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Offshore Courts and the Emerging Role of COMI in Recognition

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In recent years, offshore financial centers have been at the forefront of the development of the courts' common law powers to recognize and assist foreign insolvency proceedings. As these are jurisdictions that generally have limited (or no) statutory recognition regimes, it is not surprising that common law power continues to play an important role.

One of the more interesting questions concerns the basis upon which foreign officeholders are entitled to recognition. The longstanding traditional view was that only a foreign proceeding in the jurisdiction of the company's incorporation could be recognized. This approach is now being challenged, and a familiar term is being used to justify an alternative basis for recognition: center of main interests (COMI). Explicitly borrowed from the UNCITRAL Model Law, the COMI concept has the potential to revolutionize common law recognition by moving beyond the 19th century approach and allowing courts to respond flexibly, pragmatically and commercially to the issues raised in modern cross-border proceedings. This article discusses two recent Cayman Islands cases that exemplify this trend — *In re China Agrotech*[1] and *In re Changgang Dunxin*[2] — and places them in context as the latest judicial proclamations on COMI's emerging role in common law recognition.

In re China Agrotech: Nontraditional Recognition

China Agrotech was a Cayman-incorporated company traded on the Hong Kong Stock Exchange (SEHK). It encountered financial distress, and the SEHK suspended share trading. A creditor presented a winding-up petition against the company to the Hong Kong court, which made a winding-up order and appointed liquidators. The liquidators devised a restructuring proposal that required implementation through parallel schemes of arrangement in Hong Kong and the Cayman Islands. They asked the Hong Kong court to issue a letter to the Cayman court requesting permission for the Hong Kong liquidators to promote a Cayman scheme of arrangement in the name of China Agrotech, then made an application to the Cayman court on that basis.

The Hong Kong liquidators asked the Cayman court to recognize them as having authority to act for the company in Cayman. The statutory regime for recognition of foreign insolvency proceedings was not applicable because the liquidators were appointed outside the company's jurisdiction of incorporation. The request therefore raised two important issues. First, did the Cayman court have the power at common law to recognize and assist a foreign liquidator appointed in a jurisdiction other than where the company was incorporated? Second, if the power did exist, should it be exercised in these circumstances? The court answered both questions affirmatively.

On the first issue, the court began by considering the nature of the common law power to recognize and assist foreign insolvency courts and officeholders by reference to the Privy Council's seminal decision in *Singularis Holdings Ltd. v. PricewaterhouseCoopers*.[3] In *Singularis*, a case on appeal from Bermuda, the Privy Council affirmed the existence, and sketched out the purposes and limitations around the exercise, of the power. In particular, the board stressed that the power can only be exercised to overcome the territorial limits of the foreign court's jurisdiction and consistently with the domestic procedural and substantive law of the court granting the assistance. The former limitation restricts assistance to relief that the foreign liquidator could have obtained in its home jurisdiction. The latter limitation precludes the assisting court from extending a purely domestic insolvency statutory remedy as if the statute applied to the foreign proceeding.

The *China Agrotech* court then considered the nature of the common law power in light of the request by the Hong Kong liquidators to promote a Cayman scheme of arrangement. Under the Companies Law, the company itself has the right to make an application to the court to convene a meeting of creditors or shareholders to whom a scheme is proposed.[4] Accordingly, the court reasoned that the Hong Kong liquidators could make that application on behalf of the company if it were either (1) entitled to act under general private international law principles or (2) could be recognized using the common law power.[5] While private international law rules did not assist,[6] the court concluded that

1 2017 (2) CILR 526.
2 Grand Ct, 1 March 2018, unreported.
3 [2014] UKPC 36.
4 Section 86(1).
5 *China Agrotech* at ¶ 28.
6 *Id.* at ¶ 29. Cayman private international law rules recognize that the law of a company's jurisdiction of incorporation (the *lex incorporationis*) governs the question of who is empowered to act on the company's behalf.

the common law power could be used to recognize a foreign liquidator appointed outside the jurisdiction of incorporation.[7] The court specifically found that even though the jurisdiction of incorporation can play a special role in giving effect to a universal succession of company assets, the common law power of recognition can have a wider application than the traditional private international law rule. It is the nature of the common law power itself — informed in modern times by the principle of modified universalism — that permits its use to recognize an officeholder from the non-incorporation jurisdiction.

On the second issue – whether the common law power should be used to recognize the Hong Kong liquidators – the court cited various factors that it believed justified the exercise of the court's discretion to grant recognition. Those factors include the lack of competing creditor claims whose recovery would vary depending on whether the relief was granted, evidence that the directors of China Agrotech were unable or unwilling to act, the likelihood that no one with standing would bring a winding-up petition in Cayman, China Agrotech's "substantial contacts" with Hong Kong, the lack of need for or reason why stakeholders would benefit from a parallel liquidation in Cayman, and the lack of any "local reputational, regulatory and policy reasons requiring a local proceeding."[8]

As a final point on the basis for recognition, the court noted that China Agrotech's COMI was "probably in Hong Kong."[9] It considered that factor "to be a consideration of considerable weight to be taken into account when deciding whether the foreign, non-place of incorporation liquidation should be treated as competent and justifying assistance," although not a determinative one.[10] The court ultimately authorized the Hong Kong liquidators to act in the company's name to promote the intended scheme of arrangement in Cayman.

In re Changgang Dunxin: China Agrotech, Redux

Heard by another Grand Court judge less than four months after the *China Agrotech* judgment was handed down, the decision in *Changgang* presented a very similar fact pattern. The company, incorporated in the Cayman Islands, was listed on the SEHK and carried out its business operations from Hong Kong. Trading of its shares was suspended. A Hong Kong-based creditor presented a winding-up petition against the company to the Hong Kong court, which appointed provisional liquidators to preserve the company's assets. The Hong Kong liquidators received various restructuring proposals and identified a transaction to monetize the company's SEHK listing as the most viable.

Based on advice from their Hong Kong counsel that provisional liquidators could not exercise restructuring powers in that jurisdiction, the provisional liquidators applied to the Cayman court for recognition of their right to act in the name and on behalf of the company so they could bring a winding-up petition, then immediately seek appointment as provisional liquidators in Cayman. Following their anticipated appointment in Cayman, it was intended to adjourn the Hong Kong provisional liquidation and promote parallel schemes of arrangement in both jurisdictions in order to effect the restructuring proposal.

The core of the relief sought by the Hong Kong liquidators, recognition of the right to act for the company in Cayman, was essentially the same as in *China Agrotech*. The court cited many of the same authorities referred to in the *China Agrotech* case and the judgment itself, emphasizing the latter's analysis on COMI's role as "extremely helpful."[11] The judge ultimately cited three factors as justifying the recognition and assistance sought by the Hong Kong liquidators: (1) The two jurisdictions were not competing to be the principal liquidation; (2) the foreign liquidators were proceeding with the support of the Hong Kong court; and (3) the company's COMI was in Hong Kong. On the COMI issue, the court added that it would be consistent with comity to recognize liquidators appointed in a jurisdiction with which the company had substantial ties.[12]

A Common Law COMI Test

In one sense, *China Agrotech* and *Changgang* are simply curiosities — two *ex parte* decisions springing from an understandable desire by first-instance judges to facilitate practical commercial outcomes in odd factual circumstances. However, both judgments add to a growing body of case law on the recognition of foreign insolvency proceedings from outside the jurisdiction of incorporation that posit some form of COMI test as a valid basis for that recognition. Various levels of support for the idea of a common law COMI test can be found in judgments from England, Bermuda and Singapore.

Lord Leonard Hoffmann's speech in the U.K. House of Lords decision in *In re HIH Casualty and General Insurance Ltd.*[13] appears to be the root of the common law COMI test. Speaking *obiter dicta*, Lord Hoffmann observed that the seat of the principal liquidation would usually be the jurisdiction where the company was incorporated but opined that the concept of COMI "may be more appropriate."[14]

In re Dickson Group Holdings Ltd.[15] is a Bermuda case strikingly similar to *China Agrotech*. The Hong Kong liquidators of a company incorporated in Bermuda caused the company to apply to the Bermuda court to convene a meeting to consider a scheme of arrangement. A request for recognition of the foreign liquidators was implicit in the application. The court granted the application, noting that the assumptions underpinning the COMI concept embedded in the UNCITRAL Model Law "are hardly anathema to Bermudian common law"[16] and that the company's principal place of business and majority of assets were in Hong Kong.[17]

The Singapore court wholeheartedly embraced the common law COMI concept in circumstances involving

7 *Id.* at ¶ 30(a).
8 *Id.* at ¶ 30(f).
9 *Id.* at ¶ 30(g). The court used COMI in the same sense as defined in the UNICTRAL Model Law.
10 *Id.*
11 *Changgang* at ¶ 29.
12 *Id.* at ¶ 30.
13 [2008] 1 WLR 852.
14 *Id.* at ¶ 31.
15 [2008] SC (Bda) 37 Com.
16 *Dickson* at ¶ 23.
17 *Id.* at ¶ 36.

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three jurisdictions. In *In re Opti-Medix Ltd.*,[18] a Japanese bankruptcy trustee appointed over a British Virgin Islands company applied for recognition and assistance in Singapore to take control of local bank accounts. The company had carried on its main business in Japan. The court agreed with Lord Hoffmann's statement in *HIH Casualty* that COMI was a basis for common law recognition, rejected the suggestion that the common law could not develop along those lines, and opined that a common law COMI test should, like the statutory version, include a presumption in favor of the registered office in the absence of evidence to the contrary.[19]

Even in a competition between officeholders from the incorporation jurisdiction and the COMI jurisdiction, the door for a common law COMI has been left open. For example, *In re Founding Partners*[20] involved a Cayman company, Cayman liquidators and a U.S. federal equity receiver. Both the liquidators and receiver sought recognition in Bermuda to take possession of assets there. The case ultimately turned on the characterization of the U.S. receivership, the court determining that it was not an insolvency proceeding capable of displacing the Cayman liquidation as the main proceeding.[21] However, the court did leave open the possibility that if the U.S. proceeding was a bankruptcy, a COMI analysis might be appropriate to determine the competition.[22]

18 [2016] SGHC 108.
19 *Opti-Medix* at ¶¶ 19, 22, 25.
20 [2011] SC (Bda) 19 Com.
21 *Id.* at ¶ 45-48. In making this determination, the court had regard to the definition of foreign proceeding under, and allowed that the common law power should be informed by, the UNICTRAL Model Law.
22 *Id.* at ¶ 49.

Conclusion

Admittedly, it is still in the early days for the widespread acceptance of a common law COMI test for recognition, and there are outstanding questions to be addressed in its execution. Should the common law include a presumption in favor of the registered office? When would it be appropriate for a COMI officeholder to have priority over a local liquidator? Should there be a difference in the approach between a restructuring proceeding and a liquidation proceeding? What public policy concerns would mandate a local parallel proceeding? Ultimately, these issues will have to be worked out through academic discussion, further first-instance testing of the concept and hopefully the direct weighing in by an appeals court.

However, where statutory remedies fall flat, the guidance that has been laid down by courts in key offshore jurisdictions bodes well for providing opportunities for creative uses of common law recognition to avoid incurring the incremental time, expense and loss-of-control risk inherent in full-blown parallel proceedings. Advisors on restructuring or insolvency proceedings that involve offshore companies, claims or assets can take advantage of these new developments while remaining cognizant of the limitations and obstacles in relying on common law recognition and assistance. Whether recognition requirements are identified and planned for at the outset, or simply in reaction to new information during the course of a proceeding, the COMI's emerging role as a basis for recognition can unlock remedies and avenues not otherwise available and provide new ways for onshore and offshore professionals and courts to cooperate and coordinate. abi