Part III Diverse Cross-border Insolvency Systems among the Four Regions

Introduction

3.01 The main topic of this part focuses on what the current cross-border insolvency systems among the four regions are. The part is composed of four chapters, in which the individual cross-border insolvency system in each region will be introduced and analyzed. For each region, the introduction will start with a general overview of the local insolvency system. Further, the features and problems of the cross-border insolvency system in each region will be demonstrated in depth through legislation and case law (Please also refer to Annex III, in which the main lines of the insolvency systems among the four regions have been briefly outlined and summarized comparatively in the form of table.). In the end, comparison and summary of the cross-border insolvency systems among the four regions will be presented in the pre-conclusion.

Ch. 1 The Mainland Approach

3.02 In the Mainland, the development of cross-border insolvency law is interrelated to the reform of local insolvency system. In this chapter, the corporate insolvency system of the Mainland is reviewed at first, including the history of the corporate insolvency system and a general description of the current insolvency system. Further, the development of cross-border insolvency system is also briefly addressed. The current cross-border insolvency system is based on one article, the key elements of which are to be analyzed in detail by referring to relevant case law.

1.5 Brief Introduction into National Bankruptcy Law

3.03 In this section, the former corporate insolvency system is briefly reviewed, which was a dual national bankruptcy system according to different types of debtors. It represented struggles between the government control and market economy demand, the national efforts and the local initiatives. With new EBL's entry into effect in 2007, a comprehensive corporate insolvency system was built up and an era of separate legislation on state and non-state owned corporation insolvency was over.

1.5.1 Corporate Insolvency System of P.R.C. in History

3.04 From 1986 to 2006 the bankruptcy legal system in the Mainland China was composed of

(1) Enterprise Bankruptcy Law (for trial implementation)[135];
(2) Civil Procedure Law and Companies Law;
(3) Related judicial interpretations;
(4) Policy decrees and administrative regulations;
(5) Local rules and regulations.

[135] Hereinafter, the 1986 EBL

3.05 These five components disclosed that China's former bankruptcy law system was not in a uniform way. Before 1986 there was no bankruptcy law in China. Due to the highly centralized planned economy, the state-owned enterprises (hereinafter SOE), which existed and grew under the control of the government, were the main form of economic entity during that period. If a SOE did not do its business well, the government subsidized it to facilitate continued operations[136]. Therefore it is not surprising that the enterprises at that time had no idea about bankruptcy because it hardly happened.[137] Nevertheless, the government realized that it was not a long-term solution to keep rescuing the SOEs with the state finance.[138]

3.06 On 12 December, 1986, the 1986 EBL, the first bankruptcy law of P.R.C. was adopted, which was a remarkable commencement and a special insolvency legal regime against China's economic background at that moment. First of all, considering the economic structure at that time, the 1986 EBL only applied to the state-owned enterprises.[139] Secondly, pursuant to the 1986 EBL, the government played a significant role in the bankruptcy proceedings. For instance, a debtor can only apply for bankruptcy upon the government approval.[140] Besides, the government was in charge of the whole reconciliation-readjustment procedure.[141] In addition, the government was the statutory member of the liquidation committee.[142] Last but not the least, the employees of the insolvent debtors were highly protected by the 1986 EBL. It was stated in the 1986 EBL that the government should arrange new jobs through various channels for the workers of the bankrupt enterprises and guarantee their basic living necessities before they were reemployed.[143]

3.07 With the development of economic reform in the Mainland,[144] the non-state-owned enterprises were gradually incorporated into the bankruptcy

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[136] Stevens, Neal, Confronting the Crisis of Insolvency in China's State-owned Enterprises: Can the Proposed Bankruptcy Law Erase the Red Ink?, in: Wisconsin International Law Journal, 1998, 554.

[137] It was not until on August 3, 1986, was Shenyang Province Explosion-proof Equipment Factory the first bankrupt enterprise in China just before the 1986 EBL was adopted. It is so-called an administrative bankruptcy in accordance with the local government decree (1985 No. 24 Shenyang Government) and in the form of the recall of business license by the local administrative department for industry and commerce.

[138] Peng Zhen (the former chairman of the Standing Committee of the National People's Congress - China's legislature), The Bankruptcy Law is also the Promotion Law (in Chinese), in: People's Daily, 30/11/1986, 01.

[139] The 1986 EBL, article 2: This law applies to the enterprises owned by the whole people. In pursuant to the Constitution Law of P.R.C., article 7: The State-owned economy, namely, the socialist economy under ownership by the whole people. Therefore, 1986 EBL actually applied to the state-owned enterprises alone.

[140] The 1986 EBL, article 8.

[141] The 1986 EBL, Chapter 4 Reconciliation and Readjustment

[142] The 1986 EBL, article 24

[143] The 1986 EBL, article 4

[144] The bulk of the change in ownership structure in the Chinese economy occurred through the growth of non-state producers, including collective, private and foreign invested firms. Chronic loss-making enterprises were closed down or sold off. The total number of industrial SOEs dropped from 120,000 in the mid-1990 to only 31,750 in 2004. See Naughton, Barry, Growing

system. Adopted on April 9, 1991, the Civil Procedure Law embraced one new chapter (Chapter XIX), entitled Procedure for Bankruptcy and Debt Repayment of Legal Person Enterprises, which provided the general legal foundation for bankruptcy of the non-state-owned enterprises. In addition, pursuant to Chapter VIII of the Companies Law,[145] in which difference of ownership was no longer emphasized,[146] it was required that once the liquidation committee discovered the insolvency, it should apply to the court for a declaration of bankruptcy of the company. If the court declared that the company was bankrupt, the liquidation committee should hand over the liquidation affaires to the court.[147]

3.08 The Supreme People's Court of P.R.C. attempted to address these problems in practice by issuing several judicial interpretations.[148] In particular, the 2002 Provisions on Bankruptcy Cases[149], with 106 articles (almost three times as long as the bankruptcy law itself), was a very comprehensive interpretation with respect to the 1986 EBL. The highlight of the 2002 Provisions on Bankruptcy Cases was that it applied to both SOEs and non-SOEs,[150] which appearred to be an attempt by the Supreme People's Court to set uniform rules that govern the both.[151]

3.09 The government also promulgated number of policy decrees and administrative regulations. Those decrees and administrative regulations mainly

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out of the Plan: Chinese Economic Reform, 1978-1993, Cambridge University Press, 1995, p. 137-168; Naughton, Barry, The Chinese Economy: Transitions and Growth, The MIT Press, 2006, p. 105-106.

[145] The Companies Law was adopted on December 29, 1993, revised on December 25, 1999, 2005 and 2013.

[146] The Companies Law (1993), article 1, 7

[147] Id.

[148] In China the legal effect of the judicial interpretations used to be not very clear in theory but quite obvious in practice. . Pursuant to the Rules of Supreme People's Courts on the Judicial Interpretation, issued on June 23, 1997, revised on March 23, 2007 (No.12 [2007] of the Supreme People's Court), the judicial interpretation is made by the Supreme People's Court when people's courts meet the problems of application of laws in the trial. It also stimulates that the judicial interpretations have the same effect as laws. The judges simply apply the judicial interpretations in making decisions without doubting their effects. According to the former Legislation Law of P.R.C. (article 42 and 43) prescribes that the power of legal interpretation belongs to the Standing Committee of the National People's Congress alone. The Supreme People's Court may request the Standing Committee of the National People's Congress to give legal interpretation. The Supreme People's Court issued a rule itself to justify the legal effect of the judicial interpretations. On 15 March 2015, the Legislation Law was amended, which allows the Supreme People's Court to make interpretations concerning application of laws in the course of adjudication work. The interpretations shall refer to specific articles or provisions of laws in conformity with the objectives, principles and original meaning of laws and shall be reported to the Standing Committee of the National People's Congress for recordation within 30 days of issuance. (2015 Legislation Law, article 104)

[149] 2002 Provisions on Some Issues concerning the Trial of Enterprise Bankruptcy Cases of the Supreme People's Court, Interpretation No. 23 [2002], issued on July 30, 2002. It superseded the earlier interpretations (the 1991 Several Opinions on EBL and the 1992 Several Opinions on CPL) if there was any inconsistency in the formers.

[150] The 2002 Provisions on Bankruptcy Cases, article 4, 5

[151] Chua Eu Jin, The Reform of the P.R.C. Corporate Bankruptcy Law: Slowly but Surely, 16 (8) China Law and Practice, 2002 Oct., p. 19.

focused on the placement of employees,[152] the disposal of the bankruptcy property (especially the right to the use of the land, the secured claims and the bank loans)[153] and rearrangement of the bankrupt enterprises of the state-owned enterprises.[154]

3.10 Some local governments, including provinces and cities, enacted their own local rules and regulations to meet their local needs.[155] For example, the Enterprise Bankruptcy Rules of Shenzhen Special Economic Zone (hereinafter 1993 Shenzhen Rules), which was adopted on November 10, 1993 and was only implemented within the Shenzhen special economic zone.[156]

1.1.2 Current Corporate Insolvency System of the Mainland and Its Problems[157]

1.1.2.1 Brief Introduction into Current Corporate Insolvency System

3.11 Adopted on 27 August 2006, the current bankruptcy system in China is established based on the Enterprise Bankruptcy Law (hereafter the EBL)[158], which replaced the former 1986 EBL and came into force on 1 June 2007. Evolving synchronously with economic reform in China, the EBL provides a unified bankruptcy system, covering all types of incorporated enterprises

[152] They are mainly: (A) Regulations on the Placement of Surplus Staff and Workers of State-owned Enterprises (1993, Decree No. 111); (B) Regulations on Unemployment Insurance for Staff and Workers of State-owned Enterprises (1993, Decree No. 110); (C) The Notice of Advancing the Problem-solving and the Reemployment of the Enterprise Employees (1997, Decree No. 166); (D) Supplementary Notice of the State Council on the Relevant Issues about the Pilot Implementation of the Merger and Bankruptcy of State-owned Enterprises in Some Cities and the Reemployment of Workers (1997, Decree No. 10); (E) Notice of the Central Committee of the Communist Party and the State Council on the Basic Living Guarantee and the Reemployment of the Laid-off employees of the State-owned Enterprises (1998, Decree No.10).

[153] They are mainly: (A) Rules on the Evaluation and Management of State Assets (1991); (B) Notice of Stopping, Decreasing and Slowing the Return of the Interests of the Loans for the Enterprises which are Suspended Operation for Consolidation, Merged, Dissolved and Bankrupt (1993, Decree No. 113); (C) Notice of Several Issues on the Mortgage of the Right to the Use of the Land (1997, Decree No. 2); (D) Several Opinions on Enhancing the Land Asset Management and Promoting the Reform and Development of the State-owned Enterprises (1999, Decree No. 433).

[154] They are mainly: (A) Interim Measures on Enterprise Mergers (1989, Decree No. 38); (B) Notice of the State Council on the Relevant Issues concerning the Pilot Implementation of Bankruptcy of State-owned Enterprises in Some Cities (1994, No. 59); (C) Notice of the Several Issues on the Pilot Implementation of the Merger and Bankruptcy of the State-owned Enterprises (1996, Decree No. 492)

[155] For instance, from 1993 to 2006, there were 167 local bankruptcy decrees issued by various levels of governments, most of which related to the employee rearrangement. See: www.vip.chinalawinfo.com

[156] As part of its “open door” economic policy, China marked out a number of "special economic zones." These areas each have their own local congress and, within limits, are permitted to enact their own regulatory laws.

[157] Most part of this section has been derived from my publication ‘Can the Day Understand the Night? Brief Introduction into Problems of the Current Insolvency System in China, 2015, available at http://iiiglobal.org/iii-prize-in-insolvency.html (Last visited on 14 June 2016)

[158] Official English version is available at: http://www.npc.gov.cn/englishnpc/Law/2008-01/02/content_1388019.htm (Last visited on 14 June 2016)

regardless of types of the ownership.[159] The current EBL is also a more debtor-friendly regime. In addition to the liquidation proceedings, it provides reorganization mechanisms for the purpose of giving a second chance to those economically viable but distressed businesses, by referring to the eminent models in other jurisdictions, including, Chapter 11 of the US Bankruptcy Code and German insolvency law.[160] The current EBL also introduced a new legal profession, bankruptcy administrators, into China's insolvency system, who are designated to undertake critical administrative functions and supervisory responsibilities.[161] The Supreme People's Court also issued a number of related judicial interpretations (Please refer to Annex II), as important complementary legal references to the problems in practice, which thus play a crucial role in the current insolvency system.

3.12 Nevertheless, according to the data released by the Supreme People's Court in 2014, from 2007 when the current EBL was implemented to 2012, the amount of the requests to open insolvency proceedings seized by the courts continue to decrease at an average rate of 12.23% every year.[162] In 2012, there were 735,000 domestic enterprises in total that were deregistered or cancelled with the government bureau,[163] but only 20.52% of them utilized judicial insolvency proceedings and one decade ago it was 17.09% higher.[164] With more specific and systematic arrangements under the current insolvency system, the reasons that the caseload of insolvency proceedings continues to decline on an annual basis are complicated and multifaceted.

1.1.2.2 Introduction into Current Problems of Insolvency System

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[159] After the new EBL came into effect in 2007, Chapter XIX of the Civil Procedure Law, which was amended on 28 October 2007, was deleted. The bankruptcy part was also removed from the former Chapter VIII of the Companies Law in 2005. Article 190 of 2013 Companies Law: Where a company is declared bankrupt according to law, bankruptcy liquidation shall be conducted in accordance with the enterprise bankruptcy law.
The 1986 EBL still has some influence on the current EBL. Parallel to the normal bankruptcy proceedings, the so-called administrative closure is stipulated in the EBL, which means, certain state-owned enterprises within the period and scope as are prescribed by the State Council before the EBL is put into effect shall be handled according to the relevant regulations of the State Council and therefore are excluded from the EBL (the EBL, Article 133). The State-Owned Assets Supervision and Administration Commission ("SASAC") of the State Council estimated that roughly 2,000 SOEs might take advantage of this "administrative closure". Not until the period for administrative closure expires, will the new law truly harmonize the bankruptcy treatment of all SOEs, including SOEs and non-SOE legal person enterprises. See also Lan Xinzhen, Looking Forward to the New Bankruptcy Law (in Chinese), in: Beijing Review, 21/06/2004, visit: http://www.bjreview.cn/Cn/2004-29/200429-jj2.htm (Last visited on 14 June 2016)
[160] Shi Jingxia, Twelve Years to Sharpen One Sword: The 2006 Enterprise Bankruptcy Law and China's Transition to a Market Economy, 16 Norton Journal of Bankruptcy Law and Practice, Vol. 16, No. 5, October 2007, p.666
[161] The EBL, Chapter III
[162] Ma Jian, Statistic Analysis on Insolvency Cases Accepted by People's Court from 2003-2012 (in Chinese), in: Legal Information, 2014 (03), p.23
[163] State Administration for Industry and Commerce of the P.R.C., Analysis Report on Domestic Enterprises Life Circle (in Chinese), June 2013, p.3, available at:
http://www.saic.gov.cn/zwgk/tjzl/zxtjzl/xxzx/201307/P020130731318661073618.pdf (Last visited on 14 June 2016)
[164] Ma Jian, Statistic Analysis on Insolvency Cases Accepted by People's Court from 2003-2012 (in Chinese), in: Legal Information, 2014 (03), p.24

1.1.2.2.1 The Competing System: Participation in Distribution

3.13 The EBL, just like its literal meaning, only applies to an enterprise as legal person (or a legal person enterprise).[165] Liquidation of other organizations (who are not enterprise legal person) as prescribed by other laws, when they go bankrupt, shall be governed, mutatis mutandis, by the procedure as prescribed under this Law.[166] A natural person is excluded from the scope of the EBL. However, it is noteworthy that under Companies Law (adopted in 2005), there is one-person company with limited liability.[167] Pursuant to the article 64 of the Companies Law, where the shareholder of a one-person company with limited liability cannot prove that the property of the company is independent of his own property, he assumes the joint and several liabilities for the debts of the company. Under this circumstance, if this one-person company goes bankrupt and its natural person shareholder has the joint liability for the debts of the company, what will happen if his personal property is not enough to pay off the debts? The EBL does not provide any answer, whereas there is alternative solution in practice.

3.14 In 1992, prior to the current EBL that came into effect in 2007, the Supreme People's Court issued a judicial interpretation, Opinions of the Supreme People's Court on Some Issues Concerning the Application of the Civil Procedure Law of the People's Republic of China (hereinafter the 1992 Opinions),[168] which provides a so-called participation in distribution system.[169] Under the 1992 Opinions, the judgment debtors refer to natural persons and organizations other than the enterprises, which complemented the scope of application under the 1986 EBL. The participation in distribution system can be triggered when the assets of a judgment debtor are found insufficient to satisfy the judgment in the course of enforcement. The other creditors, after filing for petition against the same judgment debtor or having obtained the relevant enforcement basis, can apply for participation in distribution of the judgment debtor's assets seized in

[165] Not all kinds of enterprises are qualified as legal person. In accordance with article 2 of Regulations of the People's Republic of China for Controlling the Registration of Enterprises as Legal Persons (effective as of July 1, 1988), any of the following enterprises which are qualified as legal persons shall register as such in accordance with the relevant provisions of the present Regulations:
(1) enterprises owned by the whole people;
(2) enterprises under collective ownership;
(3) jointly operated enterprises;
(4) Chinese-foreign equity joint ventures, Chinese-foreign contractual joint ventures and foreign-capital enterprises established within the territory of the People's Republic of China;
(5) privately operated enterprises;
(6) other enterprises required by the law to register as legal persons.
The EBL, article 2: Where a legal person enterprise cannot pay off his debts due and his assets are not enough for paying off all the debts, or he apparently lacks the ability to pay off his debts, the debts shall be liquidated according to the provisions of this Law.
[166] The EBL, article 135.
[167] A one-person company means a company with limited liability where there is only one shareholder who is a natural person or a legal person. (the Companies Law, article 58)
[168] The 1992 Opinions, No.22 [1992] of the Supreme People's Court (in Chinese)
[169] The 1992 Opinions (in Chinese), article 297-299

that enforcement proceeding.[170] In 1998, a U-turn occurred after the Supreme People's Court issued the Provisions of the Supreme People's Court on Several Issues Regarding Enforcement of the People's Courts (For Trial Implementation, hereinafter the 1998 Trial Provisions).[171] In accordance with the 1998 Trial Provisions, the participation in distribution system can also apply to those enterprises dissolved, deregistered and shut down without liquidation, whose assets are not sufficient to pay off all the debts.[172] Moreover, in 2004, Provisions of the Supreme People's Court on Multiple Creditors that Participate in Distribution (Draft for Public Consultation) was released. Till now that judicial interpretation still has not come into effect and one of the key reasons is that it is difficult to achieve a consensus on the participation in distribution system within the Supreme People's Court.[173]

3.15 Pursuant to the current EBL, only the creditors and the debtor can apply for bankruptcy. In practice, as pointed out by Wang and Xu there are creditors who decline to file a bankruptcy petition but take advantage of the participation in distribution system in order to obtain more assets than that they can receive through the insolvency proceedings.[174] This is contradictory with the core function of bankruptcy law, which is, as remarked by Jackson, "a collective debt-collection device".[175] Instead, it encourages the creditors to individually grab the assets under no obligation to "share with other creditors, who maybe slower to take action".[176] That can lead to unfair distribution among all the creditors as a whole. In addition, unlike the strict notice procedures as required under the EBL, some of the creditors cannot even know about the proceeding and then lose the opportunity to make claims. Besides, if the court seized the application for the opening of insolvency proceedings, the whole enforcement procedure can be stayed[177] and the participation in distribution can be stayed accordingly. If the debtor is declared bankruptcy, the court should terminate the enforcement procedure.[178] Nevertheless, in accordance with article 16 of the EBL, only payment to individual creditors that is done after the people's court seizes a request for bankruptcy shall be deemed as invalid. Therefore, even if the debtor or some creditors petition for opening of bankruptcy proceedings later, the assets that have been enforced through the participation in distribution system cannot be ordered to return because neither the EBL nor other legislations provide such a legal basis to revoke a legitimate action.

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[170] The 1992 Opinions (in Chinese), article 297
[171] The 1998 Trial Provisions, No.22 [1992] of the Supreme People's Court (in Chinese)
[172] The 1998 Trial Provisions (in Chinese), article 96
[173] Chen Zhixin, Dilemma and Way Out of Civil Participation in Distribution System, in: Journal of Shanghai University of Political Science and Law (The Rule of Law Forum)(in Chinese), Vol.29, No.6, Nov. 2014, p.84
[174] Wang Xinxin, Xu Yangguang, Dilemmas and Solutions to China's Bankruptcy Law: Reasons of Decrease on the Numbers of Acceptance of Bankruptcy Cases and the Relevant Treatment (in Chinese), 19 Nov. 2014, available at http://www.chinaqingsuan.com/news/detail/7702/page/2 (Last visited on 14 June 2016)
[175] Jackson, Thomas H., The Logic and Limits of Bankruptcy, Washington D.C.: Beard Books, 2001, p.8
[176] Bartell, Laura B., Visualizing Bankruptcy, U.S.: Lexis Nexis, 2011, Chapter 1 [1/2]
[177] The 1998 Trial Provisions (in Chinese), article 102(1)
[178] The 1998 Trial Provisions (in Chinese), article 105

3.16 Further, it will result in no possibility of rescue. Under the participation in distribution system, the courts do not have to take into consideration the conditions of the enterprise business but simply determine whether the debt is due. Plus, individual collection can consume the exhaustible assets of the debtors in an inefficient way, which leaves no resources to replenish the estate of the debtor. Therefore, the coexistence of the participation in distribution system is considered by most of the judges and the academics as a leeway from formal insolvency proceedings and provokes threat to the sound development of the current EBL.[179]

3.17 The problem was partly solved on 4 February 2015 when the latest judicial interpretation concerning application of Civil Procedure Law issued by the Supreme People's Court came into effect.[180] In accordance with the new judicial interpretation, the court, upon the agreement of one of the applicants for enforcement or the respondent against whom the enforcement is sought, should stay the enforcement proceeding and transfer the case to the court at the domicile of the respondent, if the respondent, as enterprise legal person, meets the conditions set up under Article 2(1) of the EBL.[181] If the court at the domicile of the respondent accepts the insolvency case, the preservation measures on the property should be lifted. If the court at the domicile of the respondent orders the respondent bankrupt, the enforcement proceeding shall be terminated.[182] The new judicial interpretation establishes a link between the enforcement procedure and initiation of insolvency proceedings so that the access to the corporate debtors' assets through the participation in distribution system is blocked.

3.18 Nevertheless, it is noteworthy that Article 2 of the EBL is composed of two provisions. Article 2(1) stipulates the conditions concerning liquidation of debtor [183] and Article 2(2) provides the conditions of reorganization. [184] Compared to Article 2(1), Article 2(2) includes a less restrict trigger condition

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[179] Liu Guixiang, Distribution of Functions of Participation in Distribution System and Insolvency System, in: People's Court Daily, 30 April 2014, at 8; Wang Guanghua, Participation in Distribution System and Insolvency System are Different in Nature (in Chinese), in: People's Court Daily, 30 April 2014, at 8; Chen Zhixin, Dilemma and Way Out of Civil Participation in Distribution System, in: Journal of Shanghai University of Political Science and Law (The Rule of Law Forum)(in Chinese), Vol.29, No.6, Nov. 2014, p.82-87; Wang Xinxin, Participation in Distribution System Should Not Conflict with Insolvency System, in: People's Court Daily, 30 April 2014, at 8; Xu Haoshang, Ou Yuanjie, Separation of Functions of Participation in Distribution System and Insolvency System: Restructuring the Participation in Distribution System (in Chinese), in: People's Judicature, 2014 (17), p.102-107

[180] Judicial Interpretation of the Supreme People's Court concerning Application of Civil Procedure Law, [2015] Judicial Interpretation No.5 (in Chinese)

[181] [2015] Judicial Interpretation No.5 (in Chinese), article 513

[182] [2015] Judicial Interpretation No.5 (in Chinese), article 514

[183] The EBL, article 2, para.1: Where an enterprise legal person fails to pay its debt as due, and if its assets are not enough to pay off all the debts or if it is obviously incapable of clearing off its debts, its liabilities shall be liquidated according to this Law.

[184] The EBL, article 2, para.2: Where an enterprise legal person is under the circumstance mentioned in the provision of the preceding paragraph or if it is obviously likely that it is unable to pay off its debts, it may be subject to reorganization according to this Law.

based on likelihood of insolvency. Accordingly under the new judicial interpretation, enterprise debtors are ruled out of the participation in distribution system if they are considered subject to liquidation. Nevertheless, it seems that the new judicial interpretation has not completely excluded enterprise debtors, which reach the lower threshold of reorganization pursuant to Article 2(2), from the participation in distribution system.

1.1.2.2.2 Involvement of the Government

3.19 Discussions about involvement of Chinese government in handling insolvency cases often begin and end with a series of complaints about external interference. From the domestic perspectives, according to Li and Wang, involvement of the government, in particular the local government, in the insolvency proceedings, is regarded as "the most important factor influencing court's function in hearing bankruptcy cases"[185] in the Mainland. Besides, As stated in Jiang's research, which was conducted based on statutory analysis and case studies, it is pointed out that involvement of government agencies in China's bankruptcy proceedings, especially the reorganization proceedings, is excessive, which contributed to a discouraging factor for bankruptcy filings.[186] From the international perspectives, the same concern arose. Early in 2007, it is acknowledged in an investigation report published by the United States International Trade Commission that the policy-led bankruptcy proceedings under the 1986 EBL was considered as "another instrument that China's government has used to satisfy its rationalization objectives",[187] which deviated from the market-oriented function of the bankruptcy laws. In fact, a clear definition of bankruptcy laws is also one of five fundamental criteria,[188] based on which China has been seeking market economy status (MES) recognized by the EU but has been consistently rejected.[189] According to the EU, China has only met one of them, which excluded the bankruptcy laws criteria.[190] It seems that the international confidence in a well-developed bankruptcy system under market

[185] Li Shuguang, Wang Zuofa, The Function of China's Court in Enterprise Bankruptcy and the Future Trend – Observations from the Background of the Four Year Implementation of China's Existing Bankruptcy Law, in: INSOL World, the Quarterly Journal of INSOL International, Fourth Quarter, 2012, p.11

[186] Jiang Yujia, The Curious Case of Inactive Bankruptcy Practice in China: A Comparative Study of U.S. and Chinese Bankruptcy Law, in: Northwestern Journal of International Law & Business, Vol.34, Issue 3, 2014, p.569 – 570

[187] United States International Trade Commission, China: Description of Selected Government Practices and Policies Affecting Decision-Making in the Economy, Investigation No. 332-492, USITC Publication 3978, December 2007, p.30

[188] To be considered a 'market economy', a country must have a floating exchange rate, a free market, a non-intrusive government, effective business accounting standards and, lastly, a clear definition of property rights and bankruptcy laws. In Policy Department of European Parliament, Trade and Economic Relations with China 2015, June 2015, p. 24

[189] European Parliament, China and Granting of Market Economy Status thereto, 20 April 2015, http://www.europarl.europa.eu/sides/getDoc.do?type=WQ&reference=E-2015-006250&language=EN (Last visited on 14 June 2016)

[190] Policy Department of European Parliament, Trade and Economic Relations with China 2015, June 2015, p. 24, http://www.europarl.europa.eu/RegData/etudes/IDAN/2015/549062/EXPO_IDA(2015)549062_EN.pdf (Last visited on 14 June 2016)

economy conditions in China still requires time to be built up. Before that, the fear of foreign creditors to recover their investment and claims in the event of bankruptcy due to government interference can probably result in escape from the Mainland jurisdiction. I will discuss about that point later in section 1.3.

3.20 Government involvement indeed exists in the course of China's insolvency proceedings. Nevertheless, in my view, those complaints also fail to capture the complex reality of China. Some of them do not merely have negative effects but a compromising choice in a transitional economy. In this section, I'd like to explore the forms and the reasons of the government involvement based on the relevant case law.

3.21 In China, involvement of the government in the insolvency proceedings can exist in various forms. The most evident one is the liquidating committee. Under the current EBL, in addition to law firms, certified public accountant firms, bankruptcy liquidation firms or any other social intermediary agencies, the administrator can also be a liquidating committee,[191] which is an inheritance from the 1986 EBL.[192] In accordance with the judicial interpretation, the members of a liquidating committee can be appointed from the related government departments, from the social intermediary agencies included in the roster of administrators, from financial asset management companies as well as from the people's bank and the financial regulatory institution under relevant laws and administrative regulations.[193] For instance, in the Tianyi (San-an) case, it involved reorganization proceeding of a listed company, 45.43% of whose equity structure is state-owned shares.[194] The liquidating committee was appointed, which was composed of the local State Assets Supervision and Administration Committee (SASAC), the local Labor and Social Security Bureau, the local central branch of the People's Bank of China, the local branch of China Banking Supervision and Administration Committee (CBSAC), in addition to an accounting firm and a law firm.[195]

3.22 The same happened to the Huayuan case, which was a listed company directly subordinated to State-owned Assets Supervision and Administration Commission of the State Council (SASAC).[196] The court designated a liquidating committee that was mainly composed of CBSAC Shanghai Bureau, China

[191] The EBL, article 24
[192] The 1986 EBL, article 24
[193] Provisions of the Supreme People's Court on Designating the Administrator during the Trial of Enterprise Bankruptcy Cases (Interpretation No.8 [2007], issued on 12 April 2007, hereinafter Provisions of Designating the Administrator), article 19
[194] Draft Report on Connected Transaction Concerning Tianyi's Acquisition of Assets through Issuing Stocks, 2008, available at: http://business.sohu.com/20080119/n254757501.shtml (Last visited on 14 June 2016); [2007] Hubei Jinzhou Intermediate People's Court Civil Bankruptcy No.14-5 (in Chinese)
[195] Li Shuguang & Wang Zuofa, Review of the P.R.C. Bankruptcy Law in 2009, INSOL International Technical Series Issue No.11, March 2010, p.5.
[196] Gao Changjiu, Tang Zhengyu, Fu Wang, Legal Dilemmas Encountered in the Course of Listed Corporation Reorganization: Taking ST Huayuan as Example (in Chinese), Nomocracy Forum, 2010, p.45. Please note the authors are judges who participated in the reorganization proceedings of the Huayuan case.

Securities Supervision and Administration Committee Shanghai Bureau, Shanghai Financial Office, SASAC Shanghai Branch.[197] The judges, who participated in the Huayuan case, briefly explained the reason of that assignation. Reorganization of the listed company involved a series of complicated problems and had to coordinate with different government departments. For example, considering the state-owned shares in the debtor's capital structure, the reorganization should be subject to supervision of State Assets Supervision and Administration Committee. Meanwhile, the debtor was also a listed company, which should be regulated by China Securities Regulating Commission. The main creditors of the debtor were banks and thus needed the assistance from the People's Bank of China and China Banking Supervision and Administration Committee. However, the coordinating ability of the social intermediary agencies is relatively weak at this moment. That's why the judges understood that appointment of a liquidating committee might cause controversy but still found it necessary to include the related government departments into the liquidating committee in order to facilitate the reorganization proceedings, which was "in line with China's current national conditions".[198]

3.23 The government may also be requested to participate in the insolvency proceedings, which mostly relates to policy issues. Based on the case law, in particular, in the reorganization cases, the courts sought assistance from the government in matters of tax as well as all kinds of administrative approvals, such as concerning real estate, foreign merger and acquisition as well as employee replacement. Under the current EBL, tax is the second on the rank of the order of paying off debts in the liquidation proceedings.[199] With respect to how to tackle tax issues in the course of reorganization, the current EBL does not provide specific rules but the tax authority itself issued the Measures for the Enterprise Income Tax of Enterprise Reorganizations.[200] In the case of Jiande Xuehong Home Textiles Co., Ltd., the debtor was reorganized by introducing an external investor. If the debtor was charged tax according to Measures for the Enterprise Income Tax of Enterprise Reorganizations, it would put more financial burdens upon the debtor's shoulder. In that case, the problem can be solved if the reorganization with the help of an external investor can be shifted into the category of investment promotion and capital attraction, which should be subject to preferential tax policy and consequently lowered the costs. The court negotiated with the government for several times and finally persuaded the government to accept the arrangement.[201] In the reorganization case of Zhoushan Huatai Petrol Company, a Hong Kong company was accepted as one of the strategic investor, who agreed to purchase the shares of the debtor.

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[197] Zhang Haizheng, Kuang Jingting, Corporate Reorganization Case Analysis under China's New Bankruptcy Law, in: International Corporate Rescue, Vol.11, issue3, 2014, p.177

[198] Gao Changjiu, Tang Zhengyu, Fu Wang, Legal Dilemmas Encountered in the Course of Listed Corporation Reorganization: Taking ST Huayuan as Example (in Chinese), Nomocracy Forum, 2010, p.46

[199] The EBL, article 113

[200] [2010] Announcement of the State Administration of Taxation No. 4 (in Chinese)

[201] 2013 Top Ten Typical Enterprise-related Cases in Zhejiang Province, 13 January, 2014, available at: http://www.zjcourt.cn/content/20140113000001/20140113000008.html (Last visited on 14 June 2016)

However, investment from Hong Kong was regarded as foreign investment in the Mainland, which should go through time-consuming administrative procedures for approval. For the purpose of promoting the efficiency of reorganization, the court persuaded the government to complete the administrative procedure as soon as possible.[202]

3.24 In the case of Tang Ying Garment Co. Ltd., the government made an undertaking upon the request of the court, which was incorporated into the reorganization plan. The main capital of the debtor was its real estates, including the land and buildings. However, the government did not issue related ownership certificates to those real estates, which entailed the ownership of the debtor of those real estate was in question and the interests of the creditor would accordingly be affected. The court held discussion with the government for several times and the government finally agreed to issue related certificates as soon as possible and change the land status used for commercial purpose so as to raise the value of the land. Further, the reorganization plan included a written promise that the government would purchase the real estates if it failed to issue related certificates within two years, which enabled the reorganization plan to achieve a high pass rate.[203]

3.25 Sometimes the involvement of the government in the insolvency proceedings directly links to financial support or employee replacement. LDK, registered in Jiangxi Province, was a private company that manufactured photovoltaic (PV) products. According to the information published on the company's website, it was the first company of that province in China listed on the New York Stock Exchange and used to be a significant revenue contributor to that province.[204] Due to the excess capacity and anti-dumping and anti-subsidy investigation on China's photovoltaic products[205] imported into the U.S.A. and EU, the solar power industry in China plunged since 2011[206] and an array of photovoltaic enterprises went insolvent in China. The business of LDK also deteriorated in 2011. The salary of the employees had to temporarily be paid by the local government.[207] In 2012, a budget bill was passed, which allowed the local government to pay for part of the debts of the private company with fiscal funds. The government had to delete the content of the bill from its official website in order to ease the media uproar incurred.[208] By the end of 2014, LDK

[202] [2010] Zhoushan People's Court Ordinary Commercial Bankruptcy No.1 (in Chinese)
[203] [2011] Ningbo Fenghua People's Court Commercial Bankruptcy No.1 (in Chinese)
[204] The English website of Saiwei: http://www.ldksolar.com/com_about.php (Last visited on 14 June 2016)
[205] Photovoltaic products generate electricity by converting solar energy through semi-conducting materials that exhibit the photovoltaic effect.
[206] Wei Zheng, Yu Bingqing, Study of the Current Photovoltaic Development in China and Its Solutions (in Chinese), in: Sino-Global Energy, Vol.18, Issue.6, 2013, p.15-16
[207] Guo Fang, Jian Wenchao, Saiwei and the "Kidnapped" Government (in Chinese), in: China Economic Weekly, Issue 30, 2012, p.25
[208] Guo Ruyi, Xinyu Government Deleted from Its Website the Bill to Pay Saiwei's Debt with Fiscal Funds (in Chinese), 19 July, 2012, available at: http://business.sohu.com/20120719/n348571532.shtml (Last visited on 14 June 2016)

has not filed the petition for bankruptcy in the Mainland China, whereas its holding company applied for winding up in Cayman Islands in February 2014.[209]

3.26 LDK is an extreme case. On 26 June 2014, Shanghai No.1 Intermediate People's Court accepted the petition for reorganization concerning Shanghai Chaori Solar Energy Science & Technology Co. Ltd. (Chaori).[210] Chaori was a private company based in Shanghai, which also manufactured photovoltaic (PV) products and experienced financial distress. It is stated in the Chaori's draft reorganization plan that the court designated a law firm and an accounting firm as the administrators and the government participated in the proceedings in order to cooperate with the court in matters of employee replacement.[211] Another case concerning a company producing solar glass, it involved a reorganization proceeding in Zhejiang Province, which was filed in 2013. Considering the practical necessity arising from the reorganization case, the court sent a letter of request to the local government in order to discuss about employee replacement and the replacement fees prepaid by the government, in which the court also suggested that the local government participate in the liquidating committee. The local government, however, refused to take the responsibility of prepaying the replacement fees and considered that it was more appropriate for qualified intermediary agencies to be appointed as administrator. As a result, the court dismissed the application for reorganization because the court considered that the feasibility of reorganization was not very high.[212]

3.27 The reason behind that kind of government involvement is partly due to the lack of public fund related to wage guarantee. As mentioned by Wang and Yang, there are some local specialized funds for protection of labor claims established for limited purpose only available in Beijing and Shanghai.[213] At national level, such a system that provides comprehensive financial support for labor claims incurred by insolvency of enterprises has not been set up. Consequently in 2009, Opinions of the Supreme People's Court on Several Issues Concerning Correctly Trying Enterprise Bankruptcy Cases to Provide Judicial Protection for Maintaining the Order of Market Economy were published.[214] Problems, such as unpaid salaries and replacement of employee, are considered sensitive in nature and the courts are required to seek support from the local government.[215] It is

[209] LDK Investor Press Releases, LDK Solar Welcomes Appointment of Joint Provisional Liquidators in Cayman Islands, available at: http://investor.ldksolar.com/phoenix.zhtml?c=196973&p=irol-newsArticle&ID=1905143 (Last visited on 14 June 2016)
[210] [2014] Shanghai No.1 Intermediate People's Court Civil IV (Commercial) Bankruptcy No.1-1 (in Chinese)
[211] [2014] Shanghai No.1 Intermediate People's Court Civil IV (Commercial) Bankruptcy No.1-4 (in Chinese)
[212] [2013] Zhejiang Huzhou Intermediate People's Court Bankruptcy Preliminary No.1 (in Chinese)
[213] Wang Xinxin, Yang Tao, Study on Protection of Labor Claims of Insolvent Enterprises: Tolerance and Share of Costs during Social Reform (in Chinese), in: Research on Rule of Law, 2013 (01), p.29
[214] [2009] Judicial Interpretation No.36 (in Chinese)
[215] [2009] Judicial Interpretation No.36 (in Chinese), article 5

further stated "if conditions permit, the government can set up stability funds or encourage the third parties to make advance payments to settle the employees of insolvent enterprises at the first place. The advance payments made by the government or any third party can be firstly repaid in the bankruptcy procedure according to the repayment sequence of employees' claims."[216]

3.28 China's insolvency proceedings involve frequent interplay between the courts and the governments. Compared to the judiciary, the government has been given very extensive powers in administering affairs. Against that background, judicial independence alone is not sufficient to safeguard the sound and efficient operation of the insolvency proceedings (for instance, problems like taxes, employee resettlement, policy-based loans cannot be settled without the proper support of the governments[217]) and the courts have to seek cooperation from the government. Upon emerging consensus, there are "minimal judicial independence, impartiality and integrity that countries of various political stripes should adhere to".[218] Nonetheless, an individual country, which is still in the course of judicial reform, should not simply be condemned before it meets the requirement because it is a long-term and complicated domestic process "involving different balance of struggle among competing interest groups".[219] In addition, both the courts and the governments in China share the same objective of cooperation. As pointed by Zhou Xiaochuan, Governor of People's Bank of China (Central Bank of P.R.C.), "in the process of reform, China attaches special importance to social stability".[220] For example, maintaining social stability is a principle that has been incorporated into related judicial interpretations.[221] In the case of Wuxi Mingte Chemical Fiber Co., Ltd., which involved reorganization concerning a non-public company, the judge held the similar opinion as the judge in the Huayuan case, considering that involvement of government by participating in the liquidating committee has played an irreplaceable role in the reorganization case because the government can cooperate with the court in resolving the social conflicts and ensuring social stability. [222]

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[216] [2009] Judicial Interpretation No.36 (in Chinese), article 5

[217] Pan Junfeng, Study of Judicial Reorganization Practice: from the perspective of reorganization cases handled by the courts in Jiangsu Province (in Chinese), in: Wang Baoshu(ed.), Chinese Yearbook of Commercial Law, Law Press, 2011, p.209

[218] For better understanding of "minimal judicial independence, impartiality and integrity", there are some examples, such as the UN Basic Principles on the Independence of the Judiciary (endorsed by General Assembly resolutions 40/32 of 29 November 1985 and 40/146 of 13 December 1985); IBA Minimum Standards of Judicial Independence (adopted by the International Bar Association in 1982). See also Henderson, Keith E., Halfway Home and a Long Way to Go: China's Rule of Law Evolution and the Global Road to Judicial Independence, Judicial Impartiality, and Judicial Integrity, in: Randall Peerenboom (ed.), Judicial Independence in China: Lessons for Global Rule of Law Promotion, New York: Cambridge University Press, 2010, p.24

[219] Peerenboom, Randall, Judicial Independence in China: Common Myths and Unfounded Assumptions, in: Randall Peerenboom (ed.), Judicial Independence in China: Lessons for Global Rule of Law Promotion, New York: Cambridge University Press, 2010, p.88

[220] Zhou Xiaochuan, Debate on Rescue in the Midst of Financial Crisis (in Chinese), in: Journal of Financial Research, no.9, 2012, p.5

[221] [2009] Judicial Interpretation No.36 (in Chinese); [2012] Judicial Interpretation No. 261 (in Chinese)

[222] [2010] Jiangsu Wuxi Intermediate People's Court Bankruptcy No.6 (in Chinese)

3.29 Further, there are economic incentives for the governments to get involved in the insolvency proceedings. As pointed out by Zhou, the criteria of promotion of local officials have shifted from political achievements to economic contributions since 1980s.[223] Hence, the local government is highly motivated to boost growth of local economy. In 1962, an economist, Arthur Melvin Okun, published his paper based on empirical observation, in which it is stated that for every 1% increase in unemployment, a country's gross domestic product (GDP) will decrease by 2% to 4% from its potential.[224] His theory was later referred to as Okun's law. As pointed out by Knotek, Okun's law can be affected by a number of factors and consequently it might not be very precise but more useful as a forecasting tool to show the tendency.[225] In 2014, IMF conducted empirical research based on the data of a group of advanced economies—the G7 economies plus Australia and New Zealand from 1989 to 2012 and confirmed that consistent with Okun's Law, forecasts of real GDP growth and the change in unemployment are negatively correlated.[226] Bankruptcy and unemployment are directly connected, which thus may have direct influence on the political promotion of local officials.

3.30 Nonetheless, the fact that insolvency system only reminds the local governments of unemployment or bad performance on developing local economy is according to Wang and Xu, nothing but misunderstanding of the function of insolvency system.[227] The genuine purpose of establishing an insolvency system is to allow hopeless enterprise to exit the market in a prompt and efficient way and help to rescue economically viable but distressed businesses. It must be acknowledged that currently in the Mainland the advantages of the governments in facilitating the insolvency proceedings are quite evident. Nevertheless, in the context of market-oriented economy, interference of the government in dealing with insolvency cases is also expected at a proportionate degree.

1.1.2.2.3 Cautious Attitudes of the Courts towards Insolvency Cases

3.31 The cautious attitudes of the courts towards insolvency cases are mainly reflected in reluctance to accept application for insolvency proceedings. The first reason is that it is lack of specific rules for the courts to refer to. In practice, in

[223] Zhou Lian, The Incentive and Cooperation of Government Officials in the Political Tournaments: An Interpretation of the Prolonged Local Protectionism and Duplicative Investments in China (in Chinese), in: Economic Research Journal, 2004(06), p.34

[224] Okun, Arthur M., Potential GNP: Its Measurement and Significance, in: American Statistical Association, Proceedings of the Business and Economics Statistics Section, 1962, p. 98–104.

[225] Knotek, Edward S., II, How Useful is Okun's Law?, 2007, p.73-103, available at: http://www.kc.frb.org/publicat/econrev/pdf/4q07knotek.pdf (Last visited on 14 June 2016)

[226] Ball, Laurence, Jalles, João Tovar and Loungani, Prakash, Do Forecasters Believe in Okun's Law? An Assessment of Unemployment and Output Forecasts (IMF Working Paper), February 2014, available at: https://www.imf.org/external/pubs/ft/wp/2014/wp1424.pdf (Last visited on 14 June 2016)

[227] Wang Xinxin, Xu Yangguang, Dilemmas and Solutions to China's Bankruptcy Law: Reasons of Decrease on the Numbers of Acceptance of Bankruptcy Cases and the Relevant Treatment (in Chinese), 19 Nov. 2014, available at http://www.chinaqingsuan.com/news/detail/7702/page/2 (Last visited on 14 June 2016)

particular in the reorganization proceedings, the courts usually conduct a prior review before determining whether or not to open the proceeding. The first reorganization case of listed company, the case of the Zhejiang Hai Na reorganization, after the current EBL came into effect, was such an example.[228] Despite the statutory threshold of rescue stipulated under the EBL,[229] the High Court of Zhejiang Province sent a notice to the lower court, i.e. the Intermediate Court of Hangzhou, to which the reorganization petition was filed, to conduct an evaluation prior to acceptance. The main concern of the High Court of Zhejiang Province related to the feasibility of the draft reorganization plan, the employee arrangement as well as the government opinions etc.,[230] which were all included into the contents of review of the lower court before the reorganization proceedings was decided to be commenced. In the case of Yiyang Tianye Real Estate Development Company (hereinafter the Tianye company), the shareholders of the Tianye company applied for reorganization but their application was dismissed by the court of the first instance, holding that the company was not qualified for entering into reorganization proceeding upon review.[231] The shareholders then appealed to the intermediate court. The intermediate court held a hearing and invited the members of the creditor committee, the representative of the creditors, the administrator and the government authorities in charge of real estate management to give their opinions on the reorganization application. The applicants contended that the court should only conduct formal review instead of substantial review on the reorganization application. The intermediate court held that examination on the reorganization application should include both formal review and substantial review. The substantial review mainly checked with the possibility whether or not the debtor could still be rescued, including the feasibility of the reorganization plan and the capability of the participants to realize the reorganization plan.[232]

3.32 Application for reorganization of listed companies is subject to more pre-conditions. In 2012, the Supreme People's Court issued a notice concerning instructions on reorganization of listed companies.[233] When an applicant file a petition for reorganization of a listed company, in addition to the required documents set forth in Article 8 of the EBL, the applicant shall submit the report concerning the reorganization feasibility of the listed company, the briefing materials sent by the provincial people's government at the place of the listed company's domicile to the securities regulatory authority, the opinions of the securities regulatory authority, the stability maintenance plans issued by the people's government at the place of the listed company's domicile. Where a listed company applies for reorganization on its own, it also shall submit a

[228] [2007] Hangzhou Civil II First Instance No. 184 (in Chinese)
[229] The EBL, article 70, 95
The EBL, article 96: where upon examination, the people's court deems that the application for compromise conforms to the provisions of this Law, it shall rule on a compromise, announce it and hold a creditors' meeting at which to discuss the draft of a compromise agreement.
[230] Yang Zhengyu, Application of Reorganization to the Listed Companies (in Chinese), in: Guide on Civil and Commercial Trial, People's Court Press, 2008, p.209
[231] [2012] Yiyang Heshan Civil Bankruptcy Civil Verdict No.3-2 (in Chinese)
[232] [2013] Yiyang Civil II Final No.168 (in Chinese)
[233] [2012] Judicial Interpretation No. 261 (in Chinese)

feasible employee resettlement plan.[234] The courts should hold a hearing before the courts decide to accept the application if the listed companies raise objections against the creditors' application or any creditor, the listed company and any contributor respectively present a liquidation petition and a reorganization petition. Considering the possible influence on social stability, the people's courts shall submit relevant materials level by level to the Supreme People's Court for examination before rendering a ruling to accept the reorganization applications of listed companies.[235]

3.33 The second reason is although they have been granted substantial and procedural power in accordance with the EBL,[236] the actual function of the courts in practice has been limited by external factors, such as the competing system of participation in distribution system and the government interference. The Supreme People's Court has taken measures and tried to resolve this problem. In 2011, a judicial interpretation has been issued,[237] which focuses on specifying the conditions of the courts to accept the application of insolvency cases so as to facilitate the courts to accept the insolvency petitions in a timely manner. It stipulated supervision of the higher courts on the courts at the lower level.[238] Suppose that a lower court did not even respond to the bankruptcy petition, it is stipulated that the applicant can present the petition to a higher court and the higher court shall order the court at the lower level to examine the application according to law and timely render a ruling on whether to accept the application. If the court at the lower level still does not render the ruling on whether to accept the application, the higher court may directly render a ruling to accept it and at the same time designates the court at the lower level to adjudicate this case.[239]

3.34 In addition, the courts' reluctance to accept the bankruptcy application may also be attributed to the evaluation system of judges, which is quantity-based and dependent on how many cases the judges deal with. Due to its complexity, insolvency cases are usually very time-consuming. Hence, it is understandable that judges usually try to evade them and can spend more time in handling more ordinary civil and commercial cases, which can contribute to better evaluation results.[240] The further consequence is that the Mainland lacks in professional

[234] [2012] Judicial Interpretation No. 261 (in Chinese), article 3
[235] [2012] Judicial Interpretation No. 261 (in Chinese), article 4.
[236] Li Shuguang, Wang Zuofa, The Function of China's Court in Enterprise Bankruptcy and the Future Trend – Observations from the Background of the Four Year Implementation of China's Existing Bankruptcy Law, in: INSOL World, the Quarterly Journal of INSOL International, Fourth Quarter, 2012, p.8-10
[237] Provisions (I), [2011] Judicial Interpretation No. 22 (in Chinese)
[238] Song Xiaoming, Zhang Yongjian, Liu Ming (All of the authors are judges of the Supreme People's Court), Understanding and Application of Several Issues concerning the Application of the Enterprise Bankruptcy Law of the People's Republic of China (in Chinese), in: People's Judicature, 2011(21), p.028; See also Wang Xinxin, Transforming Ideas and Improving Legislation, Accepting the Bankruptcy Cases According to Law II: to understand the judicial interpretation of the EBL in depth (in Chinese), in: People's Court Daily, 15 February, 2012, p.07
[239] Provisions (I), [2011] Judicial Interpretation No. 22, article 9
[240] Li Shuguang, Wang Zuofa, The Function of China's Court in Enterprise Bankruptcy and the Future Trend – Observations from the Background of the Four Year Implementation of China's

judges in adjudicating insolvency cases. Fully aware of the problem, it has been advocated by the Supreme People's Court to promote professionalism of judges, who are to be trained with relevant professional knowledge and specialized at handling bankruptcy cases.[241] Moreover, as remarked by Eisenberg in 1987, "Bankruptcy courts would not have arisen unless specialized knowledge was believed desirable."[242] It has been suggested by the Supreme People's Court to establish special tribunals for bankruptcy cases or appoint special collegial panels to adjudicate bankruptcy cases and the judges, who are in charge of bankruptcy cases, shall be evaluated based on different criteria.[243] In practice, instead of establishing special tribunals, jurisdiction over bankruptcy cases are centralizedly allocated to certain courts in some provinces, for instance Shenzhen Intermediate People's Court (since 2011)[244] and Foshan Intermediate People's Court (since 2013) [245] in Guangdong Province, Chongqing 5th Intermediate People's Court (since 2015) [246] in Chongqing Municipality. Nevertheless, the actual effects of those special tribunals still need to be examined after a period of implementation.

1.2 Current Cross-border Insolvency Law in the Mainland

3.35 There is no national-wise legislation concerning cross-border insolvency in the Mainland before the current EBL came into effect in 2007. Under the current EBL there are no rules governing international jurisdiction or choice of law. It only provides one single article (article 5) concerning criteria of recognition related to cross-border insolvency proceedings.[247]

3.36 First of all, the article 5(1) clearly indicates the effects of cross-border insolvency proceedings. A bankruptcy proceeding opened by the Mainland court shall have extra-territorial effect on debtors' assets situated outside the territories of the P.R.C.; whereas a legally effective bankruptcy judgment or ruling rendered by a foreign court, involving a debtor's property within the territory of the P.R.C. shall make an application for recognition and enforcement to the people's court. Therefore, China's insolvency proceedings are vested with outbound universal effect and inbound territorial effect. In addition, The EBL

Existing Bankruptcy Law, in: INSOL World, the Quarterly Journal of INSOL International, Fourth Quarter, 2012, p.13

[241] [2011] Judicial Interpretation No. 281, article 2

[242] Eisenberg, Theodore, Bankruptcy in the Administrative State, in: Law and Contemporary Problems, Vol.50, No.2, 1987, p.5

[243][2011] Judicial Interpretation No. 281, article 2, 3

[244] Please visit: http://www.szcourt.gov.cn/sfgg/spzx/2014/11/27163705826.html (Last visited on 14 June 2016)

[245]Please visit: http://www.fszjfy.gov.cn/pub/court_7/gongzuodongtai/fayuanyaowen/meitijujiao/201304/t20130424_6938.htm (Last visited on 14 June 2016)

[246] Please visit: http://www.chinacourt.org/article/detail/2015/05/id/1638458.shtml (Last visited on 14 June 2016)

[247] Official English version is available at: http://www.npc.gov.cn/englishnpc/Law/2008-01/02/content_1388019.htm (Last visited on 14 June 2016)

provides no special rules concerning ancillary proceedings to foreign insolvency proceedings involving assets in the Mainland.[248]

3.37 Secondly, the article 5(2) sets out the recognition criteria on foreign insolvency proceedings. To recognize and enforce an insolvency proceeding opened outside Mainland China, the following conditions shall be met:

(1) relevant international treaties between the country concerned and Mainland China have been concluded; or
(2) reciprocal relations between the country concerned and Mainland China have been established
(3) the insolvency proceeding shall not violate the basic principles of the laws of the People's Republic of China;
(4) the insolvency proceeding shall not jeopardize the sovereignty and security of the State or public interests;
(5) the insolvency proceeding shall not undermine the legitimate rights and interests of the creditors within Mainland China.

3.38 I will discuss about the recognition criteria set by article 5(2) item by item in the subsequent sections.

1.2.1 International Treaties[249]

3.39 From 1987 till now, China has signed over 30 mutual civil and commercial judicial assistance treaties or agreements.[250] The scope of those treaties covers generally all kinds of civil and commercial cases but some of them exclude recognition of insolvency proceedings, for instance Peru, Tunisia and Spain. In addition, some of them only apply to recognition of arbitral awards, such as Korea, Singapore and Belgium. Those treaties, if applicable, serve as concrete foundation for the court to recognize foreign insolvency proceedings. In fact, before the 2007 EBL came into effect, there were already two cases that sought recognition of the insolvency proceedings based on the bilateral treaty. The first case involved an application from Italy, which is B&T Ceramic Group s.r.l. versus E.N.Group s.p.a..[251] The E.N.Group s.p.a. was declared bankrupt by the Milan Court on October 24, 1997. On September 30, 1999, the Milan Court made

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[248] Wang Weiguo, National Report for the People's Republic of China, in: Faber, Dennis, Vermunt, Niels, Kilborn, Jason, Richter Tomáš (ed.), Commencement of Insolvency Proceedings, Oxford University Press, 2012, 6.7.2

[249] Part of this section has been derived from my publication: Gong Xinyi, To Recognize or Not to Recognize? - Comparative Study of Lehman Brothers Cases in the Mainland China and Taiwan, in: International Corporate Rescue, Chase Cambria, Vol 10, Issue 4, 2013, p. 240 – 247

[250] These countries which signed the civil and commercial judicial assistance treaties with China are (in chronological order) France, Poland, Belgium, Mongolia, Romania, Italy, Spain, Russia, Turkey, Ukraine, Cuba, Belarus, Kazakhstan, Bulgaria, Thailand, Egypt, Greece, Cyprus, Hungary, Morocco, Kirghizstan, Tajikistan, Singapore, Uzbekistan, Viet Nam, Laos, Tunisia, Lithuania, Argentina, Republic of Korea, Democratic People's Republic of Korea, United Arab Emirates, Kuwait, Peru, Brazil, Algeria. Information collected from the database Chinalawinfo (website: http://www.pkulaw.cn.ezproxy.leidenuniv.nl:2048). (Last visited on 14 June 2016)

[251] Yao Hongping, Liu Ziping, Analysis of the Application of the B&T Ceramic Group s.r.l. for Recognition and Enforcement of the Italian Court Judgment (in Chinese), http://www.civillaw.com.cn/article/default.asp?id=13604 (Last visited on 14 June 2016)

decision that all of the property of the E.N.Group s.p.a., including the property overseas, shall be sold to the B&T Ceramic Group s.r.l. as a whole. In order to take over debtor's assets located in China, on December 18, 2000, B&T Ceramic Group applied to the Guandong Foshan Intermediate People's Court for recognition of the bankruptcy judgments made by the Italian Court and restored the legal status of the applicant as the shareholder in Nassetti Ettore company and the shares of Nassetti Ettore company. The Foshan Court formally and explicitly recognized the validity of the bankruptcy judgment rendered by the Italian Court based on Sino-Italy Mutual Civil Judicial Assistance Treaty.[252]

3.40 The second application was filed by a French liquidator, Montier Antoine, on 1 April 2005 to Guangzhou Intermediate People's Court for recognition of insolvency of Pellis Corium (a French company) ordered by the French court in 1998. The Guangzhou Intermediate People's Court in accordance with article 268 of the CPL[253] and the bilateral treaty recognized the effect of the bankruptcy proceeding.[254] Sometimes recognition and enforcement rules can be found in other forms of state-to-state agreement[255] but recognition cannot be guaranteed unless there is a specific arrangement. For instance, Australia has signed the Mutual Promotion and Protection of the Investment Agreement with the Chinese government in 1988, in which it is stated that the Contracting Party should make relevant recognition and enforcement rules in dealing with the investment related civil disputes,[256] which have not been done yet.

3.41 In 2006 the High People's Court of Guangdong Province requested the reply of the Supreme People's Court to clarify whether or not recognition can be granted to a judgment rendered by an Australian court. This case involved a debt

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[252] The Chinese proceeding involved a third party, a Hong Kong company. On May 2, 1999, E.N.Group s.p.a. agreed to sell the share it held of the Nassetti Ettore company which was located in China to a Hong Kong company. On July 21, 1999, the agreement was approved by the local government and then the Hong Kong company, replacing E.N.Group s.p.a., became the shareholder of Nassetti Ettore. B&T Ceramic Group argued that E.N.Group s.p.a. had no rights to do that. Therefore, the court dismissed the enforcement request because the court held that the third party (the Hong Kong company) involved, which should be solved in another lawsuit.

[253] Article 268 of the CPL (1991): In the case of an application or request for recognition and enforcement of a legally effective judgment or written order of a foreign court, the people's court shall, after examining it in accordance with the international treaties concluded or acceded to by the People's Republic of China or with the principle of reciprocity and arriving at the conclusion that it does not contradict the basic principles of the law of the People's Republic of China nor violates State sovereignty, security and social and public interest of the country, recognize the validity of the judgment or written order, and, if required, issue a writ of execution to enforce it in accordance with the relevant provisions of this Law; if the application or request contradicts the basic principles of the law of the People's Republic of China or violates State sovereignty, security and social and public interest of the country, the people's court shall not recognize and enforce it.

[254] Wang Meiying, Lian Changren, The Recognition and Enforcement of the Foreign Judgments: The Recognition of a French Bankruptcy Case (in Chinese), http://www.ccmt.org.cn/shownews.php?id=8413 (Last visited on 14 June 2016)

[255] Hu Han, Study of China's Rules and Practice in Matters of Recognition and Enforcement of Foreign Judgments (in Chinese), available at http://article.chinalawinfo.com/Article_Detail.asp?ArticleID=23700 (latest visited on 14 June 2016)

[256] *Sino-Australian Mutual Promotion and Protection of the Investment Agreement*, *article 5(3)*

dispute between an Australian company and two Chinese citizens. The Supreme Court of Western Australia rendered the judgment in 2005 and then the Australian company sought recognition thereof in Shenzhen. Later in 2006 the case was appealed to the High People's Court of Guangdong Province and the high court made decision based on the Civil Procedural Law. Without mutual civil and commercial judicial assistance treaty or reciprocity, the high court considered that the application for recognition lack of legal basis and thus refused to grant recognition. In its reply to the high court, the Supreme People's Court considered that there is "no" mutual civil and commercial judicial assistance treaty or reciprocity between China and Australia and thus held that the application for recognition of a civil judgment rendered by an Australian court should be dismissed. [257] What will happen if there is no mutual civil and commercial judicial assistance treaty? The foreign judgment will probably not be recognized.

3.42 In 2011, a judge from Shanghai Municipal High Court wrote an article about a case related to the Lehman Brothers insolvency proceeding.[258] In *Hua An Funds v. Lehman Brothers International Europe* (LBIE) case, a fund management firm of the Mainland China filed petitions to High People's Court of Shanghai Municipality based on the fund product cooperative agreement, claimed for damage of 96,4 million USD and sought an attachment of the assets of the defendant within the territory of the Mainland China right after the business of Lehman Brothers collapsed in 2008. It is noteworthy that there is a fundamental block that cannot be bypassed although the case was dealt in the form of a contract dispute, which is the effect of LBIE's insolvency proceeding in UK. The judge declined to recognize the UK proceeding on the basis of lack of the relevant international treaty between UK and China.

1.2.2 Principle of Reciprocity[259]

3.43 Generally speaking, the principle of reciprocity is the idea that States will and should grant others recognition of judicial decisions only if, and to the extent that, their own decisions would be recognized. [260] Unlike the international treaties, the principle of reciprocity is an ambiguous concept in China, which has

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[257] [2006] Civil Division IV of the Supreme People's Court Others No. 45.

[258] See Zhang Fengxiang, The Needs for Improvement of Relevant Laws Arising from the Financial Derivative Products Cooperative Disputes between Hua An Funds and Lehman Brothers International Europe (in Chinese), in: Frontier of Financial Law, 2011, p.33-45. The dispute was settled down in the way of mediation. Unlike judgments, in China, the results of mediation are not necessary to be disclosed. Nevertheless, in his article the judge provided quite detailed information and analysis on that case because as judge who made decision on that case, he found it necessary to disclose some information as reference for improvement of the legislation involved.

[259] Part of this section has been derived from my publication: Gong Xinyi, To Recognize or Not to Recognize? - Comparative Study of Lehman Brothers Cases in the Mainland China and Taiwan, in: International Corporate Rescue, Chase Cambria, Vol 10, Issue 4, 2013, pp. 240 – 247

[260] Ralf Michaels, Recognition and Enforcement of Foreign Judgments, in: Max Planck Encyclopedia of Public International Law (Rüdiger Wolfrum ed., 2009), Heidelberg and Oxford University Press, para.7.
Available at: http://scholarship.law.duke.edu/faculty_scholarship/2076 (Last visited on 14 June 2016)

neither been defined under the legislation nor interpreted by the Supreme People's Court. In 1995 the Supreme People's Court made a reply to the request of the High Court of Liaoning Province, which was, whether or not to recognize a Japanese judgment involving debt dispute. The Supreme People's Court held that China and Japan did not enter into any international treaties in matters of civil and commercial judgments and no reciprocity had been established, either. Therefore, the application should be dismissed.[261] In Japan, foreign judgments are automatically entitled to recognition in Japan if they fulfill the requirements without any formality or special procedure, such as an action for a judgment or summary judgment granting the recognition or registration of foreign judgments.[262] Therefore, it seems that in terms of reciprocity the Supreme Court did not adopt the "would be" approach but more concrete reciprocal basis, especially the precedents. In the aforementioned *Hua An Funds* case, with respect to reciprocity, the judge held that till now no relevant recognition had been given to China by the UK court and thus the effect of the UK insolvency proceeding could not be recognized on a reciprocal basis, either.[263] The judge in fact made a "substantial" review by investigating in the precedents of the counterpart foreign state in matters of recognition of China's civil or commercial judgments.

3.44 Even some foreign courts realized this problem as well. For example, in 2006 Berlin High Court recognized a money judgment rendered by a Chinese court in accordance with the article 328 of German Code of Civil Procedure (Zivilprozessordnung) on a reciprocal basis.[264] The German court indicated that China and Germany so far did not enter into any bilateral treaties concerning recognition and enforcement in the civil and commercial matters. Neither of them granted recognition to judgments rendered by the counterpart court on the reciprocal basis before. On the contrary, there have been some precedents of refusal due to lack of a reciprocal basis.[265] Nevertheless, the court considered that without international treaties one side should probably start to grant

[261] [1995] Civil Division of the Supreme People's Court Others No. 17

[262] In Japan the criteria of recognition of foreign civil and commercial judgments are governed by the article 118 of CCP Code of Civil Procedure (CCP), which was enacted since 1996. See Tada, Nozomi, Enforcement of Foreign Judgments in Japan Regarding Business Activities, in: Japanese Annual of International Law, No. 46, 2003, p. 75-94

[263]Zhang Fengxiang, The Needs for Improvement of Relevant Laws Arising from the Financial Derivative Products Cooperative Disputes between Hua An Funds and Lehman Brothers International Europe (in Chinese), in: Frontier of Financial Law, 2011, p.41

[264] Kammergericht-Berlin-Aktenzeichen: 20 SCH 13/04, Beschluss von 18.05.2006. Leitsatz: 1. Eine rechtskräftige Entscheidung eines Volksgerichts (in China) kann gemäß §328 ZPO anerkannt werden.
Available at: http://www.juraforum.de/urteile/kammergericht-berlin/kammergericht-berlin-beschluss-vom-18-05-2006-az-20-sch-1304 (Last visited on 14 June 2016)

[265] For instance, in 2001, a German company applied for recognition and enforcement of a judgment involving a finance lease contract dispute between the German company and a Chinese company, which was rendered by the court in Frankfurt. In matters of recognition, the Beijing Second Intermediate People's Court employed the same reasoning as in the aforementioned decision and refused to grant recognition. [2003] First Instance of Beijing Second Intermediate People's Court Civil Mediation No. 00002

recognition and thus solve the reciprocity deadlock. Once that obstacle was removed by Germany at first, China would probably follow.[266]

3.45 As a concept arising from sovereignty, reciprocity is not set up as a requirement either under the EIR or the UNCITRAL Model Law. In EU reciprocity is not necessary because automatic recognition of insolvency proceedings is granted based on mutual trust between the Member States under the Union regime. [267] It is deemed outdated in matters of cross-border insolvency cooperation regarding business from the point view of the Model Law, [268] although a number of countries *de jure* or *de facto* apply the reciprocity requirement in the process of implementing the Model Law.[269] However, it is noteworthy that in China although each region has its own independent legal system, none of the legal cooperative arrangements in civil and commercial matters between the Mainland China and the other three regions contain reciprocity requirement for recognition. Considering the business motivated characteristic of cross-border insolvency and the current form of legal cooperation in China, the principle of reciprocity should not play an influential role on China's regional cross-border insolvency.

1.2.3 Public Policy

3.46 Public policy is not the term that appears in article 5(2) EBL, which is replaced by fundamental principles of law, state sovereignty and security, socio-public interests as well as legitimate rights and interests of the creditors. The equivalent expressions can also be found in article 282 of the current Civil Procedure Law, which stipulates the criteria for the recognition and enforcement of a legally effective civil or commercial judgment or written order rendered by a foreign court.[270] Such diverse expressions are regarded as considerable hurdles of understanding the concept of public policy in the course of China's international judicial cooperation, in particular in the matters of recognition and enforcement of foreign judgments and foreign arbitral awards.[271]

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[266] Kammergericht-Berlin-Aktenzeichen: 20 SCH 13/04, Beschluss von 18.05.2006, para. 2(a)
[267] The EC Regulation, Recital (22)
[268] Wessels, Bob, International Insolvency Law (3rd ed.), Kluwer, 2012, at 10385
[269] They are the British Virgin Islands, Mauritius, Mexico, Romania and South Africa. See Ho, Look Chan(ed., 2nd), Cross-border Insolvency, Global Law and Business, 2012, p. 8
[270] Article 282 of CPL (2012):In the case of an application or request for recognition and enforcement of a legally effective judgment or written order of a foreign court, the people's court shall, after examining it in accordance with the international treaties concluded or acceded to by the People's Republic of China or with the principle of reciprocity and arriving at the conclusion that it does not contradict the primary principles of the law of the People's Republic of China nor violates State sovereignty, security and social and public interest of the country, recognize the validity of the judgment or written order, and, if required, issue a writ of execution to enforce it in accordance with the relevant provisions of this Law; if the application or request contradicts the primary principles of the law of the People's Republic of China or violates State sovereignty, security and social and public interest of the country, the people's court shall not recognize and enforce it.
[271] He Qisheng, Public Policy in Enforcement of Foreign Arbitral Awards in the Supreme People's Court of China, 43 Hong Kong Law Journal 1037, 2013, p.1037

3.47 As public policy has long been acknowledged as "a very unruly horse" in practice,[272] it is the judges who get astride it by exercising discretions. To grasp the concept of public policy, the ideal way is to collect the relevant case law as much as possible and then make summary. Nevertheless, the short time period of implementation of the system concerning publicity of judgments and the cross-border insolvency system combinedly result in limited access to relevant information. In addition, insufficient rules and explanation in matters of cross-border insolvency and reluctance of application thereof due to uncertainty are usually mutually reinforcing, which is to be discussed in section 1.3. On top of that, it is required by the article 4 of EBL that the provisions of the CPL should be applicable in case that the EBL does not provide the relevant provisions in dealing with the bankruptcy proceedings, for example, international jurisdiction and applicable law. As result, in the following sections, I sometimes have to refer to the civil and commercial cases as expedient alternatives for comprehension of public policy in the judicial practice of the Mainland.

1.2.3.1 Fundamental Principles of Law

3.48 Due to lack of legislative and judicial interpretation, the concept of the fundamental principles of law is quite vague and broad. Considering it is stipulated in the phrase of article 5,[273] the most related law should be the EBL itself. What are the basic principles of the EBL? The EBL itself does not specify them. After the EBL came into effect, there is only some academic discussion concerning this issue.[274] There seems to be some development in practice. In 2012, a district court in Shanghai heard a case between a local debtor and a local creditor involving individual debt collection action after the debtor was ordered bankrupt.[275] The action was considered invalid and the court clearly stated that protection of equal treatment of the creditors is the primary aim of the bankruptcy law and also serves as one of the basic principles thereof. However, without national wide case registry system and standard criteria, a comprehensive understanding of the fundamental principles of law in the context of cross-border insolvency is missing.

1.2.3.2 State Sovereignty and Security

3.49 In the Mainland, sometimes the sovereignty requirement has something to do with the language. For example, some court considered that translation of relevant documents and supporting materials from foreign language into

[272] *Richardson v.Mellish* (1824) 2 Bing.228; (1824-34) All ER Rep. 258

[273] The English translation of the EBL is provided by the National People's Congress (China's legislator) and published on its official website.
http://www.npc.gov.cn/englishnpc/Law/Integrated_index.html (Last visited on 14 June 2016)

[274] Qi Shujie, Research of Bankruptcy Law (in Chinese), Xiamen University Press, 2005, p. 62-91; Xu Defeng, Rethinking Basic Principles of Bankruptcy Law (in Chinese), in: Legal Science, issue 8, 2009, p. 49-59

[275] [2012] Shanghai Pudong New Area District Court Civil Litigation Second Division (Commercial) First Instance No. 1119

Chinese was required based on the principle of state sovereignty, which could help the Chinese court to make investigation and discover the fact.[276]

3.50 As for Taiwan, the "One China" principle is firmly held by the Mainland courts in dealing with Taiwan related case.[277] In 2004, an application for recognition of an arbitral award rendered by an arbitral tribunal in Taiwan was submitted to a Mainland court. It has been argued that the arbitral tribunal was inconsistent because the arbitral tribunal that appeared on the arbitral award submitted by the applicant was "the Arbitration Association of China" but in fact it was "the Arbitration Association of the Republic of China"[278] that rendered the award. The court noticed that the special heading appearing on the arbitral award was used in the Mainland area alone. Thus the court considered that the arbitral tribunal changed the description of its title for the purpose of facilitating recognition and enforcement of its arbitral award in the Mainland China, which could be deemed as consistency with the "One China" principle and the award thus should be recognized.[279]

3.51 Further, the dispute concerning jurisdiction can cause concerns of the principle of state sovereignty. In order to guarantee the independent judicial power of each state or region, a Chinese court can still exercise its jurisdiction over the same dispute if it falls within the ambit of competence of the Chinese court, although there are parallel civil or commercial proceedings opened in other states or regions.[280]

1.2.3.3 Socio-Public Interests

3.52 Socio-public interests play an important role in China's civil and commercial law. A civil act that violates the public interests shall be null and void.[281] For example, a contract is deemed invalid if it does harm to the socio-public interests.[282] Nevertheless, the socio-public interests, similar to other public policy provisions, do not have a concrete definition. The provision of socio-public

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[276] [2009] Wuhan Intermediate People's Court of Hubei Province Intellectual Property First Instance No. 519

[277] [2004] Xiamen Intermediate People's Court of Fujian Province Civil Recognition No. 20

[278] Republic of China was originally founded in 1912. After the establishment of the People's Republic of China in 1949, Republic of China relocated its government to Taiwan and its surrounding areas. Since 1971 the People's Republic of China restored its position in United Nations, whose representatives are "the only lawful representatives of China" and expelled the unlawful representatives of Republic of China.
See United Nations General Assembly Resolution 2758, Restoration of the Lawful Rights of the People's Republic of China in the United Nations, visit http://daccess-dds-ny.un.org/doc/RESOLUTION/GEN/NR0/327/74/IMG/NR032774.pdf?OpenElement (last visited on 14 June 2016)

[279] [2004] Xiamen Intermediate People's Court of Fujian Province Civil Recognition No. 20 (in Chinese)

[280] [2003] Xiamen Intermediate People's Court of Fujian Province Economic First Instance No. 146. In that case, the Xiamen Intermediate People's Court of Fujian Province also made detailed explanation on *forum non conveniens*. The case was regarded as model case in that regard and thus published in Gazette of Supreme People's Court Vol.7, 2004, pp.32-34

[281] General Principles of Civil Law of P.R.C., article 58(5)

[282] Contract Law of P.R.C., article 52(4)

interests functions like a general principle in order to make up for legal blanks left behind by the statutes and thus remains flexible enough in order to facilitate the judicial discretion. In practice, the provision of socio-public interests is not frequently utilized by the people's courts in handling bankruptcy cases if there are other specific provisions available. For instance, an employee filed a petition against his employer (a company) that was declared bankrupt for his salaries and compensations. The employee referred to the socio-public interests as one of the important legal basis for his claims. Without adopting the public interests argument, the court approved his claims simply pursuant to article 48 of the EBL.[283]

3.53 Nevertheless, it is noteworthy that public interests can be taken into account when it involves the state-owned company. In 2007, there was a case concerning debt assignment disputes between a creditor and two state-owned companies, one of which was the parent company of the other.[284] Both of them were declared bankrupt and had been listed in the national bankruptcy plan of the year 2003, which is so-called policy-mandated bankruptcy[285]. In accordance with the relevant administrative regulation[286], once listed in the national bankruptcy plan approved by the State Council, the debt can no longer be transferred to the external creditors. The creditor received the debt from a third party who legally took over the debt from the two debtors. The appellate court had the same opinion as the court of first instance, holding that the agreement of debt assignment violated the public interests and should be deemed as invalid. With respect to the socio-public interests, the court considered that policy-mandated bankruptcy aimed at improving the reform of the state-owned companies and maintaining the social stability, which was undoubtedly related to the socio-public interests.

1.2.3.4 Legitimate Rights and Interests of the Creditors

[283] [2011] Shenzhen Intermediate People's Court Civil Division VI Final Instance No. 94
The EBL, article 48: a creditor shall, within the time limit specified by the people's court for declaration of his claims, file his claim to the administrator.
The wages, subsidies for medical treatment and disability, comfort and compensatory funds as defaulted by a debtor, the fundamental old-age insurance premiums, fundamental medical insurance premiums that shall have been transferred into the employees' personal accounts as well as the compensation for the employees as prescribed by the relevant laws and administrative regulations are not required to be reported, for which the relevant bankruptcy administrator shall make a corresponding checklist upon investigation and make it known to the public. Where any employee has any different opinion to the relevant checklist, he may request the administrator to make correction. Where a bankruptcy administrator fails to correct it, the relevant employee may present a petition before the people's court.
[284] [2007] Hainan High People's Court Civil Division I Final Instance No. 28
[285] In addition although the EBL intends to apply to both SOEs and non-SOE legal person enterprises, the reality is that parallel to the normal bankruptcy proceedings, the administrative closure is also stipulated in the EBL (article 133 of the EBL), which means, certain state-owned enterprises within the period and scope as are prescribed by the State Council before the EBL came into effect shall be handled according to the relevant regulations of the State Council and therefore are excluded from the EBL. See also Charles D Booth, The 2006 P.R.C. Enterprise Bankruptcy Law: the Wait is Finally Over, in: 20 Singapore Academy of Law Journal, 2008, 275.
[286] [2005] Ministry of Finance Financial No. 74, article 2

3.54 What are the legitimate rights of the creditors within the territory of P.R.C.? It is a matter of applicable law. According to Wang Xinxin, one of the drafters of the EBL, it depends on where the debtor's domicile is located. If the domicile of the debtor is in the Mainland and the Mainland court can exercise jurisdiction over the debtor's insolvency proceeding, the legitimate rights shall entail all the legitimate rights granted by the laws of the Mainland(*lex concursus*), including the EBL.[287] In accordance with the EBL, they are mainly the right to apply for opening of bankruptcy proceeding (liquidation or reorganization),[288] the right to declare the claims and to participate in the creditors' meeting[289] and the right to set off. During the insolvency proceeding, most of the influential rights are granted to the creditors' meeting, which generally include (1) checking the claims; (2) supervising the work of the administrator; (3) adopting plans for reorganization or adopting agreements for compromise; (4) adopting plans for management of the debtor's property, adopting plans for realizing the bankruptcy property into money and adopting plans for distribution of the bankruptcy property; (5) deciding on whether to have the debtor continue or discontinue his business operations.[290] If the debtor is domiciled outside the Mainland and the Mainland court is thus not competent to open the insolvency proceeding, the legitimate rights shall refer to the rights in accordance with the bankruptcy law in the foreign state and other laws except for the EBL in the Mainland.[291] Accordingly, it seems that the applicability of the foreign *lex concursus* can be accepted indirectly under the current EBL.

3.55 The EBL does not set limitation on the scope of creditors, which means, in theory, foreign creditors can also apply for the opening of bankruptcy proceedings and enjoy the same legitimate rights. Nevertheless, in matters of cross-border insolvency, does a creditor, whose domicile or registered office is abroad, have the same rights as a domestic creditor under the EBL? Probably not. To recognize a foreign insolvency proceeding, only the legitimate rights and interests of the creditors "within the territory of P.R.C." is taken into consideration under the article 5 of the EBL. Also in the *Hua An* case, by referring to the article 5, the judge stated that without relevant treaties and precedents of reciprocity, the court could protect the legitimate rights and interests of the creditors within the territory of P.R.C. "in priority" in the way of accepting the lawsuit (as an ordinary civil dispute) and ordering interim attachment on the assets.[292] Nonetheless, from the perspective of international insolvency law, domestic and foreign creditors should be equally treated. Without recognition, the court could not grant any relief to assist the foreign insolvency proceedings

[287] Wang Xinxin, Wang Jianbin, Analysis About China's Acknowledging Extraterritorial Effect System Of Foreign Bankrupt Procedure And Its Improvement (in Chinese), in: Law Science Magazine, Issue 6, 2008, p.12
[288] The EBL, article 7
[289] The EBL, Chapter VI & article 59
[290] The EBL, article 61
[291] Wang Xinxin, Wang Jianbin, Analysis About China's Acknowledging Extraterritorial Effect System Of Foreign Bankrupt Procedure And Its Improvement (in Chinese), in: Law Science Magazine, Issue 6, 2008, p.12
[292] Zhang Fengxiang, The Needs for Improvement of Relevant Laws Arising from the Financial Derivative Products Cooperative Disputes between Hua An Funds and Lehman Brothers International Europe (in Chinese), in: Frontier of Financial Law, 2011, p.41.

and thus the legitimate rights and interests of the foreign creditors in the foreign insolvency proceedings will be jeopardized.

3.56 In summary, the current EBL does not provide clear explanation with respect to those various expressions regarding public policy. Although some relevant civil and commercial case law has been found for reference, its reference value is limited because cross-border insolvency law has its own features and needs interpretation peculiar to its own characters. It is suggested to clarify the detailed public policy rules under the current EBL to prevent uncertainty in deciding insolvency cases and different understanding of the same norms on domestic level.

1.3 Consequences Arising from Insufficient Rules[293]

3.57 When the problems of the domestic insolvency system bring down the amount of national insolvency cases, the insufficient rules on cross-border insolvency law discourage filings of recognition and enforcement of the foreign and regional insolvency proceedings before the Mainland courts at the same time.

3.58 On international level, Suntech Power is such a typical example.[294] In 2001, Wuxi Suntech was founded in Wuxi, Jiangsu Province, China. In 2005, Suntech Power Holdings Co. Ltd. was registered in Cayman Islands (Suntech Power). The original purpose of establishing the Suntech Power was to facilitate privatization of Suntech by purchasing the state-owned stocks and the ultimate goal was to be listed on the New York Stock Exchange (NYSE), which was realized by the end of 2005.[295] The aforementioned recession of the photovoltaic industry resulted in multiple cross-border insolvency proceedings concerning Suntech Power in China,[296] the Cayman Islands and the United States[297]. On 17 November 2014, the United States Bankruptcy Court for the Southern District of New York

[293] Part of this section has been derived from my publication Gong, Xinyi, When Hong Kong Becomes SAR, Is the Mainland Ready? – Problems of Judgments Recognition in Cross-border Insolvency Matters, in: International Insolvency Review, Wiley-Blackwell, Vol. 20, Issue 1, 2011, p.63-64; and also Gong Xinyi, Can the Day Understand the Night? Brief Introduction into Problems of the Current Insolvency System in China, 2015, available at http://iiiglobal.org/iii-prize-in-insolvency.html (Last visited on 14 June 2016)

[294] In *re Suntech Power Holdings Co., Ltd.*, Case No.: 14-10383(SMB), Written Opinion Signed On 17 November, 2014

[295] Li Yulong(ed.), Legal Analysis of Private Equity Cases (in Chinese), Law Press, 2009, p. 3-4

[296] On 20 March 2013, the Mainland court accepted the application of reorganization of Wuxi Suntech (the Wuxi proceeding). See Wu Xi Intermediate Court Successfully Concluded the Suntech Reorganization Proceeding, the Reorganization Plan Has Been Almost Completely Implemented (in Chinese), 7 January, 2014, p.4, available at: http://wxzy.chinacourt.org/public/detail.php?id=5228 (Last visited on 14 June 2016)

[297] On 5 November 2013, provisional liquidation of Suntech Power was initiated in Cayman Islands (the Cayman proceeding). On 21 February 2014, a petition was filed for recognition of Suntech Power's provisional liquidation proceeding pending in Cayman Islands as a foreign main proceeding or non-main proceeding before the United States Bankruptcy Court for the Southern District of New York (S.D.N.Y.) In *re Suntech Power Holdings Co., Ltd.*, Case No.: 14-10383(SMB), Written Opinion Signed On 17 November, 2014, available at http://www.nysb.uscourts.gov/sites/default/files/opinions/247366_67_opinion.pdf(Last visited on 14 June 2016)

(S.D.N.Y.) recognized the Cayman proceeding as the foreign main proceeding.[298] However, as of the commencement of the Cayman proceeding, it was pointed by Solyndra, one of Suntech Power's American creditors that the headquarter, manufacturing facilities and primary assets of Suntech were in China.[299] The intent to shift COMI from China to the Cayman Islands was not hidden. I will turn to the COMI issue of this case later in the section 2.1.4.2 of Part IV. The attorney representing one of the debtor's largest creditor groups called China "the last place that one would go"[300] and indicated that

"The Chinese court's jurisdiction was in doubt, and China has different concepts of the rules of law and creditors' rights compared to those found in the Cayman Islands and the United States."[301]

3.59 Interestingly in the same year, the United States Bankruptcy Court District of New Jersey in *re Zhejiang Topoint photovoltaic CO. Ltd.*, considered all parties concerned in the United States had received due and proper notice of the petition and thus granted recognition of the joint bankruptcy proceedings pending in China[302] as the main proceedings and the relevant reliefs, including suspension on disposal of assets within New Jersey.[303] It seems that the opinions on China's insolvency system in the United States are not univocal. Nevertheless, in the course of cross-border insolvency cooperation, different insolvency systems are merely different options. The underlying consideration is that the parties concerned can choose a more favorable forum to his or her benefit, if the problems in one jurisdiction are considered unacceptable and its cross-border insolvency system deemed unpredictable.

3.60 On regional level, as aforementioned in Introduction (Part I), there is no arrangement in resolving conflicts arising from cross-border insolvency between the Mainland and the SARs. How to recognize and enforce the inter-regional judgments of opening insolvency proceedings and inter-regional judgments, which are directly derived from insolvency proceedings, remains a problem. In practice, instead of submitting a request for recognition before the Mainland courts, the related judgments seek enforcement in an indirect way. In the case of

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[298] In *re Suntech Power Holdings Co., Ltd.*, Case No.: 14-10383(SMB), Written Opinion Signed On 17 November, 2014, p.3

[299] Objection of the Solyndra Residual Trust to Chapter 15 Petition of *Suntech Power Holdings Co., Ltd.* (in provisional liquidation) for Recognition of Foreign Main Proceeding Pursuant to Section 1517 of the Bankruptcy Code, In *re Suntech Power Holdings Co., Ltd.* (in Provisional Liquidation), Case No. 14-10383 (SMB), Related Docket Nos. 1, 2, 3, 4, p.2

[300] In *re Suntech Power Holdings Co., Ltd*., Case No.: 14-10383(SMB), Written Opinion Signed On 17 November, 2014, at Background, B. Foreign Proceeding, p.6; C. COMI, p.29

[301] In *re Suntech Power Holdings Co., Ltd*., Case No.: 14-10383(SMB), Written Opinion Signed On 17 November, 2014, at Background, B. Foreign Proceeding, p.5-6

[302] [2014] Jiaxing Haining Bankruptcy(Pre) No.4 (in Chinese)

[303] The bankruptcy proceedings involved Zhejiang Topoint Photovoltaic Co. Ltd. and its three affiliates, Zhejiang Jiutai New Energy Co. Ltd., Zhejiang Yutai Solar Materials Co. Ltd. and Zhejiang Willsolar Photoelectric Materials Co. Ltd. Recognition was granted altogether on 12 August 2014. Their jointly administered proceedings are (i) *Zhejiang Topoint Photovoltaic Co., Ltd.*, Case No. 14-24549-GMB; (ii) *Zhejiang Jiutai New Energy Co., Ltd.*, Case No. 14-24555-GMB; (iii) *Zhejiang Yutai Solar Materials Co., Ltd.*, Case No. 14-24557-GMB; and (iv) *Zhejiang Willsolar Photoelectric Materials Co., Ltd.*, Case No. 14-24559-GMB.

Gu Laiyun and others versus Nardu Company Limited,[304] a liquidator appointed by Hong Kong High Court became a vice president of the company through a shareholders' resolution in the Mainland. In 1993, Nardu Company, registered in HKSAR, signed a joint venture contract with a local real estate company in Guangzhou Province of the Mainland and finally established the Fuyu Company in Guangzhou Province. On 22 June 2005, Hong Kong High Court issued a winding-up order of Nardu Company Limited. On 15 February 2006, two employees of Hong Kong Grant Thornton International Accounting Firm were appointed by Hong Kong High Court as liquidators of Nardu Company Limited. On 2 March 2006, one of the liquidators, Ms. Li Fengying was elected as a vice president of Fuyu Company through a shareholders' resolution. It was stated in the same shareholders' resolution that the business license, seals, accounting records and properties, etc. of the company should be handed over to its new vice president.

3.61 The advantages of that kind of arrangement are obvious. First of all, the liquidator could directly control the assets the Hong Kong debtor located in the Mainland without waiting for the recognition of the Mainland court. The other advantage of this arrangement was fully demonstrated when the former legal representative and the manager of Fuyu Company refused to return the items mentioned, Nardu Company Limited represented by Ms. Li filed a lawsuit against them. Furthermore, due to the dual identity of Ms. Li who was both the liquidator appointed by Hong Kong High Court and the vice president of Fuyu Company, the problem whether the legitimacy of Ms. Li's representation needed to be recognized or not, or whether the winding-up order of Hong Kong High Court should be recognized in advance or not has been by passed. Instead, the Company Law of PRC was applicable to qualification of Ms. Li's actions in the Mainland[305] and the representation power of the liquidator was taken for granted on the same basis.

3.62 This strategy, in which the liquidator appointed by the Hong Kong court becomes member of management or director of the company in the Mainland, seems ideal but it is not satisfactory as a long-term solution. First of all, the status of the liquidator is confusing. They are both the liquidator appointed by the Hong Kong court and a member of management or a representative of a Mainland company at the same time. This is a solution resulting in issues of conflicts of interests, for a liquidator of a Hong Kong wound up company will have to act in the interest of the general body of creditors, whilst a member of

[304] [2007] Guangzhou Intermediate People's Court Civil Fourth Tribunal Final Instance No.7(in Chinese)

[305] The court referred to the Company Law of PRC (2005), article 152:
Where the board of supervisors or the supervisor of a company with limited liability where there is no such board, or the board of directors, or the executive director refuses to take legal proceedings after receiving the written request from the shareholders as specified in the preceding paragraph, or fails to take legal proceedings within 30 days from the date it/he receives such request, or under emergency situations, failure to take legal proceedings immediately results in irreparable damage to the interests of the company, the shareholders specified in the preceding paragraph shall have the right, in their own names, directly to bring a lawsuit to a people's court in the interests of the company.

management or a representative of a local Mainland company is required to act to the benefit of the interests of the company.

3.63 Secondly, it may be complicated and time-consuming. If the liquidators from HKSAR want to become a member of the management in order to control the relevant assets of the company in the Mainland, there are also a lot of requirements. Both the limited liability company and the public limited liability company, which are two main types of companies in the Mainland, have strict rules for the election of the member of the management stipulated either by the Company Law of PRC or by each company's own articles of association.[306] In the case Gu Laiyun and others versus Nardu Company Limited, the reason why the liquidator could successfully become the vice president of the Fuyu company in a short time was that the Nardu Company Ltd was the largest shareholder accounting for 80% of the Fuyu company. However, not all the bankrupt shareholders of Hong Kong can have the same leading portion and the other shareholders may not agree to vote for the liquidator because the idea of enabling a liquidator to interfere with the corporate governance may not be benefit to them. Even though the other shareholders are finally persuaded to vote for the liquidator, it still does not mean that the liquidator has the substantial control over the relevant assets. Without the cooperation of the former management, the handover will probably be extended by one lawsuit or more.

3.64 *First China Technology (Hong Kong) Limited versus Yeung Chung-lung and Fuqing Longyu Food Development Co., Ltd*.[307]is such an example. A provisional liquidator appointed by Hong Kong High Court was also designated by Hong Kong High Court in the same order as the sole member of board of the wound up Hong Kong company, which had a wholly owned subsidiary in the Mainland. The provisional liquidator passed a board resolution that replaced the board of its Mainland subsidiary, including its founder and former chairman, Yeung Chung-lung. The former chairman did not cooperate to facilitate the handover. Therefore, the provisional liquidator had to file a petition before the Mainland court in order to enforce the board resolution. Interestingly, the Mainland court acknowledged the validity of the board resolution, holding that the provisional liquidator exercised its power in a way that did not exceed the limits required under the order of appointment rendered by Hong Kong High Court. Nevertheless, it did not indicate whether the winding-up order should be recognized at the first place as if the winding-up order had been deemed as effective in the Mainland.

3.65 In fact, appointment of provisional liquidator or liquidator as member of the management or representative of the Mainland subsidiaries is an indispensible part of the winding-up order. A winding-up order rendered by Hong Kong court, which has independent jurisdiction, does not automatically have effect in the Mainland unless upon recognition. Prior to that, the provisional liquidators or liquidators do not have proper authority to take over the assets of the Mainland

[306] Company Law of PRC (2013), article 105
[307] [2009] Fuzhou Intermediate People's Court Civil First Instance No.166 (in Chinese)

subsidiaries. Therefore, the indirect solution adopted in practice may seemingly bring some advantages at the first sight but in essence it is merely an evasion of the genuine problems, which involve uncertainty of recognition and lack of ancillary reliefs and coordination. That's why it is necessary to make regional cross-border insolvency arrangements, which can remove the uncertainty concerned eventually.

Ch. 2 Hong Kong Approach

3.66 The first section of this chapter explains the difference of corporate insolvency system and individual bankruptcy system in Hong Kong. It also briefly introduces the recent reform of Companies Ordinance and its influence on insolvency law in Hong Kong. Further, the consultation conclusion on corporate insolvency law improvement, which was issued by the Legislative Council of Hong Kong in July 2014, is also referred to. The second section focuses on the development of the cross-border insolvency in Hong Kong by reviewing the relevant legislative proposals and analyzes its hesitation in accommodating a cross-border insolvency regime. In the third section, the non-statutory feature of HK insolvency system is presented. Key elements of HK cross-border insolvency system such as jurisdiction, recognition and coordination and communication are discussed. Considering the common law characteristics of Hong Kong, they will be examined mainly on the basis of recent case law.

2.1 Brief Introduction into Local Insolvency System

3.67 Hong Kong applies separate insolvency system to companies and individuals. After the revision of the Companies Ordinance, its corporate insolvency system has been put on the reform agenda and a statutory company rescue regime is proposed. As for cross-border insolvency, although the adoption of UNCITRAL Model Law has been taken into consideration, it is still a plan to establish a statutory cross-border insolvency system in Hong Kong, which will probably take time to come into reality.

2.1.1 Companies Ordinance and Bankruptcy Ordinance

3.68 The insolvency system of Hong Kong is not a combined system. The personal insolvency is regulated under the Bankruptcy Ordinance, whereas the Companies Ordinance deals with corporate winding-up. It is noteworthy that the Bankruptcy Ordinance is also applied to insolvent companies from time to time. For example, over the years the Department of Justice, whose role is to provide legislative advices to the Legislative Council, have on numerous occasions drafted amendments to legislation by cross-referring parts of the Companies Ordinance to the Bankruptcy Ordinance.[308] Another example is the Companies Ordinance relies on the cross-references to the provisions on unfair preferences under the BO with modifications to corporate winding-up cases,[309] which has

[308] Briscoe, Stephen, & Booth, Charles D, Hong Kong Corporate Insolvency Manual (2nd), published by Hong Kong Institute of Certified Public Accountants, 2009, p.5
[309] Cap 32 s266, 266A and 266B refer to s 50 to 51B of the BO.

been proposed for reform by introducing the relevant self-contained provisions into the Companies Ordinance.[310] Financial institutions are resolved pursuant to specialized legislation, for instance, the Banking Ordinance in matters of winding-up of a bank, Insurance Companies Ordinance in case of winding-up of an insurance company.

2.1.2 Revision of Companies Ordinance and Reform of Insolvency Law

3.69 The new Companies Ordinance (Cap 622) was passed on 12 July of 2012, which will come into effect in early 2014. Nevertheless, nothing has been changed in matters of the corporate insolvency under the new Companies Ordinance. The winding-up and insolvency related provisions still remain in the former Companies Ordinance but have a different title the Companies (Winding-up and Miscellaneous Provisions) Ordinance (Cap 32). In 2013, the Financial Services and the Treasury Bureau issued consultation paper on Improvement of Corporate Insolvency Law,[311] in which there are 46 legislative proposals to improve Hong Kong's current corporate insolvency law regime. The consultation lasted for about three month from April to July 2013.[312] In May 2014, the Financial Services and the Treasury Bureau briefed the outcome of the public consultation and the responses of the government[313] and an updated brief was submitted to the Legislative Council in July 2014.[314] It mainly covers the following topics:

(a) commencement of winding-up;
(b) appointment, powers, vacation of office and release of provisional liquidators and liquidators;
(c) conduct of winding-up;
(d) voidable transactions; and
(e) investigation during winding-up, offences antecedent to or in the course of winding-up and powers of the court.

3.70 On top of that, a new statutory company rescue regime has been proposed.[315] Till now, Hong Kong still lacks a statutory company rescue regime. Under the current system, a corporate rescue can only be brought about through

[310] Financial Services and the Treasury Bureau, Improvement of Corporate Insolvency Law Legislative Proposal (consultation paper), April 2013, at 5.16 http://www.fstb.gov.hk/fsb/ppr/consult/impcill.htm (Last visited on 14 June 2016)
[311] Financial Services and the Treasury Bureau, Improvement of Corporate Insolvency Law Legislative Proposal (consultation paper), April 2013, available at: www. fstb.gov.hk (Last visited on 14 June 2016)
[312] Legislative Council Panel on Financial Affairs Meeting on 7 July 2014, Updated background brief on review of corporate insolvency law and introduction of a statutory corporate rescue procedure, LC Paper No. CB(1)1668/13-14(02), 7 July 2014, p.1
[313] Financial Services and the Treasury Bureau, Improvement of Corporate Insolvency Law Legislative Proposals Consultation Conclusions, 28 May 2014, available at: www. fstb.gov.hk (Last visited on 14 June 2016)
[314] Legislative Council Panel on Financial Affairs, Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure, CB(1)1536/13-14(01), 7 July 2014
[315] Legislative Council Panel on Financial Affairs, Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure, CB(1)1536/13-14(01), 7 July 2014, p.3-10 & Annex B

the procedure of a scheme of arrangement according to Companies Ordinance.[316] Different from the winding-up proceeding, there is no such relief as moratorium or stay of proceedings against the company while a scheme of arrangement is being worked out. In other words, the fact that a company is pursuing a scheme of arrangement does not provide standstill to stay proceedings against the company generally or to give the company breathing space in respect of its obligations to creditors. To make up for the legislative blank in practice, a stay of proceedings against the company is usually brought about by Cap 32 s186 with the appointment of a provisional liquidator. The Hong Kong courts seem to approve this approach so as to mitigate the difficulty of the lack of a moratorium while a restructuring proposal is being worked out, until there is new legislation for a corporate rescue procedure.[317]

3.71 In 2009, the Hong Kong government formally announced a public consultation on the review of legislative proposals on corporate rescue procedure. The proposed rescue procedure will not be a US-style Chapter 11. Instead, it is recommended to introduce a regime of "provisional supervision", which is similar to voluntary administration in the UK or Australia.[318] In 2014, the provisional supervision approach has been further detailed by the government in the proposal concerning the new statutory corporate rescue procedure, which mainly includes initiation of provisional supervision/appointment of provisional supervisor, effect of provisional supervision and rights of secured creditors, status, role, duty and powers of provisional supervisor, process and termination of the provisional supervision, process and termination of the voluntary arrangement.[319] In addition, problems concerning insolvent trading provisions,[320] safeguards for abuse of the special procedure set out in section 228A of the former CO[321] have also been addressed in the proposal. Financial Services and Treasury Bureau intended to prepare an amendment bill with a view to introduce the proposal into the Legislative Council in 2015.[322]

2.2 Pending Development of Cross-border Insolvency Law

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316 Cap 622, s. 668-670, 673, 674, 677

317 See for example: *Re Keview Technology (BVI) Ltd.* [2002] 2 HKLRD 290; *Re Luen Cheong Tai International Holdings Ltd.* [2002] 3 HKLRD 610; *Re I-China Holdings Ltd.* [2003] 1 HKLRD 629; *Re Fujian Group Ltd.* [2003] HKEC 266

318 For more details of the "provisional supervision" proposal, see Booth, Charles D. & Lain, Trevor N., Rescuing Hong Kong Companies with Provisional Supervision: Proposals That Workers and Management Can Support, in: Hong Kong Law Journal (40 HKLJ 271), 2010.

319 Legislative Council Panel on Financial Affairs, Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure, CB(1)1536/13-14(01), 7 July 2014, Annex B

320 Legislative Council Panel on Financial Affairs, Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure, CB(1)1536/13-14(01), 7 July 2014, Annex C

321 Legislative Council Panel on Financial Affairs, Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure, CB(1)1536/13-14(01), 7 July 2014, Appendix III-B

322 Financial Services and the Treasury Bureau, Improvement of Corporate Insolvency Law Legislative Proposals Consultation Conclusions, 28 May 2014, p.10, available at: www. fstb.gov.hk (Last visited on 14 June 2016)

3.72 As a region deeply influenced by common law, Hong Kong does not have a comprehensive legislative framework for resolving cross-border insolvency issues but deals with the cross-border insolvency matters in a common law manner. Only a few provisions in the Companies Ordinance can be referred to in matters of cross-border insolvency. Cap 32 Part X s327 grants the court the authority to wind up the companies incorporated outside Hong Kong, which are non-Hong Kong companies in accordance with the Companies Ordinance.[323]

3.73 Although the Law Reform Commission[324] considered the adoption of UNICTRAL Model Law into the Companies Ordinance in 1999. It was stated in the Commission's 1999 Report on the Winding-up Provisions of the Companies Ordinance that

We note that there is some strong support for adoption of the UNCITRAL Model Law of Insolvency, … but we have been unable to find any jurisdiction which has adopted the Model Law and we are hesitant about recommending that Hong Kong, which is a relatively small jurisdiction, should pioneer the Model Law. (para 26.3)
…
We do not reject the Model Law. We are simply exercising caution and a watch and wait approach. When the Model Law is adopted by leading jurisdictions, that would be the time to consider adopting the Model Law in Hong Kong, but until that happens we consider that there is no benefit in being the first to adopt the Model Law. (para 26.43)[325]

3.74 In the 2014 proposal, it has been well acknowledged that

"At present, the court has the power to deal with certain cross-border insolvency cases under section 327 of the C(WUMP)O. However, there are certain limits to the extent to which a Hong Kong court will recognize the vesting and discharging effects of a non-Hong Kong order. We note that while some overseas jurisdictions have adopted the Model Law on Cross-Border Insolvency of the United Nations Commission on International Trade Law, many jurisdictions, particularly those in Asia (e.g. Singapore and the Mainland), still rely on the local legislation to handle such cases. We will closely monitor the international development in this regard and will consider how best to take forward the matter."[326]

3.75 It is observed that Hong Kong still adopted a wait-and-see attitude towards the reform of its cross-border insolvency law. Although the UNCITRAL Model

[323] Cap 622, s2: non-Hong Kong company means a company incorporated outside Hong Kong that—(a) establishes a place of business in Hong Kong on or after the commencement date of Part 16; or (b) has established a place of business in Hong Kong before that commencement date and continues to have a place of business in Hong Kong at that commencement date.
[324] The Law Reform Commission of Hong Kong was established in January 1980. The Commission considers for reform those aspects of the laws of Hong Kong, which are referred to it by the Secretary for Justice or the Chief Justice.
[325] The Law Reform Commission of Hong Kong, 1999 Report on the Winding-up Provisions of the Companies Ordinance, available at: http://www.hkreform.gov.hk/en/publications/rwind.htm (Last visited 14 June 2016)
[326] Legislative Council Panel on Financial Affairs, Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure, CB(1)1536/13-14(01), 7 July 2014, p.65

Law was published nearly two decades and over 40 countries and regions have adopted the Model Law as part of their domestic laws,[327] concerns have been expressed about the possibility of synchronous development in the neighboring jurisdictions, in particular, the Mainland. Due to the closer economic relationship between the Mainland and Hong Kong, the need for trans-regional cooperation in matters of cross-border insolvency has never been higher. For instance, many Hong Kong companies have set up branches in the Mainland. Some of the local companies may transfer their assets to their associated enterprises in the Mainland instantly before winding-up.[328] Lack of cooperation will probably result in assets dissipation.

2.3 Current Cross-border Insolvency Law in Hong Kong

3.76 In Hong Kong, it is lack of statutory that provides cross-border insolvency cooperation. This section will introduce the current cross-border insolvency system by referring to illustrative case law and touches on the topics of jurisdiction, the ways of recognition and coordination and communication. It is noteworthy that owing to lack of ancillary proceedings or reliefs for cross-border insolvency cooperation, rules of jurisdiction, which enables commencement of the parallel territorial insolvency proceedings, play a very important role in Hong Kong's current cross-border insolvency system.

2.3.1 Jurisdiction

2.3.1.1 Statutory Basis

3.77 A non-Hong Kong company, which is incorporated abroad, is called an "unregistered company" in Hong Kong[329]; it also includes an "oversea company" as a consequence of the decision of the court in the case of *Securities and Futures Commission v MKI Corporation*, which held that an "oversea company" might be wound-up as an "unregistered company" in Hong Kong.[330] It is stipulated under Cap 32 s.327(1) that subject to the provisions of Cap 32 Part X, any unregistered company may be wound-up. As a result, an insolvency practitioner appointed in the company's place of incorporation can also seek a winding-up order in Hong Kong to protect and realize the Hong Kong assets of an unregistered company.

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[327] Available at: http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model_status.html (Last visited on 10 April 2016)

[328] In the case of *Ocean Grand Holdings Limited versus Ocean Grand Aluminum Industrial (San Shui) Ltd.,* Ocean Grand, which was a holding company incorporated in Bermuda, registered in Hong Kong. Its subsidiaries were mainly located in Nanhai and Zhuhai in the Mainland, and in Hong Kong. On 24 July 2006, *Ocean Grand* presented a petition for its own winding up in Hong Kong and in Bermuda. Before the application, Ocean Grand announced on mid July 2006 that a total sum of about 840 million US dollars funds in the four Mainland subsidiaries, including *OG San Shui*, had disappeared. For more detailed information regarding this case, please refer to Gong, Xinyi, When Hong Kong Becomes SAR, Is the Mainland Ready? – Problems of Judgments Recognition in Cross-border Insolvency Matters, in: International Insolvency Review, Wiley-Blackwell, Vol. 20, Issue 1, 2011, p.62

[329] Cap 32 s326(2), Companies Ordinance

[330] *Securities and Futures Commission v MKI Corporation* [1995] 2 HKC 79

An unregistered company may be wound-up in accordance with the Cap 32 s.327(3) on the following grounds,

(a) if the company is dissolved, or has ceased to carry on business, or is carrying on business only for the purposes of winding-up its affairs;
(b) if the company is unable to pay its debts;
(c) if the court is of the opinion that it is just and equitable that the company be wound-up.

3.78 The conditions set up in Cap 32 s.327(3), including inability to pay debts, are not very difficult to satisfy, which result in that the HK courts are conferred on a wide and unfettered jurisdiction to wind up unregistered company.

2.3.1.2 Discretion in Case Law

3.79 As explained by Lord Scott NPJ in the Court of Final Appeal in *Re Chime Corporation Limited,*

"The fact, however, that the terms of a statute create or confer a jurisdiction in very wide terms does not necessarily mean that the courts have an unlimited jurisdiction to make any orders that are within the wide statutory terms." [331]

3.80 There have been settled criteria adopted by the HK courts in exercising their power under Cap 32 s.327 to wind up a non-Hong Kong company, which are so-called three core requirements:

(1) there is sufficient connection with Hong Kong, but this does not necessarily have to consist in the presence of assets within the jurisdiction;
(2) there is a reasonable possibility that the winding-up order would benefit those applying for it; and
(3) the court must be able to exercise jurisdiction over one or more persons interested in the distribution of the company's assets.

3.81 The three core requirements are gradually developed by case law.[332] The wording embedded into the three requirements, such as "sufficient connection", "reasonable possibility" is considered to leave the court with a wide margin of discretion.[333] The Hong Kong court used to hold that the mere presence of assets in Hong Kong was sufficient to establish the jurisdiction, especially satisfy the first two requirements. For instance, in *re China Tianjin International Economic and Technical Cooperative Corporation*,[334] the court should decide whether or not

[331] *Re Chime Corporation Limited* [2004] 7 HKCFAR 546, at 40
[332] The three core requirements were adopted in several cases in Hong Kong. For instance, *Re Zhu Kuan Group Co. Ltd.* [2004] HKCFI 795; HCCW874/2003 (2 August 2004), at 22; *Re Information Security One Ltd* [2007] HKCFI 848; [2007] 3 HKLRD 780; [2007] 4 HKC 383; HCCW212/2007 (13 August 2007) at 8; *Re Beauty China Holdings Ltd* [2009] 6 HKC 351, at 23; In *re Yung Kee Holdings Limited* [2012] 6 HKC 246, at 70; *Re Pioneer Iron and Steel Co. Ltd*. [2013] HKCFI 324, at 27
[333] Kwan, Susan (ed.-in-Chief), Company Law in Hong Kong – Insolvency, Sweet & Maxwell, 2012, p. 529
[334] Zoneheath Associates Ltd., as creditor, which was a United Kingdom Company, sought a winding up order in Hong Kong against China Tianjin International Economic and Technical

the HK court had jurisdiction in winding up a company incorporated in the Mainland. The court considered that presence of substantial assets, which are liable to be recovered in Hong Kong, constituted a solid ground for exercising jurisdiction.[335] In 2014, that point of view has been altered in *re Yung Kee.*[336] The company involved is a company incorporated in the British Virgin Islands ("BVI") and is not registered under the CO. It is the ultimate holding company of a Hong Kong restaurant that is well known in Hong Kong for its roasted goose. It indirectly holds all of the group's businesses and properties, including the Hong Kong restaurant. The applicant sought two reliefs before the HK court. The principal relief is an order under Cap 622 s724 (1) (former Cap 32 s168A).[337] As an alternative, the applicant also sought a winding-up order under Cap 32 s327(3)(c) that gives the HK court a discretionary jurisdiction to wind up an unregistered company on the just and equitable ground. It is noteworthy that BVI company is still solvent. As to whether the court should assume jurisdiction to wind up a foreign company, it is held that

"No single criterion, nor any prescribed combination of criteria, is to be considered as supplying an essential precondition for meeting this requirement: it is a matter of judgment to be made in the light of the evidence presented to the court in a particular case."[338]

3.82 Later in *re Pioneer Iron and Steel*,[339] the three core requirements have been further explored in detail. It is stated in the judgment that the significance of each core requirement will vary from case to case.[340] For the first core requirement, the consideration of the court is different from other aforementioned cases. Without presence of an asset in Hong Kong,[341] the court indicated that

"I accept that if the matter relied on by the Petitioners was the presence of assets in Hong Kong alone a sufficient connection would not have been demonstrated, but they are not."[342]

3.83 The company's sole shareholder and also sole director, who was resident in Hong Kong, made major business decisions concerning the company's affairs

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Cooperative Corporation, which was incorporated in the Mainland and therefore was a non-Hong Kong company. In *re China Tianjin International Economic and Technical Cooperative Corporation* [1994] HKCFI 114; [1994] 1 HKLR 327; [1995] 1 HKC 720; HCCW438/1994

[335] *Re China Tianjin International Economic and Technical Cooperative Corporation* [1995] 1 HKC 720, at 3,6

[336] *Re Yung Kee* [2014] 2 HKC 556

[337] In accordance with Cap 622 s 724 (1):

(1) The Court may exercise the power under section 725(1)(a) and (2) if, on a petition by a member of a company, it considers that—

(a) the company's affairs are being or have been conducted in a manner unfairly prejudicial to the interests of the members generally or of one or more members (including the member); or

(b) an actual or proposed act or omission of the company (including one done or made on behalf of the company) is or would be so prejudicial.

[338] *Re Yung Kee* [2014] 2 HKC 556, at 42

[339] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324

[340] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 28

[341] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 34

[342] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 35

from her base in Hong Kong.[343] Thus the court considered that "the controlling mind" of the company was based in Hong Kong, which constituted a substantial connection with Hong Kong."[344] As for the second core requirement, the court considered that it was satisfied through the use of the procedures provided for in the Companies Ordinance. For example, it is stipulated under the Cap 32 s221 that once Hong Kong proceeding commences, the liquidator will be enabled to have investigatory powers, which can be deemed as beneficial to the applicants.[345] With respect to the third core requirement, the court must be able to exercise jurisdiction over "a person who is concerned with the proper distribution of assets and over whom the Court can exercise jurisdiction other than by virtue of him being a creditor of the company".[346] The fact that the sole shareholder of the company asserted that she had a significant claim against the company was sufficient to satisfy the third requirement.[347] In addition, as indicated in *Re Pioneer Iron and Steel Group*, under the exceptional circumstance that the connection with Hong Kong is so strong and the benefits of a winding-up order for the creditors of a company are so substantial, the court would be willing to exercise its jurisdiction despite the third core requirement not being satisfied.[348]

3.84 As for how to proper understand the exceptional circumstance, the court made some explanation later in *re China Medical Technologies Inc*.[349] The debtor incorporated in the British Virgin Islands was the ultimate holding company of a group, through which it held three indirectly wholly-owned Hong Kong subsidiaries. Its principal business, involving manufacture of surgical and medical equipment, was located in the Mainland. There were three subsidiaries in the Mainland, which were held by the aforementioned three Hong Kong subsidiaries.[350] It used to be listed in NASDAQ. The debtor did not carry on any business in the Cayman Islands or in the USA, except in the case of the latter, raising funds.[351] On 27 July 2012 the Company was wound up in the Cayman Islands. On 31 August 2012 the Company filed a bankruptcy petition in the United States Bankruptcy Court for the Southern District of New York. In order to be able to avail themselves of the investigatory powers granted to Hong Kong liquidators and make clear the Mainland subsidiaries-related fundraising process, on 26 November 2012 the debtor filed a petition for an order of its winding-up in Hong Kong.[352] On 9 April 2014, the Hong Kong court dismissed the petition because the third core requirement was not satisfied.[353]

3.85 By referring to its decision in *re Pioneer Iron and Steel,* the court stressed again that the third core requirement could not be omitted unless the connection

[343] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 36
[344] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 38
[345] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] KCFI 324, at 41.
[346] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 43.
[347] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 43.
[348] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 28
[349] *Re China Medical Technologies Inc.*, [2014] HKCFI 656
[350] *Re China Medical Technologies Inc.*, [2014] HKCFI 656, at 1, 12
[351] *Re China Medical Technologies Inc.*, [2014] HKCFI 656, at 13
[352] *Re China Medical Technologies Inc.*, [2014] HKCFI 656, at 21, 22
[353] *Re China Medical Technologies Inc.*, [2014] HKCFI 656, at 54

with Hong Kong was sufficiently strong and the benefits of a winding-up order sufficiently substantial.[354] In *re China Medical Technologies Inc.,* the court found it sufficient to satisfy the first core requirement on the basis of the presence of an office in Hong Kong and staff here, albeit leased and employed by a subsidiary, a certain amount of investor relations activities, occasional board meetings and, most significantly, the use of Hong Kong accounts for a substantial amount of its banking activity.[355] However, the court considered

"it is clear that Hong Kong was peripheral to the Company's principal activities such as research and development, manufacturing and equity and debt fund raising. In my view the court would only be justified in ordering a winding up if the third core requirement is not satisfied if the court is satisfied that Hong Kong was clearly central to the Company's principal activities and in my view it is not."[356]

3.86 Given the decisions in the recent case law, it can be briefly summarized that the presence of assets have been gradually replaced, for instance, by the location of the controlling mind, which can satisfy the first core requirement concerning sufficient connection with Hong Kong. That approach shares some similarities with the idea of central administration indicated in the decisions handed down by the CJEU.[357] The power of liquidators to undertake investigations under Cap 32 s221 can be deemed as of benefit to those filing for the winding up petition, through which the second requirement can be satisfied. The third requirement can be omitted only if the court is satisfied that Hong Kong was clearly central to the debtor's principal activities. Otherwise, the winding-up order will not be granted if one of the three core requirements has not been met.

2.3.2 Means of Recognition

2.3.2.1 Commencement of Winding up Proceeding

3.87 Recognition of foreign liquidation proceedings in Hong Kong is not governed by statutory laws. A foreign liquidator usually needs to start insolvency proceedings afresh even though insolvency proceedings are under way in another jurisdiction.[358] By doing so, a foreign liquidator is appointed pursuant to the Companies Ordinance to wind up an insolvent unregistered company, who actually does not seek recognition but indirectly attempts to achieve the effects of recognition through utilizing the reliefs available under the local insolvency regime, including collection of the assets in Hong Kong in accordance with Hong

[354] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 27
[355] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 57,58
[356] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 58
[357] Case C-341/04 *Eurofood IFSC Ltd* [2006] ECR I-03813 (*Eurofood*), para. 34; Case C-396/09 *Interedil Srl (in liquidation) v Fallimento Interedil Srl, Intesa Gestione Crediti SpA* [2011] ECR I-09915 (*Interedil*), para. 51; Case C-191/10 *Rastelli Davide e C. Snc v. Jean-Charles Hidoux* [2011] ECR I-13209 (*Rastelli*), para. 35
[358] The Law Reform Commission of Hong Kong, 1999 Report on the Winding-up Provisions of the Companies Ordinance, para. 26.24
available at: http://www.hkreform.gov.hk/en/publications/rwind.htm (Last visited on 14 June 2016)

Kong law.[359] In *Re Information Security One Ltd*,[360] the company was incorporated in the Cayman Islands and registered in Hong Kong as an oversea company. In 2006, the court in the Cayman Islands ordered the company to be wound up and appointed the liquidators. Later the liquidators filed the new liquidation petition in Hong Kong to seek the assistance of the Hong Kong court to recover assets within its jurisdiction and to invoke the procedure under section 221 for the examination of various directors.[361] The Hong Kong court wound up the company by holding that there was sufficient connection with Hong Kong for the court to exercise its discretion.[362]

3.88 With respect to possibility of opening ancillary proceeding to assist the liquidation in the company's state of incorporation, the judge in *Re Pioneer Iron* held that

…[Unless] the three core requirements had been satisfied there was no independent basis for the Court to proceed to order an ancillary liquidation.[363]

3.89 The attorney who presented on behalf of the provisional liquidators provided a number of authorities, which it was suggested to support the ancillary liquidation approach. However, the court considered that

"It does not seem to me that the fact that in a particular case it is demonstrated that viewed objectively a liquidation in Hong Kong of an unregistered company will assist a foreign liquidator in carrying out his duties is a reason for making a winding-up order if the three core requirements have not been established. In my view it would be inconsistent with the principles discussed earlier in the judgment to make an order which commenced the statutory regime for the liquidation of companies in order to enable a foreign liquidator to use that regime's investigatory procedures to obtain information about the affairs of a company, which had little connection with Hong Kong other than the presence here of one of its officers."[364]

3.90 Further, the judge made it even clearer that

"It seems to me relevant that Hong Kong has not enacted an equivalent to section 426 of the Insolvency Act 1986 and is not a signatory to the UNCITRAL Model Law on Cross-Border Insolvency, which would have enabled orders to be made for the purpose of assisting liquidators of unregistered companies investigate in Hong Kong matters concerning their affairs despite the fact that the three core requirements referred to in paragraph 27 cannot be satisfied."[365]

3.91 In short, if an unregistered company is already in liquidation in its place of incorporation, a liquidator is required to be appointed in Hong Kong to wind up the insolvent unregistered company and the winding-up proceeding in Hong

[359] See *In re Bank of Credit and Commerce International SA* (No 2) BCLC 579 and *In re B.C.C.I. SA* (No 3) (1993) BCLC 1490
[360] *Re Information Security One Ltd* [2007] HKCFI 848
[361] *Re Information Security One Ltd* [2007] HKCFI 848, at 6.
[362] *Re Information Security One Ltd* [2007] HKCFI 848, at 11.
[363] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 44
[364] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 44
[365] *Re Pioneer Iron and Steel Group Co. Ltd.* [2013] HKCFI 324, at 44

Kong is supposed to be treated as ancillary. Nevertheless, Hong Kong has not adopted the Model Law, which means there is no independent legal basis for the Hong Kong courts to open an ancillary proceeding. Accordingly, whether or not a foreign liquidator can seek assistance in Hong Kong will depend on whether or not the local jurisdiction rules (three core requirements) can be satisfied and the Hong Kong court can exercise its jurisdiction.

2.3.2.2 Civil Action

3.92 It is also possible that the effects of insolvency proceedings can be recognized by the Hong Kong Court in the process of a civil action, which involves enforcement of judgments against a debtor that is subject to insolvency proceedings abroad. According to Smart, this kind of recognition shall be subject to two-stage analysis. The distinction has to be drawn between "whether a debt has been discharged and whether the creditor can levy execution".[366] First of all, the effect of the foreign insolvency proceeding is not binding on the creditor's claim in Hong Kong because the foreign discharge does not form part of the proper law, which governs the contract and gives rise to the claim.[367] Nevertheless, in the second stage, it comes to the question of enforcing the civil judgment. To fulfill the objective of universal distribution on a comity basis, the Hong Kong court may refuse execution against such assets within Hong Kong.[368]

3.93 In the case of *CCIC Finance Ltd. v. Guangdong International Trust & Investment Corporation* (GITIC),[369] CCIC applied for a garnish order against GITIC, which was a company declared bankrupt by the Mainland court. The claim was based on a "Letter of Support" from GITIC to CCIC, which related to the loan agreement, entered into between the parties concerned and governed by the laws of Hong Kong.[370] The Hong Kong Court considered the debt was due and allowed judgment to be entered against GITIC.[371]

3.94 With respect to enforcement, the court turned to determine whether the Mainland insolvency proceeding had extra-territorial effect. The court consulted four expert witnesses from the Mainland, who provided their differing expert opinions to the court on this issue.[372] The HK court held that

[366] Smart, Recognition of Japanese Reorganization Proceedings, in: International Corporate Rescue, Vol. 1, issue 4, 2004, p. 187
[367] Smart, Recognition of Japanese Reorganization Proceedings, in: International Corporate Rescue, Vol. 1, issue 4, 2004, p. 186, 187
[368] Smart, Recognition of Japanese Reorganization Proceedings, in: International Corporate Rescue, Vol. 1, issue 4, 2004, p.188
[369] *CCIC Finance Ltd. v. Guangdong International Trust & Investment Corporation* (GITIC), [2005] 2 HKC 589
[370] *CCIC Finance Ltd. v. Guangdong International Trust & Investment Corporation* (GITIC), [2005] 2 HKC 589, at 12
[371] *CCIC Finance Ltd. v. Guangdong International Trust & Investment Corporation* (GITIC), [2005] 2 HKC 589, at 47
[372] *CCIC Finance Ltd. v. Guangdong International Trust & Investment Corporation* (GITIC), [2005] 2 HKC 589, Shi Jingxia at 67; Wang Xinxin at 83; Zou Hailia, at 75; Wang Weiguo at 76

"It seems clear to me that whatever has been decided before and whatever may happen in the future, the GITIC liquidation is being pursued, without challenge, on the basis of a universal collection and distribution of assets and that the paramount principle of *pari passu* of distribution is strictly being adhered to."[373]

3.95 Hence, the court refused to allow CCIC's application for a garnishee order attaching the debtor's assets in Hong Kong, although this approach was considered unconvincing since it was not until 2007, the enactment of the new EBL, becomes the bankruptcy law of the Mainland universal in scope in outbound transactions.[374]

3.96 Later in *Hong Kong Institute of Education (HKIE) v. Aoki Corporation,*[375] HKIE, a Hong Kong company, filed a petition of enforcement of an arbitral award against a Japanese company (Aoki), which had completed the civil rehabilitation proceeding ordered by the Japanese court. Aoki alleged,

"The enforcement of the Award would be repugnant to the fair and equitable debt restructuring scheme ['the Scheme'] in force [in relation to Aoki under the civil rehabilitation proceeding in Japan, the jurisdiction where Aoki was incorporated".[376]

3.97 HKIE contended that HKIE was never invited to register its claim against Aoki in the Japanese civil rehabilitation proceedings and that it did not take part in the same.[377] After considering the authorities and academic commentaries, the court also adopted the 2-stage analysis.[378] Firstly, the court held that judgment would be entered in HKIE's favor since Japanese law could not discharge a Hong Kong debt.[379] Secondly, the court did not allow HKIE to proceed immediately to execution and further emphasized that

"Comity does not mean blind recognition of any corporate restructuring proceeding in any jurisdiction whatsoever, however bizarre or oppressive the result. … It is necessary to assess whether the foreign proceedings are on balance fair and equitable in all the circumstances. There would be an onus on the debtor to satisfy the Court that the Scheme approved by the foreign court was reasonable and just and was obtained through due process."[380]

3.98 There is risk that the creditors may be able to enforce the debts owed to them in Hong Kong if the debts are considered discharged in the foreign proceedings but not recognized as having that effect in Hong Kong. To convince the Hong Kong courts, further evidences have to be submitted, in which the foreign proceedings should be proved reasonably and justly conducted through

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373 *CCIC Finance Ltd. v. Guangdong International Trust & Investment Corporation* (GITIC), [2005] 2 HKC 589, at 84

374 See Booth, Charles D., the 2006 P.R.C. Enterprise Bankruptcy Law: The Wait is Finally Over, in: 20 Singapore Academy of Law Special Issue 275, 2008, p 311-312.

375 *Hong Kong Institute of Education v. Aoki Corporation* [2004] 2 HKC 397

376 *Hong Kong Institute of Education v. Aoki Corporation*, [2004] 2 HKC 397, at 108

377 *Hong Kong Institute of Education v. Aoki Corporation* [2004] 2 HKC 397, at 120

378 *Hong Kong Institute of Education v. Aoki Corporation* [2004] 2 HKC 397, at 123-124, 160

379 *Hong Kong Institute of Education v. Aoki Corporation* [2004] 2 HKC 397, at 159

380 *Hong Kong Institute of Education v. Aoki Corporation* [2004] HKCFI 33; [2004] 2 HKLRD 760; [2004] 2 HKC 397; HCCT109/2003, at 149, 151

due process. Therefore, it can be concluded that recognition in the course of civil action is not a direct way of cooperation with the foreign insolvency proceedings but an alternative solution in order to prevent enforcement actions brought by individual creditor on local assets.

2.3.2.3 Sanction of Schemes of Arrangement

3.99 In accordance with s. 673(2) Cap 622, the power to sanction an arrangement or compromise is conferred upon the Hong Kong courts. In UK, this power has been utilized by some companies, which have no clear links to the UK but would like to restructure their business through scheme of arrangement instead of a formal insolvency proceeding. Pursuant to the recent case law, the connection between the UK courts and those foreign companies can be established either by COMI relocation[381] or by incorporating choice of law and choice of jurisdiction clauses into the underlying agreement.[382]

3.100 That kind of restructure strategy also becomes workable in Hong Kong since 10 December 2014, when the High Court of HKSAR handed down its decision on sanction of scheme of arrangements of LDK group. [383] As aforementioned, LDK is a photovoltaic products manufacturer based in the Mainland. In order to raise funds for its business and get access to the international capital market, LDK started to build up its offshore presence oversea. In 2006, LDK Solar, as the holding company of a group of companies, was incorporated in the Cayman Islands. In 2009, LDK Silicon, as a direct wholly-owned subsidiary of LDK Solar, was also incorporated in the Cayman Islands. In 2010, LDK Silicon Holding, as a direct wholly-owned subsidiary of LDK Silicon, was incorporated in Hong Kong.[384] As aforementioned, owing to global recession of the photovoltaic market, the three aforementioned offshore companies filed petition for winding-up, LDK Solar was ordered in provisional liquidation by the Grand Court of the Cayman Islands on 27 February 2014.[385] There were three schemes, two of which were connected to LDK Solar and LDK Silicon respectively and approved by the Grand Court of the Cayman Islands.[386] The third one related to LDK Silicon Holding, which was sanctioned by the Hong Kong Court.[387] All of them sought sanction before the Hong Kong Court. Considering that LDK Solar and LDK Silicon were incorporated in the Cayman Islands, one of the creditors raised the question of the jurisdiction of the Hong Kong court to sanction schemes of arrangement in respect of foreign companies.[388]

[381] *Re Zlomrex International Finance SA* [2013] EWHC 4605 (Ch), at 13
[382] *Re Apcoa Parking (UK) Ltd and others* [2014] EWHC 997 (Ch), at 39
[383] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234
[384] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 5-10
[385] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2235, at 17
[386] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 2
[387] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 2
[388] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 25

3.101 The Hong Kong Court firstly considered that it was vested with broad jurisdiction to wind up any unregistered company in accordance with Cap 32 S. 327.[389] Secondly, the Hong Kong Court acknowledged that

"Like the jurisdiction to wind up a foreign company which has been said to be an exorbitant power, the jurisdiction of the Hong Kong court to sanction a scheme of arrangement in relation to a foreign company ought also to be exercised only where there is sufficient justification for the Hong Kong court to do so."[390]

3.102 Further, the Court identified the different criteria between the jurisdiction to wind up a company and the jurisdiction to sanction a scheme of arrangement.[391] The Court indicated that the justification for exercising the power of sanctioning a scheme should not be governed by exactly the same requirements regulating the exercise of the power of winding up.[392] By referring to English common law,[393] the Court held that only the first core requirement had to be fulfilled in the case of sanctioning a scheme of arrangement, which is, there is a sufficient connection of the scheme with Hong Kong.[394] In addition, the Court referred to the UK High Court's decision in r*e Apcoa Parking Holdings,*[395]holding that the claims of the creditors are all or partly governed by Hong Kong Law and thus sufficient connection was established with Hong Kong.[396] Moreover, the Court regarded the Hong Kong schemes as "part of a multi-jurisdictional restructuring exercise",[397] holding

"the Hong Kong schemes form part of a larger cross-border restructuring that includes the Cayman schemes and an application to the United States Bankruptcy Court for recognition of certain aspects of the Cayman scheme in respect of LDK Solar. The Hong Kong schemes and the Cayman schemes are materially identical and inter-conditional in the sense that each takes effect only if the others are sanctioned and become effective. As such they constitute a unitary restructuring exercise. It seems to me that, in these circumstances, in sanctioning the Hong Kong schemes, comity would be fostered and not thwarted."[398]

3.103 The LDK case is a typical example of the trans-regional company, which is structured into the onshore operations and the offshore operations separately. The onshore part consists of principal business mainly located in the Mainland side, whereas the offshore part is usually composed of headquarter established in the haven jurisdictions, such as Cayman Islands, operations in North America and Europe in order to gain access to international capital markets to finance the company's activities. Due to the special tax arrangement, the Mainland has

[389] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 36
[390] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 39
[391] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 36
[392] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 41
[393] *Re Drax Holdings Ltd* [2004] 1 BCLC 10, at 25; *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 43
[394] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 44
[395] *Re Apcoa Parking Holdings GmbH* [2014] 2 BCLC 285, at 19
[396] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 55,56
[397] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 63
[398] *Re LDK Solar Co. Ltd.* [2014] HKCFI 2234, at 62

granted Hong Kong more preferential tax rate than it did to other countries.[399] Hence, Hong Kong is always chosen as an intermediate place of incorporation in order to connect onshore operations with the offshore operations for more preferential tax rate, which can always be deemed as a sufficient connection. The *re LDK Solar* decision enables the liquidators from the offshore jurisdictions to avail of the Hong Kong scheme of arrangement regime, which provides much more flexible jurisdiction criteria than formal insolvency proceedings and in fact further broadens the extent of the jurisdiction power of the Hong Kong Court.

2.3.3 Cooperation and Communication

3.104 By referring to case law in other common law jurisdiction, Hong Kong is the only region among the four that utilizes protocols and video-conference to conduct coordination and communication in practice.

2.3.3.1 Protocol

3.105 If a company does no business in Hong Kong, it pays no tax in the territory on income derived from outside Hong Kong.[400] Although Hong Kong is not perceived to be an international tax haven, it has the de facto effect. Therefore, many companies that are based in Hong Kong are incorporated elsewhere and Hong Kong is also an ideal jurisdiction for holding companies since an HK-registered holding headquarters may accumulate tax-free profits gained by its subsidiaries outside Hong Kong. Against that background, it still took decades for the CO to be reformed in Hong Kong and the cross-border insolvency is not yet included in the reform agenda. Without a statutory framework, how to cope up with the ever-growing cross-border insolvency issues? In practice, the protocols are utilized by the Hong Kong court in the absence of an international treaties or legislation on cross-border insolvency, which is indeed the "judicial innovation". In most of the cases the protocols deal with coordination of concurrent insolvency proceedings in the place of incorporation (usually offshore companies in Bermuda, BVI etc.) and in Hong Kong[401] as well as group companies whose subsidiary is operating business in Hong Kong.[402] It can be concluded from those cases that the protocols should be consistent with comity without infringing on the jurisdictions of each court. Due to lack of statutory rules, the protocols should enable the liquidators to administer both liquidations in the most economical way, reducing the conflicts and complications that may arise in cross-border insolvency matters. As summarized in *Re Jinro,* the objectives of the protocols mainly focus on:

[399] Daljit, Kaur and Susarla, Kamesh, Anti-Tax Avoidance Developments in Selected Asian Jurisdictions, Asia-Pacific Tax Bulletin, Volume 17, No 4, 2011, p.261
[400] Hong Kong Economic and Trade Office, Tax Regime and Regulations, http://www.hongkong-eu.net/pg.php?id_menu=88 (Last visited on 14 June 2016)
[401] *Re Peregrine Investments Holdings Ltd.* [1998] HKCFI 643, *Greater Beijing First Expressways Ltd.* [2000] HKCFI 755, *Re Kong Wah Holdings Ltd.* [2000] HKCFI 21, *Re Akai Holdings Ltd.* [2004] HKCFI 346
[402] *Re Jinro (HK) International Ltd.* [2003] HKCFI 239

" A. harmonizing and coordinating the proceedings in Hong Kong and in other jurisdictions if required;

B. ensuring the orderly and efficient administration of proceedings in the above jurisdictions;
C. identifying, preserving and maximizing the value of the debtor's worldwide assets for the collective benefit of the creditors and other interested parties, wherever located;
D. sharing of information and to minimize duplication of effort and costs;
E. complying with the laws of Hong Kong and foreign jurisdictions, and to satisfy the statutory and professional obligations of foreign representatives"[403]

2.3.3.2 Applicability of Video-conference

3.106 In *Re Chow Kam Fai David,*[404] the debtor was required to attend the hearing of the bankruptcy petition to be cross-examined on his affidavit. The debtor applied to the court to be permitted to be cross-examined using video conference facilities (VCF). The court of the first instance considered that the giving of evidence by VCF was an exception rather than the rule and that it would be a matter of privilege accorded to the respondent and not a matter of right for him to be allowed to do so.[405] This approach was supported by the court of appeal, which further indicated that

"There is no doubt that VCF is a highly useful tool. It must be a question of judgment in each case as to whether VCF should be used for the taking of evidence. No doubt, on those occasions when the witness is giving evidence that is technical or purely factual, without important issues as to credibility, a court may be more disposed to allow evidence to be given by the use VCF. Questions of cost and convenience are no doubt also important considerations that the court will have to weigh in deciding whether to allow evidence to be given using VCF. But, first and foremost, it seems to me that the judge was correct in his approach that a party wishing to give evidence using VCF should establish a sound reason why that privilege should be accorded."[406]

3.107 The court held that the cross-examination of the respondent using VCF would be inappropriate in this case because both the court of the first instance and the court of appeal casted doubts in the honesty of the debtor, which can be told clearly from his avoidance of his contractual and legal obligations.[407] Moreover, the reason that the debtor applied for using VCF is because the debtor might be subject to arrest in Hong Kong for failure to observe the earlier order requiring his attendance for examination.[408] The court of appeal also indicated that the decision of the judge in this respect was clearly an exercise of his discretion. However, the facts of the *Re Chow Kam Fai David* case are rather extreme. It is suggested that in other cases, for example where a director is prepared to be examined by video-conference but not to come to Hong Kong, the discretion may well be exercised differently based on all the relevant

[403] *Re Jinro (HK) International Ltd.* [2003] HKCFI 239, para.32
[404] *Re Chow Kam Fai David* [2004] HKCA 111
[405] *Re Chow Kam Fai David* [2004] HKCA 111, at 16
[406] *Re Chow Kam Fai David* [2004] HKCA 111, at 19
[407] *Re Chow Kam Fai David* [2004] HKCA 111, at 25
[408] *Re Chow Kam Fai David* [2004] HKCA 111, at 21

circumstances.[409] Therefore, it is possible that the HK court applies video-conference to communication in the course of cross-border insolvency cooperation.

Ch.3 Macao Cross-border Insolvency System

3.108 Due to its territoriality approach, the cross-border insolvency system is hardly established in Macao. This chapter will mainly focus on the exclusive jurisdiction exercised by Macao courts over foreign insolvency proceedings and its possible influences on practice.

3.1 Brief Introduction into Local Insolvency System

3.109 According to the latest statistics released, from 2000 to 2014, the Court of First Instance of Macao accepted 88 insolvency cases in total,[410] whereas the annual total of the winding-up orders made by the Hong Kong court in 2014 alone reached 271.[411] It is evident that insolvency cases in Macao relatively rarely happen.

3.110 One of the reasons is the insolvency law is a bit outdated. Insolvency law of Macao is incorporated into the Civil Procedure Code of Macao (CPCM), which is enacted in 1999. As mentioned in the Part I, Macao's legal system is deeply influenced by Portugal, which is based upon the tradition of European Civil Law countries. Although the CPCM has been recodified due to Macao's reunification with P.R.C., the legacy of Portuguese laws still remains in the current code.[412] Even after the current CPCM came into effect, the Macao court still substantially referred to the 1961 Civil Procedure Code of Portugal in handling insolvency cases.[413]

3.111 Both companies and natural persons are governed by the CPCM. Commercial enterprises, which are companies or whoever commit commercial activities,[414] shall be regulated by the rules of bankruptcy in accordance with the CPCM.[415] Debtors, who are not commercial enterprises and not able to pay the debts when they fall due, can be declared insolvent and regulated pursuant to relevant rules under the CPCM.[416] Corporate insolvency proceedings in Macao

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[409] Kwan, Susan (ed.-in-Chief), Company Law in Hong Kong – Insolvency, Sweet & Maxwell, 2012, p. 559

[410] Data collected from http://www.court.gov.mo/zh/subpage/statisticstjb?report=2013 (Last visited on 14 June 2016)

[411] Data collected from http://www.oro.gov.hk/cgi-bin/oro/stat.cgi?stat_type=W&start_year=2009&start_month=1&end_year=2014&end_month=12&Search=Search (Last visited on 14 June 2016)

[412] Feng Wenzhuang, Brief Introduction into the Compositions of Macao Civil Proceedings (in Chinese), in: http://www.dsaj.gov.mo/macaolaw/cn/data/prespectiva/issued/VASCO.pdf (Last visited on 14 June 2016)

[413] Case No.84/2001, see: http://www.court.gov.mo/tools/attachment/1385027673kxmur.pdf (Last visited on 14 June 2016)

[414] Commercial Code of Macao, article 1

[415] CPCM, article 1043 - 1184

[416] CPCM, article 1185 - 1198

are described as "cumbersome, inflexible, and time-consuming."[417] In particular, lack of pre-liquidation asset protection under Macao's insolvency system has been condemned,[418] which can also explain the scarcity of insolvency cases there.

3.2 Current Cross-border Insolvency Law in Macao

3.2.1 Exclusive Jurisdiction

3.112 There is no cross-border insolvency provision provided in the CPCM. In accordance with the Article 20 of the CPCM, the Macao courts shall have exclusive jurisdiction over the lawsuits concerning the bankruptcy or insolvency of legal persons, whose domicile is within Macao.[419] In accordance with Commercial Code of Macao, the domicile of companies shall be established in a determined place,[420] which should be registered in accordance with the Commercial Registration Code of Macao.[421] Moreover, companies with their registered office in Macao cannot avoid the application of the provisions of Commercial Code of Macao against the third parties by relying on the fact that they do not have their main administration here.[422] Therefore, it seems that the registered office is a decisive factor to the domicile of Macao companies. Foreign insolvency proceedings will not have effects in Macao, unless the foreign judgment is recognized according to the relevant rules.[423] With respect to affirmative requirements for recognition of civil judgments from outside Macao, it is stated under the Article 1200-I of the CPCM that

" 3. The court which rendered the judgment shall exercise jurisdiction over the case without fraud and the judgment does not fall into the ambit of the exclusive jurisdiction of Macao court."

3.113 In short, the territorial approach of Macao in matter of cross-border insolvency is quite self-explanatory. More importantly, even if foreign insolvency proceedings are recognized, they will only be able to affect the debtors' assets in Macao, after the claims of all Macao creditors, whose debt has its origin in Macao, have been satisfied.[424]

3.2.2 Treatment of Priority under the Commercial Code of Macao

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[417] Sue Kendall, Winding Up Macanese Companies in Macau-The Zhu Kuan Experience Brings Positive Development, Out of Court, Autumn 2004, p.3

[418] Pace, Vincent A., The Bankruptcy of the Zhu Kuan Group: A Case Study of Cross-border Insolvency Litigation against a Chinese State-owned Enterprise, 27 U. Pa. J. Int'l L. 517, 2006, p.565

[419] CPCM, article 20

[420] Commercial Code of Macao, article 181

[421] Commercial Registration Code of Macao, article 5

[422] Commercial Code of Macao, article 175-II

[423] CPCM, article 1199

[424] Garcia, Augusto Teixeira, Macao Insolvency Law and Cross-border Insolvency Issues, New Zealand Association for Comparative Law: hors série (Wellington) Vol. XIX, 2015, p. 341

3.114 It is stated under the Article 83 (Liability for obligations contracted outside Macao) of the Commercial Code of Macao that

" 1. The assets of a foreign company, which are possessed by the representative office in Macao, are only liable for the debts abroad after all the debts incurred by operating business in Macao are paid off.

2. A decision of a foreign authority that orders a foreign company bankrupt shall only be binding on the assets mentioned in the previous paragraph after the payment obligation therein has been observed."[425]

3.115 With respect to distribution of the local assets of a foreign company, according to the Article 83 of the Commercial Code of Macao that the local claims in Macao have priority over the foreign claims. In addition, if a foreign company is declared bankrupt by the court at its place of incorporation, the decision can be recognized but will not be enforced until the local debts have been paid off through the local assets. Besides, in accordance with the article 739 of the Civil Code of Macao, the local fines[426] and tax claim[427] are ranked as the first priority. Moreover, it is stipulated under the Decree of Labor Relations in Macao that in case of bankruptcy or judicial liquidation of assets, the employees as a creditor has priority over other creditors.[428]

3.3 Development in Practice

3.116 The insolvency proceeding in Macao is hardly fully reported and the relevant information is released mostly through the judgments of other jurisdictions.

3.3.1 *Re Zhu Kuan* case

3.117 In *Re Zhu Kuan* case, Zhu Kuan Group (ZKG) was incorporated in Macao since 1988. Zhu Kuan (Hong Kong) Company Limited (ZKHK) was incorporated in Hong Kong on 19 May 1992. They were both established as "window companies" for the commercial activities of the Zhuhai Municipal Government ("ZMG") of the People's Republic of China ("the P.R.C."). In 2004, the companies were declared winding-up and the liquidators were appointed in each proceeding. To restructure the companies, the Hong Kong liquidator in the Hong Kong proceedings and the Macao liquidator have worked closely in the way that the Hong Kong scheme of arrangement for the ZKG or application was to be followed in Macao.[429] Regardless of Macao's exclusive jurisdiction provision on insolvency, there is possibility that cross-border cooperation can still be voluntarily achieved between the liquidators.

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[425] For the official text of the Commercial Code of Macao (in Chinese) please visit http://bo.io.gov.mo/bo/i/99/31/codcomcn/codcom0001.asp#l1t1 (Last visited on 14 June 2016)

[426] Macao Rules of Court Litigation Fees, article 102

[427] Macao Civil Code, article 739 (a)

[428] Decree of Labor Relations in Macao, Decree-Law nº 24/89/M, 3 April 1989 (With amendments introduced by the Decree-Law nº 32/90/M, 9 July 1990), article 32

[429] *Re Zhu Kuan (Hong Kong) Co Ltd.* [2007] HKCFI 1119, para.1,4,5,12

3.3.2 *Central Steel Macao* Case

3.118 Being a free trade port with roughly 27 square kilometers territory, Macao continues to implement its low taxation policy, which is guaranteed by the Basic Law,[430] and attempts to become a haven of offshore commercial activities.[431] There is a case involving Central Steel (Macao Commercial Offshore) Limited (hereinafter, Central Steel Macao) that was incorporated in Macao. It was an indirect wholly owned subsidiary of China Metal Recycling (Holdings) Limited (hereinafter, China Metal) incorporated in the Cayman Islands and registered under s.333 of the repealed Companies Ordinance (Cap. 32) as a non-Hong Kong company, which has numerous subsidiaries in other jurisdictions including the Mainland and Macao.

3.119 In 2013, the Securities and Futures Commission of HKSAR (hereinafter the SFC) filed a petition for the compulsory winding up of China Metal to Hong Kong High Court in light of the evidence of fraud and dishonesty on the part of its senior management, in particular the existence of records of fictitious transactions, forged documents, and round robin of funds.[432] As the sourcing arm of the group for the acquisition of scrap metal from international markets for its operation in the Mainland, Central Steel Macao, as alleged by the SFC, was "at the center of a fraudulent scheme".[433] Upon the request of a winding-up order by the SFC, Hong Kong High Court appointed two joint provisional liquidators for China Metal, who were also appointed as directors of Central Steel Macao on the same day in order to gain access to and taking control of the subsidiary.[434] It seems that the same approach of appointing directors has been adopted to address the regional cross-border insolvency issues between Hong Kong SAR and Macao SAR. (Please refer to section 1.3 for the disadvantages of such arrangements.)

3.120 Macao's insolvency caseload stays at a very stable low level. Restricted by its territorial approach, Macao's cross-border insolvency system is a relatively closed system and lack of interactivity with other jurisdiction, although there might be possibility of cooperation in some individual case. With respect to distribution on local assets, the local creditors will be treated with priority over foreign ones. Moreover, owing to employee protection and the superior ranks of certain local compulsory claims, foreign creditors probably will not have high expectation for the local assets. When the development of Macao's offshore activities is on the rise but the cross-border insolvency law does not make any progress, Macao can also become a forum that can be avoided, in particular on

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[430] Basic Law of Macao SAR, article 106

[431] Although there exists taxation of income in Macao, the level of taxation is significantly lower than that of industrialized Western countries. Macao makes active efforts to attract foreign investment, namely through the Macao Investment Promotion Board. There is special procedure for investors to obtain permanent residence in Macao and a special regime for offshore industrial and financial activities. See Godinho, Jorge A.F., Macao Business Law and Legal System, in: LexisNexis Hong Kong, 2006, p18-20.

[432] *Re China Metal Recycling (Holdings) Ltd.* [2014] HKCFI 2404, paras.1, 2, 11

[433] *Re China Metal Recycling (Holdings) Ltd*. [2015] HKCFI 332, paras.9, 10

[434] *China Metal Recycling (Holdings) Ltd. and Another v. Chun Chi Wai and Others* [2013] HKCFI 1305, para.7

regional level, by replacing the directors or management personnel in the local subsidiary.

Ch.4 Taiwan Cross-border Insolvency System

3.121 The current Bankruptcy Act of Taiwan (TBA) is decades old. That's why the insolvency system in Taiwan is undergoing reform. In this section, the revised draft of the Debt Clearance Act (the 2015 Draft), in particular, its new chapter concerning cross-border insolvency, is introduced. It further discusses the development of the current cross-border insolvency by referring to the case law. Due to the territorial approach adopted by the current TBA, discussion mainly covers the topic of jurisdiction and recognition. It will be demonstrated in this section that the opinions of Taiwan courts with respect to the effect of foreign insolvency proceedings vary and different criteria of recognition have been applied in practice. In the end, the possible influences of parallel recognition rules of civil judgments to the Mainland and SARs on trans-regional insolvency proceedings will be examined.

4.1 Brief Introduction into Local Insolvency System

3.122 The current Bankruptcy Act of Taiwan (hereinafter TBA) was enacted in 1935. It applies to both legal persons and natural persons[435] with the exception of the financial institutions.[436] Pursuant to TBA, there are two types of proceedings, one of which is reconciliation and the other is liquidation.[437] Reorganization is stipulated separately under Taiwan Corporate Act (hereinafter the TCA).[438] In accordance with TCA, the corporates, which issue stocks or corporate bonds with possibility of revival, can apply to the court for reorganization.[439] Although insolvent natural persons may also use TBA to resolve their indebtedness, it has been seldom employed owing to its out-of-date provisions. After breakout of credit card debt crisis, in 2008 the Taiwan Consumer Debt Clearance Act came into effect (TCDCA). TCDCA aims at assisting debtors in restructuring their debts and maintaining their basic living standard in a more efficient way.[440] Nevertheless, none of the aforementioned laws, except for the article 4 under TBA, have anything to do with cross-border insolvency.

4.2 A New Chapter of Cross-border Insolvency under the 2015 Draft

3.123 Some new ideas concerning cross-border insolvency sprouted up in 2007 when the Judicial Yuan issued a draft of the new bankruptcy law (also in a new name, Debt Clearance Act). The draft integrated three types of proceedings,

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435 TBA, article 3

436 The ways of resolution of the Taiwanese financial institutions are scattered in relevant laws and regulations, such as Insurance Act, Insurance Deposit Act, Banking Act, Financial Institutions Merger Act, Financial Holding Company Act and etc.

437 TBA, Ch. II & Ch. III,

438 TCA, article 282 - 314

439 TCA, article 282

440 TCDCA, article 1; see also Shyuu, Shu-Huan, Basic Structures of Debt Clearance Law (in Chinese), Taiwan: Yuanzhao Press, 2007, p 18.

reconciliation, liquidation and reorganization. It also provided a specialized chapter in handling the cross-border insolvency. In February 2014, the Judicial Yuan released a revised draft of the Debt Clearance Act (the 2014 Draft) for public consultation. Under the 2014 Draft, Chapter VI is entitled Recognition of Debt Clearance Proceedings Rendered by the Foreign Courts. It is composed of 23 provisions, which covers key aspects of the cross-border insolvency, including jurisdiction, recognition criteria, the effect of the foreign proceedings, the applicable law and the duty of cooperation. On 2 June 2015, the Judicial Yuan approved the 2014 Draft, which will soon be moved forward into legislative process.[441] On 15 June, 2015, the Judicial Yuan published the approved draft (the 2015 Draft). The approved 2015 Draft will be used as basic reference in this dissertation.

4.2.1 Venue and International Jurisdiction

3.124 The 2015 Draft designates a specialized court exclusively to adjudicate recognition of foreign debt clearance proceedings in Taiwan, which is the Taipei District Court.[442] Besides, a debt clearance proceeding comes under the venue of the Taiwan's court exclusively situated at the domicile of the debtor. If the debtor's head office or principal place of business is located abroad, the place where to adjudicate the debt clearance proceedings is its head office or principal place of business in Taiwan.[443] In other words, the courts of foreign countries, within the territory of which the head office or principal place of business of the debtor is located, shall have jurisdiction to commence the foreign debt clearance proceedings. Recognition of such foreign debt clearance proceedings shall not preclude opening of the parallel debt clearance proceedings in Taiwan, [444] where the local head office or local principal place of business of the debtor is situated. Besides, if the forum to adjudicate the debt clearance proceedings within Taiwan cannot be ascertained based on the aforementioned factors, the proper venue for opening the local debt clearance proceedings shall be the place where the debtor's principal assets is situated.

4.2.2 Recognition: Restrictions and Effects

3.125 Recognition is granted on a reciprocal basis under the 2015 Draft[445] and the court can refuse to recognize the foreign proceedings if

1. in accordance with the laws of Taiwan, the foreign courts do not have jurisdiction;
2. the interests of the domestic creditors are inappropriately impaired in the foreign proceeding;
3. recognition of the foreign proceeding is on contrary to the public policy or *boni*

[441] Please visit: http://jirs.judicial.gov.tw/GNNWS/NNWSS002.asp?id=192147 (Last visited on 14 June 2016)
[442] The 2015 Draft, article 297(1)
[443] The 2015 Draft, article 7(2)
[444] The 2015 Draft, article 315(1)
[445] The 2015 Draft, article 299(2): if the foreign country where the debt clearance proceeding is opened does not recognize the debt clearance opened by Taiwan courts, the courts may dismiss the application by issuing a ruling.

mores[446]

3.126 Moreover, after the Taiwan courts commence the debt clearance proceedings, the foreign debt clearance proceedings, upon which recognition has been granted, can be stayed.[447] In addition, the 2015 Draft also provides the conditions, upon which the courts can withdraw the recognition of the foreign debt clearance proceedings:

1. the foreign debt clearance proceeding falls in the ambit of Article 299;
2. the foreign debt clearance proceeding has been terminated or rescinded;
3. the documents submitted by the liquidator in accordance with Article 298-I and Article 300-I are forged, altered or involving other fraudulent behaviors.
4. the liquidators, administrator or debtors seriously violate the statutory obligations.[448]

3.127 If there are debt clearance proceedings against the same debtor pending before the Taiwan's court, the recognition of foreign debt clearance proceedings should be ceased unless recognition will be more beneficial to the local creditors in Taiwan.[449]

3.128 Except as otherwise provided, the effect of recognition dates back to the opening of debt clearance proceedings ordered by foreign courts.[450] Once recognized, the foreign debt clearance proceedings shall have effect on the assets of the debtor or interested party within Taiwan.[451] To dispose of, distribute and transfer the debtor's assets located within Taiwan, the petitions should be filed to the Taiwan court for approval.[452] The court shall refuse to grant approval if the petitions can inappropriately impair the interests of the local creditors.[453] In addition, in order to ensure the *pari passu* distribution among the creditors, the hotchpot rules have been introduced into the 2015 Draft. It is required that the creditors, who have in the course of foreign debt clearance proceedings, obtained a dividend on their claims shall share distributions made in the Taiwan proceeding only where creditors of the same ranking obtained an equivalent distribution.[454] Moreover, it is also stipulated that if creditors, who will in the course of foreign debt clearance proceedings, obtain dividends on their claim, shall take distributions made in the Taiwan proceeding only where creditors of the same ranking have obtained an equivalent distribution or they can provide appropriate guarantee. If the guarantee cannot be provided, their distributions shall be held in escrow.[455]

4.2.3 Applicable Law

[446] The 2015 Draft, article 299
[447] The 2015 Draft, article 315(2)
[448] The 2015 Draft, article 310
[449] The 2015 Draft, article 314(1)
[450] The 2015 Draft, article 309(1)
[451] The 2015 Draft, article 304(1)
[452] The 2015 Draft, article 305(1)
[453] The 2015 Draft, article 305(3)
[454] The 2015 Draft, article 318(1)
[455] The 2015 Draft, article 318(2)

3.129 With respect to the rules of applicable law, except as otherwise provided in this chapter, the law applicable to foreign debt clearance proceedings, once recognized, and their effects, shall be that of the foreign country within the territory of which such proceedings are opened (*lex concursus*).[456] There are also certain exceptions to *lex concursus*, mainly including employment contract, right of offset and right of avoidance. Despite the effects of foreign debt clearance proceedings, the law applicable to the employment contract shall be that of Taiwan if it is more beneficial to the employees.[457] The law applicable to right of offset, which can only be initiated upon the commencement of the debt clearance proceedings and shall not be interfered by the opening of the foreign debt clearance proceedings, shall be the law governing the contract.[458] The law applicable to right of avoidance shall be that of the foreign country where the debt clearance proceedings are opened unless it is proved that the law originally governing the contract forbids the avoidance.[459]

4.2.4 Duty of Cooperation

3.130 The 2015 Draft provides some general rules concerning the duty of the domestic and foreign liquidators or administrators to cooperate with each other. The liquidators or administrators appointed in the Taiwan debt clearance proceedings can request the foreign liquidators or administrators for necessary cooperation and information as well as provide the foreign liquidators or administrators with necessary cooperation and information.[460] Further, it is stated that Chapter VI of the 2015 Draft shall apply mutatis mutandis to recognition of debt clearance proceedings opened in the Mainland China, Hong Kong and Macao.[461]

3.131 In summary, the 2015 Draft provides a relatively comprehensive cross-border insolvency regime. Nevertheless, several limitations have been set on recognition criteria of foreign insolvency proceedings. Protection of interests of the local creditors is emphasized, in particular, which may have impact on the stay of recognition, approval of disposal of local assets and applicable law to the employment contract. Moreover, it is also observed that Taiwan tends to apply uniform rules in matters of recognition of cross-border insolvency proceedings regardless of its place of origin among China, Hong Kong, Macao and other foreign countries, which is a different approach from recognition of civil and commercial judgments.

4.3 Current Cross-border Insolvency Law in Taiwan

4.3.1 Jurisdiction

[456] The 2015 Draft, article 304(2)
[457] The 2015 Draft, article 306
[458] The 2015 Draft, article 307
[459] The 2015 Draft, article 308
[460] The 2015 Draft, article 317(1)
[461] The 2015 Draft, article 319

3.132 There are no specific rules concerning international insolvency jurisdiction under TBA. In practice, some courts refer to the doctrine of *forum non conveniens*. In the case of *Chinatrust Commercial Bank (CTCB) v. Richard S. & Lehman Brothers Treasury Co., B.V.*, the plaintiff filed a damage claim against the defendants on the ground of their infringing acts by intentionally concealing important information and unjustified enrichment therefrom.[462] This case was lodged as a civil claim but indeed originated from Lehman Brother's global insolvency proceedings. As stated in the arguments of the defendants (Richard S. & Lehman Brothers Treasury Co., B.V.) in the first instance, in 26 January 2010 CTCB withdrew the lawsuit against Lehman Brothers Holdings Inc. because it feared that its claim would be eliminated from the creditor list by the courts which opened the insolvency proceeding of Lehman Brothers Holdings Inc. if its individual actions continued. Instead, CTCB filed a petition against Lehman Brothers Treasury Co., B.V., which is a subsidiary of Lehman Brothers Holdings Inc., by referring to the theory of reverse piercing the corporate veil.[463] The case went through three levels of adjudication and was treated as ordinary civil petition and concentrated on how to determine the *locus delicti*.[464] Nevertheless, on an international scenario, if a creditor is still allowed to take individual enforcement actions against a foreign debtor's assets in the local court after opening of a foreign proceeding, it will be inconsistent with the principle of *pari passu* among the creditors and jeopardize the collective insolvency regime.

3.133 First Commercial Bank lodged a damage petition against Lehman Brothers Treasury Co., B.V. in 2010 as well. The lower court applied the doctrine of *forum non conveniens* and dismissed the application of the plaintiff. Later the High Court approved the decision of the lower court and dismissed the appeal. In deciding whether or not the court has jurisdiction on this dispute, it held

"… The appellant purchased and paid for the bonds outside Taiwan. Even if the respondent shall undertake the tort liability, *locus delicti* is not situated in Taiwan. In accordance with the Article 15 of Code of Civil Procedure, our court does not have jurisdiction on this dispute. … In addition, the respondent argued that pursuant to Dutch insolvency law, once the debtor is declared bankrupt, all the compulsory execution and attachment on the debtor's assets as well as the lawsuits filed against the debtor should be stayed. In the bankruptcy proceeding, all the unsecured creditors can only submit their claims to the liquidator, instead of initiating separate actions. … The appellant argued that the bankruptcy proceeding of the respondent was already opened on 8 October 2008 in the Netherlands. If our court makes decision on this dispute, it will be difficult to be recognized by the Dutch court. Consequently, the goal of the litigation cannot be met. "[465] (translated by author)

3.134 Later in 2012, the Supreme Court reversed the ruling rendered by the High Court, holding

[462] Taiwan Taipei District Court Litigation No. 1807 [2010]
[463] Taiwan Taipei District Court Litigation No. 1807 [2010]
[464] Taiwan High Court Appeal from Ruling No.215 [2011]; Taiwan Supreme Court Appeal from Ruling No. 1022 [2011]
[465] Taiwan High Court Appeal from Ruling No.286 [2012]

"… [I]t has been proved that the finance of Lehman Brothers are highly integrated, who took advantage of establishment of different entities in order to separate the responsibilities. The affiliated companies were set up and exploited as tools, which helped to evade or hide the responsibilities and make profits by issuing bonds. The respondent, together with Lehman Brother International (Europe), Lehman Brothers Holdings Inc. and Lehman Brothers Commercial Corporation Asia Limited shall take the joint liability for the damages … In addition, … the loss of the appellant occurred within Taiwan. … The High Court did not make investigation on the appellant's aforementioned arguments but considered that Taiwan did not have jurisdiction on this dispute. The ruling is questionable. …"[466] (translated by author)

3.135 By referring to the respondent's argument, the High Court seemed to be aware of the effects of foreign insolvency proceedings on the local civil lawsuit. Nevertheless, the Supreme Court again regarded this dispute as an ordinary civil case and thus assumed Taiwan's jurisdiction over this case without taking into consideration the existing bankruptcy proceeding commenced abroad.

4.3.2 Recognition

4.3.2.1 Statutory Limitation on the Effects of Foreign Proceedings

3.136 It is stipulated under the Article 4 of TBA that

"If reconciliation or declaration of bankruptcy is rendered in a foreign country, it shall have no binding effect on the assets of the debtor or the bankrupt, which are located in Taiwan."[467]

3.137 It is self-explanatory that Article 4 abides by the principle of territoriality in matters of cross-border insolvency. It was further explained by the Taiwan Supreme Court in its decision handed down in 1996 that in accordance with Article 4 of TBA, reconciliation or declaration of bankruptcy is rendered in a foreign country shall have no binding effect on the assets of the debtor within Taiwan. On the basis of reciprocity, the foreign courts can also refuse to recognize the effect of a Taiwanese bankruptcy order on the assets situated in the foreign states.[468] It is observed that the Supreme Court of Taiwan used to apply the principle of territoriality, not only to the inbound effects of the foreign bankruptcy orders in Taiwan, but also to the outbound effects of Taiwanese bankruptcy orders in the foreign states. However, if declaration of bankruptcy rendered by foreign courts shall not be recognized, a parallel proceeding or derivative claims originating from foreign bankruptcy proceeding may occur, which can result in execution of debtor's property located in Taiwan and thus damage the collectivity of insolvency proceedings.

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[466] Taiwan Supreme Court Appeal from Ruling No. 529 [2012]

[467] In the process of translation, the author has made some technical modification in wording of this article. In the original Chinese version of article 4 TBA, it is stated China instead of Taiwan. Please note that the act was enacted in 1935, i.e. before establishment of P.R.C. Nowadays, it might cause misunderstanding if China is being utilized here. In order to make clear the effective geographic extent of this article, the corresponding context is thus translated into Taiwan.

[468] Taiwan Supreme Court No. 1592 [1996]

4.3.2.2 Flexible Interpretations in Practice

3.138 Certain lower courts followed the aforementioned holdings of the Supreme Court,[469] whereas the majorities incline to interpret Article 4 in more flexible ways. Some courts adopt the optional recognition approach, considering that the limitation set up by Article 4 only applies to the assets located within Taiwan but does not preclude all effects of the foreign proceedings from being recognized. In 1999 the Taipei District Court heard a case between a company registered in Cayman Islands and a company registered in BVI. The former company was ordered winding-up in Hong Kong. The debtor filed a petition for damages due to the provisional attachment initiated by the defendant after the commencement of the HK winding-up proceeding. With respect to the effect of the winding-up order of the HK court, the court held that:

"… Although it is stated under the article 4 of TBA that "if reconciliation or declaration of bankruptcy is rendered in a foreign country, it shall have no binding effect on the assets of the debtor or the bankrupt, which are located in Taiwan", it shall be interpreted that declaration of bankruptcy has no binding effect merely on the assets located in Taiwan. Therefore, the defendant argued that the declaration of winding-up rendered by HK court had no binding effect at all in Taiwan, which is contrary to the legislative purposes of TBA and thus cannot be accepted…"[470] (translated by author)

3.139 The defendant appealed to Taiwan High Court. The Taiwan High Court agreed with the lower court and dismissed the appeal.[471]

3.140 In 2011, the Taiwan High Court recognized the power of liquidators appointed by Hong Kong High Court in Lehman Brothers insolvency proceeding (*Taipei Fubon Bank v. Lehman Brothers Commercial Corporation Asia Limited*). The court also considered that Article of TBA only excluded the effect of the foreign insolvency proceedings on the assets located within Taiwan but it does not deny the effects of all the actions done by foreign courts in foreign insolvency proceedings, especially the effect of appointment of legal agents or statutory representatives for the debtor rendered by the court. Otherwise, the debtor would not be able to participate in or respond to any suits due to lack of legal agent in Taiwan. Consequently the creditors in Taiwan will not be able to make any property reservation or compulsory execution on the assets of the debtor in Taiwan and even their claims will not be able to be recognized and thus will be disadvantaged.[472]

3.141 Generally speaking, the liquidators are appointed to administrate and coordinate the insolvency proceedings and one of their key functions is to realize all or part of the debtor's local assets, which is contrary to the purpose of Article 4. In that case, the mere recognition of the appointment of the liquidators, who will not be allowed to take any action on the local assets, is not very meaningful but only of some symbolic value.

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[469] Banqiao District Court Bankruptcy No.9 [2012]
[470] Taipei District Court International Trade No.9 [1999]
[471] Taiwan High Court International Trade Appeal No. 9 [2002]
[472] Taiwan High Court Important Appeal No. 23 [2011]

3.142 Some courts identify recognition of foreign insolvency proceedings as non-litigation lawsuit and thus apply Article 49 of the Non-litigation Law,[473] instead of Article 4 of the TBA. In 2009, the Taiwan court recognized a ruling rendered by Hong Kong High Court [In The High Court of the Hong Kong Special Administrative Companies (Winding- Up) Proceeding NO. 441 of 2008]. In accordance with article 42-I of the HK and Macao Act[474] Taipei District Court identified the case as a "non-litigation lawsuit" and thus applied Article 49 of the Non-litigation Law, holding

"… Upon investigation, the aforementioned ruling is not contrary to public policy or good morals of Taiwan. The applicant also asserted that on 2 July 1998 Hong Kong Court of Appeal recognized the insolvency ruling rendered by Taiwan Court in the case of Chen Li Hung & Another v. Ting Lei Miao & Others, 2000-1 HKC 461. By referring to Taiwan Supreme Court Appeal No. 1943 [2004], mutual recognition can be confirmed. In accordance with the relevant law, upon the request of the applicant, the application is hereby approved." [475] (translated by author)

3.143 Further, some courts held that the Article 49 of the Non-litigation Law adopted the automatic recognition approach. Accordingly, the foreign insolvency proceedings are deemed as automatically effective and thus it is not necessary for the Taiwan courts to grant recognition. In 2012, Taipei District Court handed down a decision concerning recognition of a Japanese insolvency proceeding.[476] The Japanese liquidator, referring to the judgment of Taipei District Court in the former Lehman Brothers decision (Taipei District Court Trial on Application No. 514 [2009]), applied for recognition of a reorganization ruling rendered by Tokyo District Court. Taipei District Court dismissed the application, holding:

"Except as otherwise provided by law or in pursuit of a ground for execution, the party concerned shall apply to the court in Taiwan who shall render a judgment for compulsory execution of foreign judgments. Under any other circumstances, there is no legal ground for the court to grant recognition on the effect of foreign judgments. That's why the Non-Litigation Law only lists some exceptional conditions to refuse recognition but it does not require that the foreign judgments can only be deemed as effective after the Taiwan courts grant recognition. Therefore, it is inconsistent with the article 49 of Non-litigation Law that the applicant applied for recognition of reorganization proceeding ordered by Tokyo District Court."[477] (translated by author)

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[473] Non-litigation Law, article 49: a final and binding judgment rendered by a foreign court shall be recognized, except in case of any of the following circumstances: 1. Where the foreign court lacks jurisdiction pursuant to the laws of Taiwan; 2. The interested parties, who are citizens of Taiwan, assert that documents or notices of opening of the proceedings have not been served to them and therefore they are not able to exercise their rights; 3. Where the performance ordered by such judgment or its litigation procedure is contrary to public policy or morals of Taiwan; 4. Where there exists no mutual recognition between the foreign country and Taiwan, except that the foreign judgment does not have adverse effect on Taiwan.

[474] In accordance with article 42-I of HK and Macao Act, in determining the conditions for the validity, jurisdiction, and enforceability of civil judgments made in Hong Kong or Macao, Article 402 of the Code of Civil Procedure and Article 4, Paragraph 1 of the Compulsory Execution Law shall apply mutatis mutandis.

[475] Taipei District Court Trial on Application No. 514 [2009]

[476] Taipei District Court Trial on Application No. 355 [2012]

[477] Taipei District Court Trial on Application No. 355 [2012]

3.144 As for relevance of its former judgment, Taipei District Court pointed out that in the case of Taipei District Court Trial on Application No. 514 [2009], it was a case related to Hong Kong and accordingly recognition was rendered on the basis of Article 42 of the HK and Macao Act, which thus did not apply to the Japanese insolvency proceeding.[478] As aforementioned in para.2.73, Taiwan applies parallel recognition rules of civil judgments to the Mainland and SARs. Since Article 42 of the HK and Macao Act is regarded as proper legal basis for recognition of Hong Kong insolvency proceedings, the corresponding legal basis for recognition of the Mainland insolvency proceedings shall be Article 74 of the Mainland Act. In accordance with the interpretation the Taiwan Supreme Court concerning Article 74 of the Mainland Act, the civil ruling or judgment rendered in the Mainland do not have *res judicata* in Taiwan and therefore should be subject to substantial review when applying for recognition.[479] Consequently, the differential criteria adopted by Taiwan to recognize civil judgments rendered by the Mainland and SARs will be extended to the insolvency proceedings under the current Taiwan's legal system.

4.3.2.3 Possible Influences of Parallel Recognition Rules

3.145 Multi-layered recognition systems concerning cross-border insolvency are not something unique. In UK where the insolvent has interests in a country that is outside the EU, the CBIR implementing the UNCITRAL Model Law should be used to seek the cooperation of the foreign courts. If the insolvent has interests in a Member State of the European Union (EU), the provisions of the EC Regulation on Insolvency Proceedings prevail in UK. As for some designated countries, most of which are Commonwealth countries, s426 of the English Insolvency Act 1986 will take precedence. The common law is also applied alongside the CBIR and sometimes also s426 as alternative grounds for relief. The reason why UK adopted such an intricate system for cross-border insolvency is more complicated. It is promoted by development of international insolvency law, influenced by EU legal integration as well as its own legal tradition and political heritages. What's more, it is also expected that the same rules will be applied to recognition of insolvency proceedings in accordance with the 2015 Draft,[480] which will solve the problem in the near future.

3.146 However, Taiwan's parallel recognition rules of civil judgments to the Mainland and SARs will still evoke problems of *pari passu* treatment among the creditors from different regions. For instance, it is provided under the Enterprise Bankruptcy Law of P.R.C. that

" Where the debtor or creditor has objections to what is recorded in the form of claims, he may file an action with the people's court that has accepted the application for bankruptcy."[481]

[478] Taipei District Court Trial on Application No. 355 [2012]
[479] Taiwan Supreme Court Appeal No. 2376 (2008)
[480] The 2015 Draft, article 319
[481] The EBL, article 58

3.147 That means the debt owed to some creditors in the Mainland insolvency proceeding shall be affirmed by the people's court either by a ruling or by a judgment. If the debtor is declared bankrupt in Taiwan and the creditors want to participate in the Taiwan bankruptcy proceeding, they will have to report their claims to the liquidator of Taiwan proceeding.[482] In order to prove their claims to Taiwan liquidator, they should submit the Mainland ruling or judgment for confirmation. The creditors from the Mainland have to apply for recognition to Taiwan court with the possibility that the court might refuse to recognize them since those rulings or judgments are rendered in the Mainland and thus not automatically recognized. The creditors from the Hong Kong, Macao or foreign proceedings, however, may not have the same problem because their rulings or judgments will be automatically recognized (see para.3.160 of Part III).

Conclusion

3.149 The cross-border insolvency systems in the four regions have different characteristics and each of them has their own problem. The national insolvency system in the Mainland has developed synchronously with its economic reform. Insolvencies of state-owned and non-state-owned companies were not treated in a uniform manner because the state-owned enterprises used to be the main form of economic entities and those insolvency proceedings were directly interfered by the government. In 2006, the current EBL was adopted, covering all types of incorporated enterprises. Although the former bankruptcy law still has some influence on the 2006 EBL, it lays emphasis on corporate rescue by introducing reorganization proceedings.

3.150 Nevertheless, with more advanced arrangements under the current EBL, the amount of insolvency cases declines on an annual basis. One of the reasons is existence of the competing system - participation in distribution system. It provides a leeway from ordinary insolvency proceedings, because assets distributed through the participation in distribution system are irrevocable, which undermines the principle of collectivity, one of the fundamental principles of the insolvency law. Involvement of government is also a very important factor that has influence on implementation of the current EBL. Although there are obvious advantages of government involvement in the insolvency proceedings, it is required by the market-oriented economy to reconsider the relationship between the local governments and the local enterprises and the means of their involvement, which cannot touch the bottom line of the independence of the courts in the insolvency proceedings. Thirdly, it is observed that the actual function of the courts in practice has been limited and restrained. The tentative solution to the problems is to establish specialized tribunals for bankruptcy cases.

3.151 The current EBL provides one article (article 5) that deals with cross-border insolvency issues. The first provision governs the effects of China's insolvency proceedings, which are vested with outbound universal effect and inbound territorial effect. The second provision stipulates the criteria of

[482] TBA, article 65

recognition, which is composed of the key elements, including the international treaties, the principle of reciprocity and the reservation of public policy. In practice, for the countries, which have mutual civil and commercial judicial assistance treaties or agreements, it is more likely that the effects of the insolvency proceedings in those countries can be recognized in the Mainland. Besides, the Chinese courts still hold quite restrictive reciprocity standards in rendering recognition of foreign civil and commercial judgments. As for the reservation of public policy, it has been incorporated in article 5(2) EBL in the form of diverse expressions, such as fundamental principles of law, state sovereignty and security, socio-public interests as well as legitimate rights and interests of the creditors, which can cause considerable hurdles of proper understanding in practice. The current EBL does not provide clear explanation with respect to those various expressions regarding public policy. Although some relevant civil and commercial case law has been found for reference, its reference value is limited because cross-border insolvency law has its own features and needs interpretation peculiar to its own characters and a comprehensive understanding of public policy in the context of cross-border insolvency is still missing.

3.152 Meanwhile, the insufficient rules on cross-border insolvency law discourage filings of recognition and enforcement of the foreign and regional insolvency proceedings before the Mainland courts at the same time. On international level, the Mainland jurisdiction has been intentionally avoided due to lack of confidence in its insolvency system and uncertainty of its cross-border insolvency legislations. On regional level, the absence of regional cross-border insolvency arrangements resulted in invention of substitutes based on company law, i.e. appointment of provisional liquidator or liquidator as member of the management or representative of the Mainland subsidiaries. Nevertheless, as an indispensible part of the winding-up order, such a solution can bring complexity to the proceedings owing to the dual identities of the liquidators and delay the process because of the resistance of the former members. Moreover, the solution, as an indispensible part of effects of the parallel proceedings, which do not automatically have effect in the Mainland, is merely an evasion of the genuine problem.

3.153 In Hong Kong SAR, individual bankruptcy and corporate winding-up proceedings are governed by separate ordinances. The personal insolvency is regulated under the Bankruptcy Ordinance, whereas the Companies Ordinance sets rules on corporate winding-up. Although the Companies Ordinance has experienced revision, it did not change anything related to corporate insolvency. In July 2014, Legislative Council Panel on Financial Affairs issued Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure, which recommended the regime of provisional supervision similar to voluntary administration in the UK and Australia. Hong Kong still held a wait-and-see attitude towards the reform of its cross-border insolvency law. Although the UNCITRAL Model Law was published nearly two decades and over 20 countries and regions have adopted the Model Law as part of their domestic laws, concerns have been expressed about the possibility of synchronous development in the neighboring

jurisdictions, in particular, the Mainland. Thus, evolvement of Hong Kong's statutory cross-border insolvency system is still pending.

3.154 The current Hong Kong cross-border insolvency law is greatly influenced by common law practice. Despite the legal basis provided under Cap 32 s.327, the case law has set up three core criteria to determine jurisdiction of the Hong Kong courts over non-Hong Kong companies. Given the decisions in the recent case law, it can be briefly summarized that the presence of assets have been gradually replaced, for instance, by the location of the controlling mind, which can satisfy the first core requirement concerning sufficient connection with Hong Kong. The power of liquidators to undertake investigations under Cap 32 s221 can be deemed as of benefit to those filing for the winding up petition, through which the second requirement can be satisfied. The third requirement can be omitted only if the court is satisfied that Hong Kong was clearly central to the debtor's principal activities. Otherwise, the winding-up order will not be granted if one of the three core requirements has not been met. In Hong Kong, jurisdiction also plays an important role in recognition of foreign insolvency proceedings. There is no independent legal basis for the Hong Kong courts to open an ancillary proceeding. To seek assistance of the Hong Kong courts, a foreign liquidator usually needs to start insolvency proceedings afresh even though insolvency proceedings are under way in another jurisdiction. However, the purpose of seeking assistance alone does not suffice to be granted a winding-up order if three core requirements have not been satisfied.

3.155 The effects of insolvency proceedings can also be recognized by the Hong Kong Court in the process of the civil action, which is subject to two-stage analysis. First of all, the foreign insolvency proceeding is not deemed effective in Hong Kong because the foreign discharge does not form part of the proper law, which governs the contract and gives rise to the claim. Nevertheless, on the second stage, it comes to the question of enforcing the civil judgment. To fulfill the objective of universal distribution on a comity basis, the Hong Kong court may refuse execution against such assets within Hong Kong. However, there is still risk that after passing the first-stage analysis, the effects of the foreign proceedings are still not recognized in Hong Kong. It is required to submit further evidences to prove that the foreign proceedings were reasonably and justly conducted through due process. Therefore, it can be concluded that recognition in the course of civil action is not a direct way of cooperation with the foreign insolvency proceeding but a factor to be determined in execution of the civil judgment.

3.156 The third means to seek recognition in Hong Kong is to utilize the power of the courts to sanction scheme of arrangement as stipulated under Cap 622 s. 673(2). In the case of sanctioning a scheme of arrangement, only the first core requirement is needed to exercise jurisdiction. By referring to the UK High Court's decision, the Hong Kong court held that the claims of the creditors are all or partly governed by Hong Kong Law and thus sufficient connection was established with Hong Kong. As part of a multi-jurisdictional restructuring scheme, sanction of Hong Kong scheme of arrangements will enable Hong Kong to participate in the global unitary restructuring exercise on a comity basis. With

respect to cooperation and coordination, video-conference may also be taken into consideration in matters of communication and coordination of concurrent insolvency proceedings. In Hong Kong it is possible that assistance can be provided in the form of protocols without infringing on the jurisdictions of each court. Video-conference may also be taken into consideration in matters of communication and coordination of concurrent insolvency proceedings.

3.157 Macao's insolvency caseload stays at a very stable low level. By adopting exclusive jurisdiction over insolvency proceedings of a company, Macao follows a territorialism approach in handling cross-border insolvency cases, which gives rise to interactivity with other jurisdiction. With respect to distribution on local assets, the local creditors will be treated with priority over foreign ones. Moreover, owing to employee protection and the superior ranks of certain local compulsory claims, foreign creditors probably will not have high expectation for the local assets, although there might be possibility of cooperation in some individual case. When the development of Macao's offshore activities is on the rise but the cross-border insolvency law does not make any progress, Macao can also become a forum that can be avoided, in particular on regional level, by replacing the directors or management personnel in the local subsidiary.

3.158 In June 2015, the Judicial Yuan of Taiwan issued the approved draft of the Debt Clearance Act (the 2015 Draft) in order to conduct reform on the current decade-old Bankruptcy Act. The 2015 Draft provides one new chapter concerning cross-border insolvency, which is a relatively comprehensive cross-border insolvency regime, including rules of jurisdiction, recognition criteria, applicable laws and duty of cooperation. Nevertheless, several limitations have been set on recognition criteria of foreign insolvency proceedings. Protection of interests of the local creditors is emphasized, in particular, which may have impact on the stay of recognition, approval of disposal of local assets and applicable law to the employment contract. There are also some general rules concerning the duty of the domestic and foreign liquidators or administrators to cooperate with each other. Moreover, it is observed that Taiwan tends to apply uniform rules in matters of recognition of cross-border insolvency proceedings regardless of its place of origin among China, Hong Kong, Macao and other foreign countries, which is a different approach from recognition of civil and commercial judgments.

3.159 There are no specific rules concerning international insolvency jurisdiction under the current TBA. Therefore, the relevant provisions under Code of Civil Procedure are applied by analogy in dealing with the jurisdiction issues. Accordingly in practice, the Taiwanese court tended to regard the cross-border insolvency cases as ordinary civil cases and thus assumed Taiwan's jurisdiction over this case without taking into consideration the existing bankruptcy proceeding commenced abroad. In addition, the current TBA (article 4) set limitation on the foreign insolvency proceedings, which shall have no binding effect on the assets of the debtor within Taiwan. The majorities of the courts opt to interpret the limitation in more flexible ways. Some courts adopt the optional recognition approach, considering that the limitation only applies to the assets located within Taiwan but does not preclude all effects of the foreign

proceedings, such as appointment of liquidators, from being recognized. Generally speaking, the liquidators are appointed to administrate and coordinate the insolvency proceedings and one of their key functions is to realize all or part of the debtor's local assets, which is contrary to the purpose of article 4. In that case, the mere recognition of the appointment of the liquidators, who will not be allowed to take any action on the local assets, is not very meaningful but only of some symbolic value.

3.160 Some courts identify recognition of foreign insolvency proceedings as non-litigation lawsuit and thus apply article 49 of the Non-litigation Law, instead of article 4 of the TBA. Further, some courts held that the article 49 of the Non-litigation Law adopted the automatic recognition approach. Accordingly, the foreign, including Hong Kong and Macao, insolvency proceedings are deemed as automatically effective and thus it is not necessary for the Taiwan courts to grant recognition. However, as aforementioned in Part I, recognition of the Mainland judgments was granted on a different basis, which provides that judgment rendered in the Mainland do not have *res judicata* in Taiwan and therefore should be subject to substantial review when applying for recognition. Consequently, the differential criteria adopted by Taiwan to recognize civil judgments rendered by the Mainland and SARs will be extended to the insolvency proceedings under the current Taiwan's legal system. It is expected that the problem will be solved in the near future if the 2015 Draft is passed by the Legislative Yuan, which contains the uniform recognition criteria on cross-border insolvency proceedings regardless of its place of origins. Nevertheless, Taiwan's parallel recognition rules of civil judgments to the Mainland and SARs will still evoke problems of *pari passu* treatment among the creditors from different regions.

3.161 For a sovereign state that has gone through reunification, to harmonize legal conflicts thereof is something inevitable in the process of further integration. Meanwhile, driven by economic interaction, legal cooperation also has to be carried out between the Mainland China and Taiwan. Considering the special political composition and diverse cross-border insolvency systems among the four regions, the most urgent issues are concerning how to achieve efficient recognition by overcoming the jurisdiction hurdles and promote coordination of the concurrent insolvency proceedings opened in the four regions.