

Legislative Council
Panel on Financial Affairs

Improvement of Corporate Insolvency Law

Purpose

This paper briefs Members on the legislative proposals to improve Hong Kong's corporate insolvency law. A copy of the consultation document on the legislative proposals, which is issued today for a three-month public consultation, is attached for Members' perusal.

The Improvement Exercise

2. On 7 November 2011, we briefed Members on the Administration's plan to roll out a legislative exercise to improve the insolvency and winding-up provisions of the Companies Ordinance (Cap 32) ("CO"). The underlying objectives of the corporate insolvent law improvement exercise are to facilitate more efficient administration of the winding-up process; and increase protection of creditors through streamlining and rationalising the company winding-up procedures and enhancing regulation of the winding-up process, having regard to international experience. An effective company winding-up process with due regard to the protection of creditors will facilitate the development of Hong Kong as a global major business centre and reinforce our position as an international financial centre.

3. In January 2012, we established an Advisory Group chaired by the Official Receiver and comprising representatives from the business sectors, relevant professions, private insolvency practitioners, the academic sector as well as members of the Standing Committee on Company Law Reform ("SCCLR") to provide technical inputs and expert advice to the Government on the legislative proposals to be included in the improvement exercise. The Advisory Group completed its work in October 2012.

4. With the benefit of expert advice by the Advisory Group, the Government has drawn up 46 legislative proposals to improve the corporate

insolvency and winding-up provisions of the CO. Reference has also been made to the relevant recommendations of the “Report on the Winding-up Provisions of the Companies Ordinance” issued by the Law Reform Commission in 1999 where appropriate. These proposals cover the following five aspects of the winding-up process, namely –

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

5. Enactment of these proposals will bring improvements to the existing corporate insolvency regime in the following ways –

- (a) **protection of creditors will be enhanced**, notably through –
 - (i) introducing new provisions for the court to make orders for restoring the position to what it would have been if a company had not entered into a “transaction at an undervalue”¹ within a specified period before commencement of its winding-up (*Proposal (A) of Chapter 5 of the consultation document*);
 - (ii) introducing standalone provisions in the CO on “unfair preferences”², so as to overcome the existing problems arising from applying the relevant provisions in the Bankruptcy Ordinance (Cap. 6) to the corporate insolvency context (*Proposal (B) of Chapter 5*);
 - (iii) modifying provisions on invalidation of floating charges³ to

¹ Transactions at an undervalue are transactions entered into by a company prior to its winding-up that involve an outright gift given by the company to a party, or entered into by the company with a party on terms that provide for the company to receive no consideration or for a consideration which is significantly less than the value of the subject of the transaction.

² Unfair preferences are transactions entered into by a company prior to its winding-up that put a particular creditor in a better position than other creditors in disregard of the priority position of preferential creditors and in breach of the *pari passu* principle of distribution amongst unsecured creditors.

³ A floating charge is a charge created over a class or classes of assets, present or future, and the subject matter of which could, in the ordinary course of the business of the company, be changing from time to time. It is contemplated that the company may carry on its ordinary course of business in respect of the class(es) of assets charged until crystallisation. For example, a charge over all the present and future book debts of a company where the company retains the ability to deal with the books debts and their proceeds freely in the ordinary course of its business.

invalidate certain floating charges created by a company in favour of persons who are connected with the company within a specified period before commencement of the winding-up of the company (*Proposal (C) of Chapter 5*);

(iv) introducing additional safeguards to reduce the risk of abuse of the special procedure as set out in section 228A of the CO which enables directors of a company to commence a voluntary winding-up (*Proposal (B) of Chapter 2*);

(b) the **winding-up process will be streamlined**, which may inter alia result in cost-savings to creditors, notably through –

(i) streamlining and rationalising the proceedings of the committee of inspection⁴ (COI), such as enabling the COI to function through written resolutions sent by post or using other electronic means (*Proposal (B) of Chapter 4*);

(ii) streamlining the process for determining the bills of costs and charges of the agents employed by the liquidators, by allowing the liquidators to seek the agreement of the COI on those bills of costs and charges (*Proposal (C) of Chapter 4*);

(iii) allowing communication by liquidators with creditors, contributories, members of COI and other interested parties by electronic means (*Proposal (D) of Chapter 4*); and

(c) the **integrity of the winding-up process will be further enhanced**, notably through –

(i) expanding the list of persons disqualified for appointment as a liquidator or a provisional liquidator to cover persons with potential conflict of interest (*Proposal (A) of Chapter 3*);

(ii) introducing a new statutory requirement for prospective liquidators and provisional liquidators to make a statement of relevant relationships before their appointment (*Proposal (B) of Chapter 3*); and

(iii) introducing provisions to the effect that liquidators would not be

⁴ A COI is a joint body formed by representatives of creditors and members of the company for supervising the liquidator, and may give directions to the liquidator in the course of winding-up the company.

absolved from liabilities arising from their misfeasance or breach of duty notwithstanding their release by the court (*Proposal (F) of Chapter 3*).

Public Consultation

6. We welcome comments on the legislative proposals to improve our corporate insolvency and winding up regime as set out in the consultation document. To encourage members of the public and relevant stakeholders to provide their views on the proposals, we will also organise a public consultation session during the public consultation period and attend briefing sessions with the SCCLR and stakeholder organisations.

Next Step

7. The three-month public consultation period will end on 15 July 2013. We will carefully study the comments received during this consultation in preparing the necessary legislation. Subject to the outcome of the consultation, the Government plans to introduce an amendment bill into the Legislative Council in 2014/15.

Financial Services and the Treasury Bureau
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