

Insights

THE HONG KONG APPROACH WHERE DEBTORS LODGE A PETITION FOR THEIR OWN BANKRUPTCY – HOW TO PREVENT ABUSE OF PROCESS

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SUMMARY

If a person presents a petition for their own bankruptcy (“**self-petition**”), are there any safeguards to ensure that the self-petition is genuine, as opposed to a cynical device by the person to buy themselves time to pay, or to give themselves some negotiating position with their creditors?

This interesting question was considered in a recent Hong Kong judgment.

On 6 December 2021, at a hearing of four debtor’s petitions (with the neutral citation [2021] HKCFI 3732), the Court dismissed each of the self-petitions on the ground that it constituted an abuse of process.

On 10 December 2021, the Court gave its reasons for judgment, and the judgment gives helpful guidance as to the likely judicial approach when dealing with self-petitions in the future.

BRIEF FACTS

The Court considered four debtor’s petitions which shared a similar fact pattern - *Re So Tsz Man* (HCB 7033/2020), *Re Lee Wing* (HCB 7299/2020), *Re Tam Wai Yiu* (HCB 7569/2020) and *Re Qiu Wenjun* (HCB 3930/2021)::-

1. Each of the debtors had presented a self-petition for their own bankruptcy on the ground that they were unable to pay their debts.
2. Prior to the hearing on 6 December 2021, numerous hearings had been scheduled before a Master. However, the debtors had failed to attend some to all of these hearings. This was despite the warning letters issued by the Court informing them that failure to attend the next hearing would result in the dismissal of the petition.

3. Each of the debtors filed numerous affirmations stating that they had been discussing debt restructuring proposals with their creditors and asked for an adjournment of the petition so as to discuss the proposals with the creditors.
4. When asked by the Court, each of the debtors confirmed that they did not want a bankruptcy order to be issued against them.
5. Each of the debtors confirmed, when quizzed by the Court, that their creditors had not pressed them to make any repayment after the presentation of the petition.
6. Upon the Court's enquiry with each of the debtors, it became apparent that they had been told by persons who allegedly have some knowledge of bankruptcy proceedings that by presenting the self-petitions, they could achieve what in effect is a moratorium with the creditors, because the creditors would not be able to require the debtors to repay the debts pending determination of the petitions.

LAW REGARDING GROUNDS FOR PRESENTING A SELF-PETITION

Section 10 of the Bankruptcy Ordinance (Cap. 6) ("**BO**") provides as follows:-

"Grounds of debtor's petition"

1. *A debtor's petition may be presented to the court only on the ground that the debtor is unable to pay his debts.*
2. *The petition shall be accompanied by a statement of the debtor's affairs containing—*
 - a. *such particulars of the debtor's creditors and of his debts and other liabilities and of his assets as may be prescribed; and*
 - b. *such other information as may be prescribed.*
3. *A debtor's petition may be presented whether or not the aggregate amount of indebtedness is equal to or exceeds the amount provided for a creditor's petition under section 6(2)(a)."*

PROCEDURAL REQUIREMENTS FOR A SELF-PETITION

The Court emphasised that presenting a self-petition is a serious matter.

When filing a debtor's petition for bankruptcy, the debtor is required to complete:-

- a. A "Debtor's Bankruptcy Petition" on Form 3 of Bankruptcy (Forms) Rules (Cap. 6B) ("**Forms Rules**"), which requires the debtor to (i) state that they "*request the court that a bankruptcy order be made against [them]*" and (ii) sign the petition in the presence of a witness.

- b. A "Statement of Affairs (Debtor's Petition)" on Form 28C of the Forms Rules, which must be verified by an affidavit.

These procedural requirements under the Forms Rules are designed to ensure that a debtor presents a petition to seek a bankruptcy order only if they (1) are unable to pay a debt and (2) genuinely wish to seek a bankruptcy order.

PURPOSE OF SECTION 10 OF THE BO

The statutory purpose of section 10 of the BO is to permit an insolvent debtor to invoke the bankruptcy jurisdiction where they are unable to pay their debts. By invoking the bankruptcy jurisdiction, however, the debtor gives up all their property in return for being freed from the burdens of their debts and, upon discharge from bankruptcy, to make a clean start.

The statutory scheme of bankruptcy is designed to avoid multiple executions and other forms of enforcement against the debtor's assets, so as to ensure that all creditors will be dealt with fairly and equitably through the bankruptcy process, and to achieve a fair and orderly distribution of the debtor's assets amongst their creditors.

COURT'S POWER TO DISMISS A BANKRUPTCY PETITION

Section 5(3) of the BO provides that the Court has a general power to dismiss or a stay a petition "*if it appears to it appropriate to do so on the grounds that there has been a contravention of rules or for any other reason*".

The Court in Re So Tsz Man indicated that the Court should dismiss a self-petition as an abuse of process if it is shown that the debtor is able to pay their debts.

COURT'S JUDGMENT

In the present case, the Court said it was clear that the debtors did not intend to seek genuinely a bankruptcy order from the Court. Instead, they used self-petitions as "*the means to suspend their obligations to make repayment of the debts and to negotiate with the creditors on the terms of repayment*".

The Court emphasised that, it is not open to a debtor to make a request for a bankruptcy order in the self-petition if they do not in fact intend to seek the order when the petition comes to be heard by the Court. If a debtor does not wish the Court to make a bankruptcy order against him, they should not present a self-petition in the first place. Further, it is not the function of a self-petition to allow a debtor to achieve a moratorium with their creditors. The debtor is free to negotiate with their creditors, and does not need to maintain a self-petition to carry on such negotiations.

The Court regarded it was an abuse of process for a debtor to present a self-petition but then to seek to postpone the determination of the petition by not attending the scheduled hearing(s) or by

asking for an adjournment for the purpose of negotiating with their creditors.

As a result, the Court in Re So Tsz Man dismissed each of the four self-petitions for being abusive of the Court's process.

COURT'S FUTURE APPROACH ON SELF-PETITIONS

The Court expressed the view that it is a matter of concern that many debtors had chosen to present a self-petition, which process comes at a not insignificant cost to the debtor, including (1) a deposit to the Official Receiver pursuant to rule 52(1)(a) of the Bankruptcy Rules (Cap. 6A) (currently at \$8,000), (2) a filing fee of \$1,045 to the Court and (3) other fees which may be charged by the agents or solicitors for assisting the debtor in the preparation and filing of the petition and the statement of affairs.

To ensure that in future debtors will not be misled by others as to the proper purpose of self-petitions, and to prevent further abuse of process, the Court (save in exceptional circumstances) is likely to adopt the following approach in dealing with self-petitions:

1. If a debtor does not attend the scheduled hearing before a Master, the Master will adjourn the petition to the Bankruptcy Judge for dismissal for want of prosecution.
2. The Court will not allow an adjournment of the petition simply on the ground that the debtor needs more time to negotiate with their creditors.
3. At the hearing before the Bankruptcy Judge, if the debtor does not attend the hearing, the petition will be dismissed for want of prosecution and/or abuse of process.
4. If the debtor attends the hearing before the Bankruptcy Judge and informs the Court that they do not wish to seek a bankruptcy order, the petition will be dismissed for abuse of process.

In all of the above scenarios, the costs of the Official Receiver will be borne by the debtor and be paid out of the deposit. The Court reminded debtors who do not wish to seek a bankruptcy order that it will be to their advantage to withdraw the self-petition at the hearing before Master so as to minimise the costs payable to the Official Receiver.

ORO'S ANNOUNCEMENT

On 10 December 2021 (the same day as the handing down of the reasons for judgment in Re So Tsz Man), the Official Receiver's Office ("**ORO**") announced an "Important Notice for Petitioner in Bankruptcy Proceedings". The ORO reminded, among others, debtors in self-petition cases and their legal representatives of their duties to ensure their bankruptcy petitions are prosecuted efficiently and expeditiously. Their duties include but are not limited to the following:-

1. attending the petition hearing and adjourned hearings (if any) at the appointed date and time;

2. communicating proactively with the court on matters regarding the petition;
3. responding in a timely way to any requisitions that may be raised by the court from time to time; and
4. proceeding with the petition efficiently and applying for adjournment only where circumstances fully justify.

The ORO further reminded potential self-petitioners and their advisers that any petitions presented that (a) are not in compliance with the relevant requirements or (b) amount to an abuse of process (e.g. the bankruptcy proceedings being invoked in an improper manner or for an improper purpose such as using it as a means for negotiation with creditors) are liable to be dismissed by the court with costs ordered against the debtors in self-petition cases.

Re So Tsz Man, together with the ORO's announcement, serve as a timely and important reminder that the self-petition is a tool which can be employed only under specific conditions. Debtors should obtain proper legal advice before presenting a self-petition to avoid dismissal of the petition and adverse costs consequences.

RELATED PRACTICE AREAS

- Restructuring & Insolvency/Special Situations
- Corporate
- Litigation & Dispute Resolution

MEET THE TEAM



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