. If there is evidence that the purpose of the payment was to induce the supplier/creditor to continue to supply the company, then clearly, there could be no desire to prefer the creditor.[23]

One could argue that this device employed by the Courts in Australia was designed to mitigate the harshness of a legislation which only focuses on the effect of transactions during the "relevant time". By looking at some ongoing transactions on a global rather than an individual basis, the Australian Courts are able to rule in such a way that is 'fairer' to those supplier/creditors.[24]

It must be noted nevertheless that the outcome in Australia and in Hong Kong could still be different in some instances. Where the company settles old bills in order to induce the creditor supplier to continue to supply it with goods or services but the value of the goods or services supplied is less than the payments in settlement of old bills, then in Australia there would be a preference to the extent of the difference in value between the two.[25] In Hong Kong, there would probably be no preference, as the company might not be described as having a desire to prefer that supplier/creditor.

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[20] See the decision of the High Court of *Australia in Airservices v Ferrier* [1996] 137 ALR 609.

[21] *Australia in Airservices v Ferrier* [1996] 137 ALR 609 at 622, lines 20–30.

[22] *S Richards & Co Ltd v Lloyd* [1933] 49 CLR 49 at 62.

[23] See paragraphs 9.014–9.017.

[24] Whilst there has been support from some quarters in changing our legislation so that it looks at effect only along the lines of the Australian model; the present instance is a good example of why that change might swing the pendulum too far against supplier/creditors.

[25] *Australia in Airservices v Ferrier* [1996] 137 ALR 609 at 623. For there to be a preference in Australia, the transaction must: "have the effect of giving the creditor a preference over the other creditors, the payment must ultimately result in a decrease in the net value of the assets that are available to meet the competing demands of the other creditors".

Influenced by a Desire to Prefer

General

The law is conveniently set out by Millet J (as he then was) in *Re MC Bacon*:[26] **9.017**

> "A man is taken to intend the necessary consequences of his actions, so that an intention to grant a security to a creditor necessarily involves an intention to prefer that creditor in the event of insolvency. The need to establish that such intention was dominant was essential under the old law to prevent perfectly proper transactions from being struck down. With the abolition of that requirement intention could not remain the relevant test. Desire has been substituted. That is a very different matter. Intention is objective, desire is subjective. A man can choose the lesser of two evils without desiring either. It is not, however, sufficient to establish a desire to make the payment or grant the security which it is sought to avoid. There must have been a desire to produce the effect mentioned in the subsection, that is to say, to improve the creditor's position in the event of an insolvent liquidation. A man is not to be taken as desiring all the necessary consequences of his actions. Some consequences may be of advantage to him and be desired by him; others may not affect him and be matters of indifference to him; while still others may be positively disadvantageous to him and not be desired by him, but be regarded by him as the unavoidable price of obtaining the desired advantages. It will still be possible to provide assistance to a company in financial difficulties provided that the company is actuated only by proper commercial considerations. Under the new regime a transaction will not be set aside as a voidable preference unless the company positively wished to improve the creditor's position in the event of its own insolvent liquidation".

The applicable principles have been considered above.[27]

The applicant does not have to produce direct evidence (and more often that not simply cannot) of the requisite desire; its existence may be inferred from the circumstances of the case.[28] However it will be insufficient to simply point to the fact that there was a preference in favour of the creditor and hence ask the Court to infer that, *ipso facto*, there must have been a desire to prefer that creditor. For the application to succeed, more evidence is required.

It is thus clear that as a matter of Hong Kong law, if the company is doing an act which has the effect of preferring a creditor, but it has done so as a result of the creditor exercising pressure (commercial or otherwise) on it then that is not a payment which can be recovered as being a preferential payment.[29]

Whether the company was influenced by a desire to prefer a particular creditor is a matter of fact to be determined in each individual case having regard to the totality of

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[26] [1990] BCLC 324 at 335–336. Applied in *The Official Receiver v James Conrad Louey* (unrep., HCMP 2770/2003) at [87] and cited with approval in *Re Sweetmart Garment Works Ltd* [2008] 2 HKLRD 92.

[27] See para.9.004.

[28] *Re MC Bacon* [1990] BCLC 324. Applied in *The Official Receiver v James Conrad Louey* (unrep., HCMP 2770/2003) at [87].

[29] See n 34.

I. OVERVIEW*

12.001 The cross-border aspects of corporate insolvency raise complex issues arising from the fact that different jurisdictions have a diversity of laws and practices for dealing with such matters. The importance of this issue has gained greater prominence because in a globalized market place it is not unusual for companies to have business dealings, operations, and assets in many countries. As such, when companies face financial distress or have collapsed, creditors in multiple jurisdictions compete for whatever assets these entities possess across a number of jurisdictions. However, in the absence of a harmonization of these laws, there has been a historical tendency for each jurisdiction to view assets and liabilities under its control in isolation. The result has often been economically harmful chaos. Such sentiments became more acute in the post Global Financial Crisis economic climate. Hence, Hong Kong's courts will most likely hear more cross-border corporate insolvency cases as the territory is a host to a large number of overseas companies, as well as offshore investors.

Over the years a more rational approach has developed and the Hong Kong courts have proved keen to deal with such matters in a broad spirit of comity, albeit that this is made more difficult by the relatively basic statutory provisions, with much having been left to judicial ingenuity, and with important uncertainties still remaining.[1] The major themes discussed in this chapter are as follows:

- *The territorial reach of the Hong Kong courts' corporate insolvency jurisdiction*: the major question here concerns the circumstances in which the Hong Kong court will assume jurisdiction to wind up a foreign company, or to appoint provisional liquidators or approve a scheme of arrangement. See paragraphs 12.002 to 12.015 below.
- *The interaction between Hong Kong and foreign courts in the exercise of a corporate insolvency jurisdiction*: the major issues here concern the notion of principal and ancillary jurisdictions, the ideal being that the ancillary jurisdiction will defer to the principal jurisdiction on most important matters, with a view to bringing about a just, practical and economically rational winding-up of affairs. A relatively recent development in connection with this ideal concerns the judicial promotion of court-endorsed agreements known as "crossborder protocols" between liquidators and similar officers appointed in different jurisdictions. It is important in this context, however, not to lose sight of the fact that certain matters of "administration" always remain governed by Hong Kong law. See paragraphs 12.016 to 12.032 below.

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* There are a number of useful monographs written primarily from an English law perspective to which the Hong Kong reader may find it useful to refer: see Sheldon, *Cross-Border Insolvency*, 3rd edn (Bloomsbury Professional, 2011); Fletcher, *Insolvency in Private International Law*, 2nd edn (Oxford: Oxford University Press, 2007); Bloxham and Baird, "Cross-Frontier Issues", (2002) in *Tolley's Insolvency Law* (London: Butterworths, 1996–2005).

[1] Note that the (new) Companies Ordinance (Cap.622) came into effect in March 2014. The winding-up and insolvency related provisions have survived and have since been retiled as the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32).

- *Ancillary applications in the course of a winding-up*: a number of intricate issues arise in connection with the cross-border aspects of certain applications often made in the course of a winding-up. As will be seen, the Hong Kong courts have taken a flexible approach. See paragraphs 12.033 to 12.041 below.
- *The cross-border effect of court orders*: a Hong Kong court will regard its own winding-up order as having, at least in so far as not expressly limited, broad effects in respect of a company's assets. Similarly, a Hong Kong court's approval of a scheme of arrangement will be regarded, by a Hong Kong court at least, as operating as a universal discharge of liabilities. The principles governing a Hong Kong court's recognition of the vesting or discharging effects of a non-Hong Kong court order are, however, considerably more nuanced. See paragraphs 12.042 to 12.053 below.
- *Reform*: the need for reform of Hong Kong cross-border insolvency law is perhaps not as urgent as it was once thought to be, since the judges in Hong Kong have started to make progress towards filling many of the important gaps. Nevertheless, that process has its limitations. The enactment of the UNCITRAL Model Law on Cross-Border Insolvency remains a possibility, but as yet no concrete steps have been taken for this purpose in Hong Kong.[2]

II. CROSS-BORDER REACH OF THE HONG KONG COURTS' JURISDICTION

Introduction

12.002 The issues discussed in this section principally concern the extent to which the Hong Kong court has jurisdiction over non-Hong Kong companies and other non-Hong Kong business organisations. As will be seen, there is broad jurisdiction in theory, defined by five alternative circumstances discussed below. There are, however, some judicially-imposed limitations upon its exercise, known as the "three core requirements", albeit expressed in terms which permit a certain flexibility of assessment. The jurisdiction extends to the appointment of provisional liquidators; an important point given that provisional liquidators are now commonly appointed in Hong Kong to assist with company restructuring rather than as a precursor to winding-up. As will be seen, there is clearly jurisdiction to approve schemes of arrangement in respect of non-Hong Kong companies which are insolvent, but some scope for debate outside the insolvency context. This section closes with discussion of certain issues of cross-border service of documents in respect of which the law is somewhat obscure and often causes confusion.

[2] For a discussion on the nature and application of the UNCITRAL Model Law on Cross-Border Insolvency in Great Britain, see Goode, *Principles of Corporate Insolvency Law*, 4th edn (London: Sweet & Maxwell, 2011), p.793–818

Different Categories of "Company"

12.003 The Hong Kong court has jurisdiction to wind-up the affairs of any company incorporated in Hong Kong irrespective of whether: (i) it does, or has ever done, business in Hong Kong; (ii) it has assets in Hong Kong; or (iii) its shareholders or directors have anything to do with Hong Kong.[3] This is unsurprising as details of the applicable winding-up regime are discussed elsewhere in this book. However, what may be more surprising to the uninitiated is that the Hong Kong courts' winding-up jurisdiction has long extended to companies incorporated outside Hong Kong as these are referred to in the legislation as "unregistered companies".[4] The following points should be noted:

(1) The phrase "unregistered companies" is confusing in at least two respects, in that it includes: (i) entities other than companies and (ii) entities which have been registered outside or within Hong Kong, or both. However, the phrase is well entrenched and will be used in this chapter;

(2) The venerable statutory phrase "oversea companies" (replaced in July 2005 with the new phrase "non-Hong Kong companies") has a different technical meaning and should not be confused with the notion of "unregistered companies";

(3) In marked contrast with the position in respect of the bankruptcy of individuals[5] or in respect of *in personam* actions in the Hong Kong courts,[6] the restrictions

[3] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.176, which simply provides that: "The Court of First Instance shall have jurisdiction to wind up any company". "Company" has a special narrow meaning in this context: a company incorporated under the Companies Ordinance (Cap.622) or under the predecessor Companies Ordinance (CO): see s.2 (definitions of "company" and "existing company").

[4] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), Part X (Winding-Up of Unregistered Companies), ss.326 to 331A. The statutory words are rather inadequate, in that s.326(1) provides that "unregistered company" includes, *inter alia*, any "company" other than one "registered' under the Companies Ordinance and its predecessor. This is confusing for two reasons: (i) "company" is defined in s.2 to mean only a company registered under the Hong Kong Companies Ordinance and its predecessors, a definition which, if applied to s.326(1), would nullify the scope of Part X, and (ii) Part 16 of the Companies Ordinance provides for "registration" of certain companies incorporated overseas. Note that point (i) does not appear to have been argued in Hong Kong and it is suggested that it is plainly bad; and point (ii) has been argued but has been rejected by the court "as suffering from the classic mistake of taking words out of context and construing them on their own." See *Securities and Futures Commission v MKI Corporation Ltd* [1995] 2 HKC 79, Rogers J, as the court pointed out, the adoption of a more literal construction of s.326(1): "would mean a company which has not established a place of business in Hong Kong could be wound up by the Hong Kong Court, whereas a company which has established a place of business and has become registered in Hong Kong could not be wound up. That seems to me, at the very least, would make it a very odd piece of legislation". The effect of this first instance decision was subsequently confirmed by the legislature by way of amendment of s.326(2) of Cap.32 to clarify the point "for avoidance of doubt". The important practical point to note is that "oversea" companies registered under Part XI are therefore subject to the "foreign company" rather than "domestic company" winding-up provisions of Cap.32. An argument related to point (i) was recently taken in England, in an attempt to convince the court that the winding-up jurisdiction in respect of foreign companies was limited to companies which had a place of business in England; that attempt failed, as it should fail in Hong Kong if ever made: *Mazur Media Ltd v Mazur Media GmbH* [2004] EWHC 1566 (Ch), [2004] 1 WLR 2966 Lawrence Collins J.

[5] See Bankruptcy Ordinance (Cap.6), s.4: a bankruptcy petition may not be presented unless the individual debtor is domiciled in Hong Kong, or present in Hong Kong on the day of presentation, or has, at any time in the three years immediately preceding presentation, been ordinarily resident in Hong Kong or has had a place of residence in Hong Kong or has carried on business in Hong Kong.

[6] See Johnston, *The Conflict of Laws in Hong Kong*, 2nd edn (London: Sweet & Maxwell, 2012), Chapter 3.

on the international reach of this jurisdiction mostly consist of broad and flexible principles rather than precisely drawn connecting factors; and

(4) Once jurisdiction has been established over an unregistered company, the court's powers are broadly similar to those in respect of Hong Kong companies but, as will be seen below, their exercise is often significantly different.

Definition of "Unregistered Company"

12.004 The definition of an "unregistered company" under the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32) provisions discussed above extends to:

(1) "Any company" other than a company incorporated under Hong Kong law. Given that the words used in the Ordinance are capable, on their face, of different meanings, it is worth clarifying that the concept includes companies incorporated in Mainland China or Macau as well as companies incorporated abroad.[7] It also encompasses companies incorporated in Taiwan, notwithstanding that the Government of the People's Republic of China does not recognise the Government which exercises *de facto* authority over Taiwan.[8] It is irrelevant for this purpose whether the company in question is registered in Hong Kong under Part 16 of the Companies Ordinance; and[9]

(2) "Any partnership whether limited or not" and any "association" other than: (i) a partnership, association or company which consists of fewer than eight members and is not formed or established outside Hong Kong; and (ii) a partnership registered under the Limited Partnerships Ordinance.[10] It therefore encompasses, for example, non-Hong Kong general partnerships, limited partnerships and limited liability partnerships.[11] It is however also possible to seek a bankruptcy order under the Bankruptcy Ordinance against a partnership, in its firm name, which does business in Hong Kong[12] and "such a bankruptcy order shall affect the joint and several property of all

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7 See *MKI Corporation Ltd*, [1995] 2 HKC 79, above.

8 This is clear from reading Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.326(1) and the Foreign Corporations Ordinance (Cap.437), s.2 together: the latter provides for recognition of legal personality of "bodies" with "corporate status" by the Hong Kong courts where such status is conferred by "the laws of a territory outside Hong Kong which is not at that time a recognised State" if "it appears that the laws of that territory are at [the] time [that the question arises before the Hong Kong court] applied by a settled court system in that territory." The concept of a "recognised state" is defined by Foreign Corporations Ordinance (Cap.437), s.2(2)(a) with reference to recognition by Her Majesty's Government in the United Kingdom, but this is to be interpreted post-1 July 1997 as a reference to recognition by the Central People's Government of the People's Republic of China (see Interpretation and General Clauses Ordinance (Cap.1), Sch 8, para.1(b)). See *Chen Li Hung v Ting Lei Miao* (2003) 3 HKCFAR 9.

9 Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.326(2) declares: "for the avoidance of doubt" that the concept includes a registered non-Hong Kong company.

10 Limited Partnerships Ordinance (Cap.37).

11 With reference to an LLP, that is, a foreign corporate entity having legal personality but called a "partnership", it seems best to regard it as a "company" within the meaning of s.326. Practically speaking, it does not matter whether it is regarded as a "company" or "partnership" for winding-up purposes, but the distinction is important under s.168A in connection with the jurisdiction to disqualify directors: see para.12.039 below.

12 Bankruptcy Ordinance (Cap.6), s.7(1).

the partners"[13] notwithstanding that "all or any of the partners of the firm are not resident or domiciled in Hong Kong".[14] Where proceedings are brought under the two different Ordinances, or where one Ordinance's regime appear more appropriate in a case where both potentially apply, it is suggested that the court's discretionary power to stay proceedings should be exercised so as to prevent wasteful duplication.

The concept of "unregistered company" is wide enough to encompass most entities or associations in the broadest sense, whether incorporated or not, provided that they were formed for gain or profit,[15] whether lawful or unlawful.[16] The jurisdiction extends to state-owned enterprises,[17] though not to enterprises formed by international treaty between a number of states.[18] The judicially approved test for limiting the wide word "association" is, at least, no more precise than a consideration of whether the legislature "cannot reasonably have intended" there to be jurisdiction to wind up a particular type of association.[19]

The Distinction between Winding-Up and Dissolution

12.005 Although the phrase "winding-up a company" (rather than "winding-up the affairs of a company") has long been the official legal usage, winding-up does not affect the company's legal personality as such. Winding-Up is a process relating to the

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13 Bankruptcy Ordinance (Cap.6), s.7(1)(b).

14 *Ibid.*, s.7(1)(c).

15 *Re St James's Club* (1852) 2 De GM & G 383, a decision of Lord St Leonards LC, sitting as the Court of Appeal in Chancery, holding that a social club was not an "association" within the meaning of the Joint Stock Companies Winding-Up Amendment Act 1849: "Though 'associations' are mentioned, I cannot think that word is to be treated without regard to the particulars with which it is associated … I will not say what associations are within the Acts; but, bearing in mind that the individuals who form a club do not constitute a partnership, nor incur any liability as such, I think associations of that nature are not within the Winding-Up Acts. I find in all these Acts to which I have referred, that every provision is inconsistent with including such an association as this club is. If such had been the intention of the Legislature, why should not the word 'club' have been expressly mentioned? If, however, the Legislature has used ambiguous expressions, I will not extend their signification beyond their natural import. At first sight, the word 'association' would seem to include the case of clubs, but in looking at the context, I am clearly of opinion that it does not".

16 See the case of *Re Senator Hanseatische Verwaltungsgesellschaft mbH* [1996] 4 All ER 933, CA (Eng), for an example in which a foreign company whose sole or main business was criminally unlawful (a pyramid scheme) was wound up on the "just and equitable" ground.

17 See *Re Zhu Kuan Group Company Ltd*, (unrep., 2 August 2004, HCCW 874/2003, Barma J) (Hong Kong court having power to wind up a Mainland China state-owned enterprise).

18 *Re International Tin Council* [1989] Ch 309, [1988] 3 All ER 257, CA (Eng). In that case, the petitioners argued that the *ratio* of the *St James's Club* decision was simply that the court does not have jurisdiction to wind up "associations which do not carry on business". However, the Court of Appeal held that the absence of jurisdiction was to be more broadly understood, since Parliament could not reasonably have intended a treaty-based organisation to be subject to winding-up in the English Court, approving the reasoning of Millett J at first instance: "Sovereign states are free, if they wish, to carry on a collective enterprise through the medium of an ordinary commercial company incorporated in the territory of one of their number. But if they choose instead to carry it on through the medium of an international organisation, no one member state, by executive, legislative or judicial action, can assume the management of the enterprise and subject it to its own domestic law. For if one could, then all could; and the independence and international character of the organisation would be fragmented and destroyed. And if a member state has no such right, then *a fortiori* a non-member state has none. In my judgment, to impute to Parliament an intention, by general words only, to confer on the court a jurisdiction contrary to these principles and without precedent is unacceptable".

19 *Re International Tin Council* (n 18).

management of the company's affairs, the settling of its liabilities and the distribution of its assets. Although in the case of a Hong Kong company it is usually followed by a dissolution, the two matters are distinct.[20] This point has two main aspects: first, and as one would expect, the Hong Kong court has no power to dissolve a non-Hong Kong company; secondly, the fact that a non-Hong Kong company has already been dissolved under the laws of its place of incorporation does not prevent the Hong Kong court from winding it up.[21]

The Five Alternative Circumstances in which an Unregistered Company may be Wound Up by the Hong Kong Court

12.006 The circumstances in which an unregistered company may be wound up by the Hong Kong court are where:

(1) it has been dissolved;[22]

(2) it has ceased to carry on business;[23]

(3) it is carrying on business only for the purpose of winding-up its affairs;[24]

(4) it is unable to pay its debts;[25] or

(5) the court is of opinion that it is just and equitable that it should be wound up.[26]

It is usually possible to satisfy one or more of these conditions[27] in a case where the petitioner has some rational reason for seeking to wind up the company.[28] Unlike a Hong Kong company, however, an unregistered company may not be wound up

[20] Thus, for example, a definition of winding-up as "a collective insolvency process leading to the end of the company's existence (dissolution)" (Goode, *Principles of Corporate Insolvency Law*, 4th edn, London, Sweet & Maxwell, 2011) is perfectly serviceable to describe an ordinary purely domestic winding-up, but is not apposite to describe a Hong Kong court's exercise of its winding-up jurisdiction over a foreign company, which may not necessarily result in dissolution.

[21] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327A: "Where a company incorporated outside Hong Kong which has been carrying on business in Hong Kong ceases to carry on business in Hong Kong, it may be wound up as an unregistered company under this Part, notwithstanding that it has been dissolved or otherwise ceased to exist as a company under or by virtue of the laws of the place of its incorporation". Indeed, under s.327(3)(a), the fact that a non-Hong Kong company has been dissolved is one ground on which it may be wound up.

[22] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(3)(a).

[23] *Ibid.*

[24] *Ibid.*

[25] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(3)(b).

[26] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(3)(c). Winding-up on the "just and equitable" ground is discussed elsewhere in this book.

[27] Section 327(3)(a) of Cap.32 contains an "or" between its three limbs. Paragraphs (a), (b) and (c) are separated merely by semi-colons, without an "or" or "and", but the English Court of Appeal long ago confirmed that the equivalent English statutory words are disjunctive: *Banque des Marchands de Moscou (Koupetschesky) v Kindersley* [1951] Ch 112 at 125, [1950] 2 All ER 549 at 555, *per* Evershed MR: "This form of words is substantially identical with that which has consistently appeared in all the relevant legislation since the Act of 1848 (11 and 12 Vict, c 45). As a matter of language it is plain that the three conditions named are independent and not cumulative". The words are now to be found, in England, in the Insolvency Act 1986, s.221(5).

[28] Contrast the position in individual bankruptcy, in which one of a number of much more narrowly drawn jurisdictional heads must be satisfied.

voluntarily by the Hong Kong court.[29] In connection with circumstance (4), inability to pay debts, the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32) provides that such inability may be demonstrated by any one of the following four means, the first of which is of most practical importance (all of these means of demonstrating inability to pay debts can be rebutted in the usual ways discussed elsewhere in this publication):

(i) *Statutory demand duly served and not satisfied within 3 weeks*: inability to pay debts may be established by a creditor,[30] to whom the company is indebted for HK$10,000 or more,[31] serving on the company, by one of the means discussed at paragraph 12.012 below, a demand signed by the creditor[32] requiring the company to pay the sum so due: if the company, for three weeks after the service of the demand, neglects to pay the sum or to secure or compound for it to the satisfaction of the creditor then the court may conclude on that basis that the company is unable to pay its debts.[33] There is no statutorily prescribed form for such a demand,[34] but safe accepted practice is to use the following form of words:

"Statutory Demand

Section 327(4)(a) of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance, Cap.32 of the Laws of Hong Kong

To: [Name of debtor]

For the attention of [insert the name of the governing body, e.g. the Board of Directors. In the case of a non-Hong Kong debtor company which is registered under Part 16 of the Companies Ordinance, insert the name of the registered authorised representative]

Dear Sirs,

We, [name of creditor] of [address of creditor] HEREBY DEMAND payment of the amount now due by you to us, pursuant to [describe the instrument, judgment or other matter sufficient to identify the debt], of [specify currency and sum due in both words and figures]

[29] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(2). The issue of voluntary winding-up, as opposed to a compulsory winding-up by the court, was affirmed in *Re ECM Real Estate A.G.* (in liq.) [2014] 1 HKC 78.

[30] The statute specifies that the creditor may be "by assignment or otherwise".

[31] The Financial Secretary has power under s.327(6) of Cap.32 to change this sum.

[32] The statutory wording is "under his hand".

[33] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(4)(a).

[34] Hong Kong corporate insolvency law has no equivalent to (i) the detailed provisions of the Bankruptcy Ordinance and Bankruptcy Rules in respect of statutory demands addressed to individuals or (ii) the provisions as to the form and content of statutory demands in respect of companies under the English Insolvency Rules (rr 4.4 to 4.6). But a prescribed form of statutory demand for corporate insolvency is proposed by the Improvement of Corporate Insolvency Law Legislative Proposals Consultation Document, April 2013: available at www.fstb.gov.hk; Financial Services Bureau, Publications-Consultation Papers.

AND TAKE NOTICE that if the said sum is not paid by you to us at our address given above within twenty one (21) days of the date of service of this notice upon you or if you do not secure or compound for the said sum to our reasonable satisfaction we shall proceed under the provisions of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32) for the winding-up of your company by the Court.

Dated this [ ] day of [month, year].

Yours faithfully,

[Name of individual signing: if creditor is not an individual, also state signatory's position, e.g. director, and insert the words "for and on behalf of [creditor]"]

(ii) *Proceedings against member*: secondly, inability to pay debts may be established by showing that any action or other proceeding has been instituted against any member for any debt or demand due, or claimed to be due, from the company, or from him in his character of member and, notice in writing of the institution of the action or proceeding having been served on the company by leaving the same at its principal place of business, or by delivering it to any officer of the company, or by otherwise serving the same in such manner as the court may approve or direct, the company has not within 10 days after service of the notice paid, secured or compounded for the debt or demand, or procured the action or proceeding to be stayed, or indemnified the defendant to his reasonable satisfaction against the action or proceeding, and against all costs, damages and expenses to be incurred by him by reason of the same.[35]

(iii) *Failure to satisfy judgment*: thirdly, inability to pay debts may be established by showing that execution or other process issued on a judgment, decree or order obtained in any court in favour of a creditor against the company, or any member thereof as such, or any person authorised to be sued as nominal defendant on behalf of the company, has been returned unsatisfied.[36]

(iv) Residual: fourthly, it may be otherwise proved to the satisfaction of the court that the company is unable to pay its debts.[37] In practice, this will be relevant in cases where it is impracticable to serve a statutory demand or to wait for the prescribed three weeks before commencing winding-up proceedings.

Save for these special rules, the provisions of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32) with respect to winding-up apply to

[35] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(4)(b).
[36] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(4)(c).
[37] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(4)(d).

non-Hong Kong companies as they do to Hong Kong companies,[38] with the minor exception of a special definition of contributories.[39]

The Three Core Requirements for Taking Jurisdiction in Respect of an Unregistered Company

12.007 Even if one of the five conditions mentioned above is satisfied, the Hong Kong courts recognise certain limits upon the *exercise* of jurisdiction in respect of the winding-up of unregistered companies.[40] It used to be thought that the presence of assets in Hong Kong was a pre-condition of the exercise of jurisdiction but it has now been

[38] Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.327(1). Section 331 goes on to provide that the provisions of Part X (ss.326 to 331A) with respect to non-Hong Kong companies are: "in addition to and not in restriction of any provisions hereinbefore in this Ordinance contained with respect to winding-up companies by the court, and the court or liquidator may exercise any powers or do any act in the case of unregistered companies which might be exercised or done by it or him in winding-up companies formed and registered under the (new) Companies Ordinance (Cap.622): Provided that an unregistered company shall not, except in the event of its being wound up, be deemed to be a company under this Ordinance, and then only to the extent provided by this Chapter".

[39] See Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), s.328 (*cf* the somewhat less extensive definition in s.171 in connection with Hong Kong companies). Nominally there are also special provisions for the stay of proceedings against non-Hong Kong companies and contributories in connection with a winding-up: ss.329 and 330. However, these mirror ss.324 and 325 in respect of Hong Kong companies.

[40] *Securities and Futures Commission v MKI Corporation* [1995] 2 HKC 79, above, in which Rogers J relied principally on the English decision of *In re a Company (No. 00359 of 1987)* [1988] 1 Ch 210; also reported sub nom *International Westminster Bank plc v Okeanos Maritime Corporation* [1987] BCLC 450, [1987] 2 All ER 137. In *Okeanos*, the company had no assets in the jurisdiction and the purpose of the winding-up petition was to enable claims for fraudulent and wrongful trading to be brought under the English Insolvency Act 1986: in Hong Kong, there is liability for fraudulent trading under s.275 of the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32), but no equivalent to the more stringent English concept of wrongful trading. In *Re Irish Shipping Ltd* [1985] HKLR 437, HC, Jones J took jurisdiction to wind up an Irish company already wound up in Ireland on the ground that there were assets (namely, a ship) in Hong Kong, relying on *In Re Compania Merabello* [1973] 1 Ch 75, in which Megarry V-C said: "I would accordingly attempt to summarise the essentials of the relevant law relating to the existence of jurisdiction to make a winding-up order in normal case in respect of a foreign company as follows: (1) There is no need to establish that the company ever had a place of business here. (2) There is no need to establish that the company ever carried on business here, unless perhaps the petition is based upon the company carrying on or having carried on business. (3) A proper connection with the jurisdiction must be established by sufficient evidence to show (a) that the company has some asset or assets within the jurisdiction, and (b) that there are one or more persons concerned in the proper distribution of assets over whom the jurisdiction is exercisable. (4) It suffices if the assets of the company within the jurisdiction are of any nature; they need not be "commercial" assets, or assets which indicate that the company formerly carried on business here. (5) The assets need not be assets which will be distributable to creditors by the liquidator in the winding-up: it suffices if by the making of the winding-up order they will be of benefit to a creditor or creditors in some other way. (6) If it is shown that there is no reasonable possibility of benefit accruing to creditors from making the winding-up order, the jurisdiction is excluded". Furthermore, it has been found that where the three core requirements are not satisfied, the fact that the winding-up of a foreign company would assist a foreign liquidator in carrying out his duties alone is not sufficient grounds for the court to order it; *Re Pioneer Iron and Steel Co Ltd* (unrep., 6 March 2013, HCCW 322/2010, Harris J). Also, the case of *MKI Corporation* [1995] 2 HKC 79 makes clear that the jurisdiction is no longer limited to cases where there are assets in Hong Kong: see now the more recent English authorities discussed below. As Rogers J noted in *MKI Corporation*, Knox J in *Re Real Estate Development Co* [1991] BCLC 210 added that the court must be able to exercise jurisdiction over one or more persons interested in the distribution of the company's assets: the subsequent English decisions on that subject are discussed below; Rogers J also referred to *Re Hibernian Merchants Ltd* [1958] 1 Ch 76, [1957] 3 All ER 97, albeit noting that that case was unopposed.