

Management of insolvency services

The Audit Commission ("Audit") conducted a review to examine the management of insolvency services by the Official Receiver's Office ("ORO") with a view to identifying areas for improvement. A related audit review on the subject was previously conducted and reported in March 2012.¹

2. Hon Paul TSE Wai-chun declared that his law firm was one of the contractors as private insolvency practitioners ("PIPs") under the outsourcing schemes of ORO.

3. ORO is responsible for providing insolvency services in Hong Kong, including the compulsory winding-up of companies and personal bankruptcy under the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) and the Bankruptcy Ordinance (Cap. 6) respectively. In 2019-2020, ORO's estimated expenditure was \$223 million, of which \$177 million (about 80%) was related to personal emoluments or personnel related expenses. According to ORO, under the outsourcing schemes, nearly all winding-up cases and about 25% of the debtor-petition summary bankruptcy cases are undertaken by PIPs.

4. The Committee noted the following findings from the Director of Audit's Report:

- from 2016-2018, the annual achievements of a 18-month time target for processing summary bankruptcy cases were below 50%, ranging from 34% to 40%;
- in March 2008, ORO commenced an exercise with a view to clearing outstanding matters of 1 200 pre-2002 insolvency cases (i.e. date of bankruptcy or winding-up order before 2002). However, as at 31 December 2019, after more than 11 years, 200 (17%) cases remained outstanding;
- as at 31 December 2019, 1 996 bankruptcy cases involving landed properties remained outstanding, including 1 565 (78%) cases with bankruptcy orders made before 2006 (i.e. over 14 years ago);
- as at 30 November 2019, ORO had placed monies recovered from 21 winding-up cases (\$4.7 million) and 207 bankruptcy cases

¹ Chapter 5 of Director of Audit's Report No. 58 - "Provision of insolvency services"

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(\$40.2 million) in the suspense accounts pending clarifications, and 8 (38%) of the 21 winding-up cases were released cases² and 29 (14%) of the 207 bankruptcy cases were released/rescinded/withdrawn cases;

- according to the Panel T scheme,³ ORO would conduct quality audits on cases allocated to PIPs. However, up to 31 January 2020, no quality audits had been conducted;
- field audits⁴ had been completed on only 3.1% and 2.7% (78% and 68% of target coverage) of the cases outsourced under the two most recently completed contracts of the Panel T scheme;
- in the period from 2016 to 2019, no warning letters had been issued to PIPs for their unsatisfactory performance even though Audit found eight incidents of PIPs failing to submit preliminary examination questionnaires within seven working days of the interview with the bankrupts. Warning letters could have been issued according to the Conditions of Contract of the tenders;
- information about liquidator's accounts and trustee's accounts outstanding from PIPs and six substantiated or partially substantiated complaints against PIPs received from 2015 to 2019 was not recorded in the registers of unsatisfactory conduct of PIPs;
- as at 31 December 2019, there were 763 liquidator's accounts and 15 355 trustee's accounts overdue but not yet submitted. Of them, 302 (40%) liquidator's accounts and 146 (1%) trustee's accounts had been overdue for more than five years. Besides issuing reminder letters, no other follow-up actions had been taken by ORO;
- the statutory corporate rescue procedure, insolvent trading provisions and the cross-border insolvency recommended by the Law Reform

² Winding-up cases that the Official Receiver had been released from the role of liquidators by the court were known as released cases.

³ Panel T scheme was an open tender system to appoint professional firms (in the accounting, legal and secretarial fields) with relevant insolvency work experience to take up appointment as provisional liquidators/liquidators in summary winding-up cases under section 194(1A) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance.

⁴ ORO staff were required to conduct field audits of the selected cases outsourced under the Panel T scheme and debtor-petition summary bankruptcy case scheme respectively as one of the measures to monitor the performance of PIPs.

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Commission of Hong Kong in 1996 and 1999 respectively, had not yet been implemented;

- the usage of individual voluntary arrangement⁵ ("IVA") as an alternative to bankruptcy as a percentage of total bankruptcy and IVA cases in the period from 2014 to 2018 was low, ranging from 6% to 8%; and
- after ORO's fee revision in 2013, ORO's cost recovery rates had fluctuated notably (ranging from 97% to 326%) and ORO could meet the full-cost target (from 95% to 105%) only in 2013-2014, 2016-2017 and 2018-2019.

5. The Committee asked for written responses regarding the administration of in-house insolvency services, monitoring of PIPs and other matters. The replies from **Secretary for Financial Services and the Treasury** and **Official Receiver** are in *Appendices 47* and *48* respectively.

6. After studying the above replies, the Committee decided to hold a short public hearing on 12 June 2020 to seek details from the Administration on the measures that had been/would be taken to address/rectify the inadequacies identified in the Audit Report. **Mr Christopher HUI Ching-yu, Secretary for Financial Services and the Treasury** and **Ms Phyllis MCKENNA, Official Receiver** made opening statements at the beginning of the Committee's short public hearing held on 12 June 2020. The full texts of the opening statements of Secretary for Financial Services and the Treasury and Official Receiver are in *Appendices 49* and *50* respectively.

7. At the short public hearing, **Secretary for Financial Services and the Treasury** and **Mr Sam HUI Chark-shum, Deputy Secretary for Financial Services and the Treasury (Financial Services)** 3 updated the Committee about the progress of the legislative procedures of statutory corporate rescue procedure and insolvent trading provisions and domestic legislation relating to cross-border insolvency. **Official Receiver** further explained the measures to handle extra winding-up and bankruptcy cases in view of economic downturn utilizing the

⁵ The Bankruptcy Ordinance provided for an IVA as an alternative to bankruptcy since April 1998. Under an IVA, a debtor made a repayment proposal to the creditors. If the repayment proposal was approved, it would legally bind all the creditors.

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Anti-epidemic Fund, clear outstanding cases, monitor case progress, provide training to employees and resources to PIPs for handling of cases and the action plan of ORO in response to Director of Audit's recommendations. The supplementary written responses provided by **Official Receiver** after the hearing are in *Appendix 51*.

8. The Committee wishes to be kept informed of the progress made in implementing the various recommendations made by Audit.