立法會
Legislative Council

LC Paper No. CB(1)1637/99-00
(These minutes have been seen by the Administration)

Ref: CB1/BC/6/99/2

Bills Committee on
Companies (Amendment) Bill 2000

Minutes of meeting
held on Tuesday, 22 February 2000, at 3:00 pm
in Conference Room A of the Legislative Council Building

Members present	**:**	Hon James TIEN Pei-chun, JP Hon Albert HO Chun-yan Hon LEE Cheuk-yan Hon Eric LI Ka-cheung, JP Hon Margaret NG Hon Ronald ARCULLI, JP Hon HUI Cheung-ching Hon CHAN Kwok-keung Hon CHAN Yuen-han Hon SIN Chung-kai Hon Mrs Miriam LAU Kin-yee, JP
Member absent	**:**	Hon HO Sai-chu, SBS, JP
Public officers attending	**:**	**Financial Services Bureau** Miss Susie HO Deputy Secretary for Financial Services Miss Julina CHAN Principal Assistant Secretary for Financial Services **Companies Registry** Mr G W E JONES Registrar of Companies

Mr John BUSH
Secretary of the Standing Committee on Company Law Reform

Official Receiver's Office

Mr E T O' CONNEL
Official Receiver (Ag)

Mr Edward LAU
Assistant Principal Solicitor

Department of Justice

Mr Geoffrey FOX
Senior Assistant Law Draftsman

Miss Shandy LIU
Senior Government Counsel

Clerk in attendance : Ms LEUNG Siu-kum
Chief Assistant Secretary (1)4

Staff in attendance : Mr KAU Kin-wah
Assistant Legal Adviser 6

Miss Irene MAN
Senior Assistant Secretary (1)9

I Election of Chairman

Mr Ronald ARCULLI was elected Chairman of the Bills Committee.

II Meeting with the Administration

(LegCo Brief Ref: FSB C2/1/12C(99) IX, LC Paper No. CB(3)423/99-00, LS58/99-00, LC Paper No.CB(1)1024/99-00(02)(03))

2. At the invitation of the Chairman, the Deputy Secretary for Financial Services (DS for FS) briefed members on the purpose and the salient aspects of the Bill. After a consultation process in 1995, the Law Reform Commission (LRC) gained positive response and support from various parties for a corporate rescue

procedure. Apart from adopting most of the recommendations made by the LRC in its report on "Corporate Rescue and Insolvent Trading" in 1996, the Administration also incorporated in the Bill a number of proposed amendments to certain sections of the Companies Ordinance (Cap. 32). DS for FS explained that on corporate rescue, Hong Kong companies that ran into financial difficulties at present would try to come to a voluntary arrangement on debt restructuring with their creditors. With the introduction of the Bill, these companies would be provided with a statutory framework under which they could carry out the corporate rescue operation. One of the two main features of the proposed statutory corporate rescue was the introduction of a moratorium during the provisional supervision i.e. the corporate rescue procedure. During the moratorium, the debtor company would be protected from creditor action for an initial period of 30 days, and thereafter extension of up to six months from the commencement of the provisional supervision could be made, subject to the court's approval. The second feature was the appointment of a provisional supervisor to take over the control of the debtor company and to formulate a voluntary arrangement proposal for the creditors' approval during the provisional supervision period.

3. DS for FS pointed out that the Bill had taken into account the interests of both the employees and creditors. A debtor company would be required to establish a trust account to settle all the outstanding wages and entitlements owed to employees before commencing provisional supervision. However, major secured creditors holding at least one third of the company's liabilities could reject the proposal of corporate rescue within three days upon receipt of notice of commencement of provisional supervision from the provisional supervisor. In that case, provisional supervision would cease and the provisional supervisor would vacate his office. On the other hand, such major secured creditors allowed the provisional supervision to proceed, the provisional supervisor would play an important role of a professional or a corporate rescue doctor. DS for FS emphasized that this arrangement would not solve all the problems of a company in financial difficulties, but would provide it with a respite as well as an opportunity to turn around, instead of going down the winding up route immediately in which case creditors might get less dividend in terms of their debts.

4. DS for FS advised that, apart from corporate rescue, the Bill also contained provisions on insolvent trading as recommended by the LRC. If a

liquidator, in the course of winding up a company, discovered that the directors or other senior management of the company still continued to trade while the company was insolvent, he could make application to the court to declare that a responsible person, i.e. a director or a member of senior management, was liable for insolvent trading.

5. DS for FS said that the Bill would also amend certain sections of the Company Ordinance (Cap. 32), including providing the Official Receiver with the authority to appoint a provisional liquidator, who would thereafter be a liquidator of the company; simplifying the filing requirements in respect of annual returns by companies; and lowering the threshold for the requisitioning of an extraordinary meeting from the present requirement of members holding not less than one-tenth of the paid-up share capital to one-twentieth.

Overseas models

6. Mr Albert HO enquired about the history and experience of overseas countries which had adopted similar corporate rescue procedures. The Official Receiver(Atg) (OR/Atg) advised that a number of jurisdictions were examined, including those of the United Kingdom (UK), Australia and the United States. The concept of moratorium was being studied in detail by UK. In Hong Kong, the LRC proposed in 1996 a statutory rescue procedure that an initial 30-day moratorium be implemented to give debtor companies a chance to turn around. The provisional supervisor, as an independent third party with specialized knowledge being respected and trusted by creditors, would have to take up the duties passed to him by the directors within seven days of the appointment and sort out with secured creditors to determine whether the company could be saved. Normally, directors and shareholders who initiated the rescue procedure would have already tried to work out a solution before the intervention of the provisional supervisor to avoid liquidation.

7. On members' enquiry about the reference of the moratorium model, OR/Atg advised that the 30-day period was unique in Hong Kong. The proceedings of Chapter 11 of the US Bankruptcy Code were similar to the moratorium; however, the directors would be still in control of the company. As such, the LRC considered the US model not appropriate for Hong Kong. The

extension of 30-day to 6-month moratorium period was based on the Canadian model.

8. As the corporate rescue model recommended by the LRC was largely based on the Australian and Canadian provisions, Mr HUI Cheung-ching requested information reflecting the effectiveness of the corporate rescue models implemented in these two countries. DS for FS undertook to provide the information.

(*Post-meeting note*: the Administration's response was circulated to members vide LC Paper No.CB(1)1074/99-00(01).)

Arrangements for employees

9. Upon the Chairman's enquiry about the consultation results on the treatment of employees' entitlements, DS for FS advised that LRC had proposed after the consultation in 1995 that the Protection of Wages on Insolvency Fund (PWIF) should be used to meet outstanding claims of those employees who were laid off by a company under provisional supervision. However, taking into account the views expressed by respondents, including both employer and employees groups, during the extensive consultation exercise held in 1998, the Financial Services Bureau came up with the present proposal that it would be a statutory responsibility of employers to clear all arrears of wages and entitlements owed to its employees before it could initiate the rescue procedure.

10. Noting that the employers had to first settle all the arrears of wages and entitlements to employees for the corporate rescue procedure, Mrs Miriam LAU considered that companies capable of doing so would not need to be rescued and expressed reservation about the extent to which the rescue procedure would be used. She enquired how the Australian model dealt with the employees' issue in view of the possible huge amount of money involved. In response, DS for FS advised that according to the banks in Hong Kong which had been involved in corporate rescues, the largest debt of companies in financial difficulties was not arrears of wages and entitlements owed to employees. Furthermore, the target companies to be rescued would be those which had viable businesses but suffered from temporary financial difficulties, and thus should be able to turn around and also have the ability to set aside the required amount of fund in the trust account for employees' benefits.

11. The Principal Assistant Secretary for Financial Services (PAS for FS) supplemented that on treatment of debts owing to employees, the Administration had studied the overseas experience, including those of the United States, Canada, Japan, Europe, Australia and Singapore. However, none of them had arrangements akin to the PWIF in Hong Kong. Based on the Administration's research, there were mainly two ways in handling employees debts owed by the company in a corporate rescue equivalent regime in these countries: 1) employees were treated as creditors and participated in the discussions on voluntary arrangement; and 2) arrears of wages were treated as priority debts in the voluntary arrangement. Since many overseas countries had a comprehensive social security schemes to cater for unemployment, which were different from the situation in Hong Kong, it would not be appropriate to make direct comparison with them. The 1998 consultation exercise showed clearly that there were objections from both the employers and employee groups to the proposed change in the scope of the PWIF. The Administration understood from market practitioners that in most cases, debts owed to employees was not the most critical debt for companies undergoing corporate rescue. The Administration therefore considered that on balance, the prudent approach would be to require employers to clear all the outstanding wages and entitlements of its laid off employees before starting the rescue procedure. It should also be noted that under the Bill, the company was not required to pay those contingent liabilities in respect of employees whose employment contracts continued after the commencement of the provisional supervision.

12. Given that the Bill would apply to companies of all scales and employment debts might contribute a large portion of debts in small and medium companies, Mrs Miriam LAU expressed concern whether those companies which had the potential to turn around but were not able to settle all the employment debts could be exempted from such a requirement. PAS for FS explained that the initiation of the corporate rescue procedure was a commercial decision. Creditors should be able to judge whether the company had a chance to turn around and hence whether further financial assistance should be provided to save the company. She emphasized that the Bill was to provide companies with viable businesses with a breathing space and not intended to prolong the death of non-viable businesses.

13. The Chairman shared Mrs Miriam LAU's concern that when a company

was in financial difficulty, it would have already requested the employees to defer or cut wages voluntarily. The company might not be able to satisfy the requirement of a trust account where sufficient assets or cash had to be available. The Chairman also showed concern for the cost incurred in appointing the provisional supervisor given that the workout concerned would require in-depth professional knowledge. OR/Atg acknowledged the members' concern. The LRC recognized that the Bill might be rarely used due to the cost element, however, the Administration observed that the success of the Bill relied not on the frequency of its usage but on whether it was successfully used. DS for FS stressed the importance of taking the first step of introducing a statutory corporate rescue procedure in Hong Kong. In order to balance the interest of all parties, the employers would be required to settle all outstanding wages and entitlements first before commencing a provisional supervision.

14. Mr LEE Cheuk-yan enquired whether the trust account would be provided explicitly in the legislation. He sought clarification on whether the employer or the provisional supervisor would be liable for the employees' contracts within the moratorium. In response, DS for FS advised that the requirement on setting up a trust account was explicitly provided in clause 168ZA(c)(iv)(A) in which sufficient money had to be made available in a bank account to meet all the debts and liabilities owed to employees. The Assistant Principal Solicitor (APS) advised that clause 168ZK(1) provided the circumstances under which the provisional supervisor would be personally liable for the wages and other emoluments. However, the provisional supervisor would be indemnified out of the assets of the company concerned.

15. Miss CHAN Yuen-han enquired how employees' interest could be protected if a company were unable to pay the employees during the course of moratorium and the voluntary arrangement. OR/Atg responded that once the rescue procedure was initiated, the company would be required to have sufficient assets or fund available in the trust account to meet all the outstanding claims of employees. Meanwhile, the provisional supervisor would have another 14 days to decide whether to adopt the contracts of the existing employees. He might choose to lay off some workforce based on commercial judgement. After that, the provisional supervisor would become personally responsible for the ongoing statutory entitlements of the employees and other debts of the company. For new debts incurred after the commencement of the provisional supervision, any creditors, including employees, could petition for the winding up of the company

whenever necessary since the moratorium would only apply to debts outstanding prior to the corporate rescue procedure.

16. Miss CHAN Yuen-han asked whether in the case where the provisional supervisor decided that the company could not be saved and could not afford the wages for current employees during the moratorium, the employees would be advised to approach PWIF. OR/Atg advised that if the provisional supervisor was unable to meet the contractual commitments with the creditors, including the employees, or if debts occurred after the commencement of the provisional supervision, the Bill provided for the creditors to go for voluntary winding up of the company. The employees could also seek assistance from the PWIF.

17. Mr LEE Cheuk-yan expressed concern whether the employees, as creditors, would be able to wind up the company if the provisional supervisor owed them wages during the moratorium when the company was undergoing a rescue procedure. He quoted a case in which the affected employees could neither wind up the company nor seek assistance from the PWIF because the PWIF would not offer assistance if the status of winding up was not clear. He also asked whether the employees would be given one vote only among the many creditors in seeking for the winding up of the company, and whether they had the right to object to the financial re-arrangement.

18. In a voluntary arrangement proposal, APS clarified that only the debts incurred before the commencement of the voluntary arrangement would be handled; new debts incurred after the commencement would be outside the scope of the voluntary arrangement, and the creditors, including employees, would not be bound by the moratorium and were allowed to petition for winding up of the company. The court would then decide whether a winding up should take place after weighing all relevant factors on a case by case basis. As such, the voting scenario suggested by Mr LEE would not exist. Moreover, if a company was not able to shoulder the daily expenses in the course of the arrangement, including wages, the provisional supervisor should evaluate the chance for the company to be saved. He could by all means suspend the arrangement if he found little hope in saving the company. PAS for FS supplemented that clause 168ZD(4)(a) provided clearly that new debts incurred after the commencement of the provisional supervision would not be bound by the moratorium.

(*Post-meeting note*: the Administration's further explanation on the right

of employees was circulated to members vide LC Paper No. CB(1)1074/99-00(01).)

19. Mr Eric LI pointed out that there was no overseas experience in settling all arrears of entitlements of employees first before doing the rescue. Given that at present over 99% of winding up jobs were done by PWIF, he anticipated that the frequency of using the Bill might not be high in future and enquired about the number of precedents in which wages could be settled before winding up of the companies.

20. DS for FS advised that overseas countries offered different types of protection to employees and since no other countries had any arrangement similar to the PWIF in Hong Kong, it would be difficult to make direct comparisons. OR/Atg advised that approximately 40% of the compulsory winding-up petitions filed in the High Court currently were handled by the Legal Aid Department on behalf of affected employees, 85% of the companies that went into compulsory liquidation in Hong Kong had little or no assets whereas other companies capable of paying the ongoing costs might have approached liquidators in the private sector. The Administration considered it important to establish a mechanism to assist the companies in addition to the informal corporate workouts, though it might not be used too frequently. Mr Eric LI remarked that the Bill would not be applied to the majority of cases in Hong Kong and the chances of using it would be helping marginal cases in financial re-arrangements. The Administration should recognize clearly that this would be a huge law with limited usage.

Conflict between directors and provisional supervisors

21. With reference to the LegCo Brief, Mr James TIEN noted that directors and senior management were encouraged to act on insolvency and develop their plans of saving the company at an early stage. Meanwhile, the provisional supervisor would formulate a proposal for creditors as a corporate doctor and got all the power of decision, including dismissing the directors of the company. Mr TIEN expressed concern whether it would be fair to the directors if they did not agree to the provisional supervisor's decisions but would have to be liable for them.

22. OR/Atg advised that since the statutory corporate rescue procedure would be initiated by directors or shareholders, they would have to take a

commercial decision as to whether the company should come to a voluntary arrangement under Section 166 of the Companies Ordinance (Cap. 32). Since there was no statutory moratorium for such informal voluntary arrangement, the creditors, especially the small ones, could present a petition to wind up the company at any time. Against this background, the Administration proposed a statutory moratorium to bind small and big creditors alike in a corporate rescue procedure to prevent immediate winding up of the company. Although the provisional supervisor would be given the right to dismiss directors, the provisional supervisor would in reality co-operate with the directors to turn the company around.

23. Mr James TIEN considered that should directors choose to contiune their business against the financial difficulty, they would prefer running the business for the next six months themselves instead of letting the provisional supervisor step in. He also questioned the rationale for the provisional supervisor to be indemnified out of the assets of the company even though his decisions were not acceptable by the directors. DS for FS drew members' attention to the duties of the provisional supervisor as listed in the 18th Schedule of the Bill where the provisional supervisor would be required to act in the best interests of the company. As such, she believed there should not be conflicts between the directors and the provisional supervisor.

24. As directors might usually bear a personal liability on behalf of the company, Mr James TIEN enquired whether the directors would still be liable if the provisional supervisor had turned the company into a worse condition, and whether the directors could at any time during the provisional supervision offer voluntary liquidation. In response, DS for FS explained that once provisional supervision was initiated, the management of the company would be taken over by the provisional supervisor from the directors. But it was envisaged that the provisional supervisor would work closely with the directors on the daily management of the company. Nevertheless, in order to balance the interest of all the stakeholders involved, creditors would be given the right to terminate the procedure.

25. Mr James TIEN took the view that after giving the provisional supervisor a try to save the company in a specified period, the directors should also have a choice to suspend the provisional supervision if they were dissatisfied with the provisional supervisor, taking into account that the directors would be

personally liable for the company's debts. To address the member's concerns, DS for FS said that if the provisional supervisor failed to submit a satisfactory proposal to the creditors within the first 30 days, his request for extension of the moratorium would have to be approved by the court. The court would consider the performance of the provisional supervisor and examine the situation and would not necessarily extend the moratorium as requested. Besides, further extension after the six-month period would have to be approved by the creditors. The Chairman remarked that any directors or shareholders could also go to court to oppose to the extension applied by the provisional supervisor after the 30-day period.

Appointment of provisional supervisor

26. Miss Margaret NG requested the Administration to supply a list of all the provisions in the Bill which deviated from the recommendations of the LRC.

> (*Post-meeting note*: the list of provisions in the Bill deviated from the recommendations of the LRC was circulated to members vide LC Paper No. CB(1)1074/99-00(01).)

Miss NG also enquired about the Official Receiver's procedures of appointing a panel of professionals eligible for appointment as provisional supervisors, and the ways of determining the scale of fees on which a provisional supervisor would be remunerated. Since the provisional supervisor would be indemnified out of the assets of the company, Miss NG was concerned whether the amount left for the creditors would be affected. Furthermore, Miss NG referred to clause 30 and sought clarification on whether the provisional supervisor could also be appointed as the provisional liquidator.

27. Regarding the panel of provisional supervisors and the level of remuneration, OR/Atg advised that the Administration currently had a panel A and B scheme for insolvent liquidation. For panel A liquidation, the company would go into liquidation with more than HK$200,000 in assets, and there was an approved panel of insolvency practitioners who should be able to demonstrate experience in insolvency and the necessary expertise to undertake the administration of insolvent liquidation. He also advised that as the provisional supervisor would be indemnified out of the assets of the company, the amount ultimately became available for creditors would become less. However, the

Hong Kong Monetary Authority issued guidelines in November 1999 to authorized institutions on informal corporate workouts and recognized that corporate doctors should be paid out of the assets of the companies. When a company went into insolvent liquidation, the fees and charges of the liquidator were met out of the assets of the company as a first charge before onward distribution of dividends to creditors. This practice had been going on for quite some time and the Bill only reflected the current practice.

28. DS for FS pointed out that clause 30 was not directly related to the corporate rescue procedure but was an amendment to the Companies Ordinance (Cap.32) in order to provide the Official Receiver with the authority on appointment of provisional liquidators. The proposed legislation allowed a provisional supervisor to become the liquidator of the company because he should comparatively be more familiar with the situation and operation of the company and thus the cost of liquidation would likely to be lower.

29. Since the panel members would be favourably remunerated, Miss Margaret NG showed grave concern about how they would be selected. In order to avoid criticism, there should be an explicit set of objective criteria for the appointment that would be made known to the public beforehand and sufficient safeguard for the transparency and fairness should be in place in the appointment process during which the public could raise query if necessary. Besides, she expressed worries that there might be conflict of interest if the provisional supervisor could become the liquidator.

30. The Senior Assistant Law Draftsman (SALD) advised that clause 168W provided clearly the requirements of the panel members and the setting up of the appeal channel through the Administrative Appeals Board. Besides, the appointment criteria and composition of the panel would be publicized through the notice in the Gazette. OR/Atg pointed out that the panel members would have to be highly experienced individuals who could gain confidence and respect from the creditors, and possessed sound knowledge in insolvency and corporate workout. However, the Administration had yet to finalize the details of the criteria.

31. While Miss Margaret NG expressed concern that the large accounting firms would probably have monopoly over this area of practice, Mr Eric LI pointed out that if the criteria so set were unattainable to the majority of firms, the monopoly situation could happen. However, he considered that the panel A and B scheme would provide a chance also for smaller practitioners to gain experience.

This scheme had been in place for years and professional accountants were familiar with its operations. On the scale of fees, Mr Eric LI considered that if it was a fixed fee, then the mechanism of appointing the panel members should be on a rotational basis due to the absence of competition. Nevertheless, as long as a channel was available for all to eventually get to panel A, he considered it a transparent process.

32. DS for FS assured members that the list of all qualified persons on the panels would be published. It would be up to the directors to choose whoever suitable to become the provisional supervisor of the company. In actual practice, the appointer would be expected to approach the provisional supervisor and let him take a look at the affairs of the company first before formally initiating the corporate rescue procedure. In the documents that the company would have to file with the Official Receiver, the Registrar of Companies and the High Court Registry, one of them would be on the expected remuneration of the provisional supervisor, so that there would be a fair indication to the creditors about the total cost involved in appointing the provisional supervisor for producing the proposal. As for the scale of fees, the Administration would liaise with professional bodies and the parties concerned to come up with an acceptable scale. There were also provisions within the Bill for creditors to raise objection with the court concerning the amount of remuneration payable to the provisional supervisor. Since it was the Government's policy to create more competition within the insolvency practitioner market, the establishment of the panel B scheme could provide a training ground for new practitioners to join the field. Once there was a fair amount of competition, the market itself would determine the fees and the remuneration would come down and become more accessible for companies.

III Any Other Business

33. In view of the complexity of the Bill, Mr James TIEN considered that the Committee might not be able to complete the scrutiny of the Bill by the end of June 2000. Miss CHAN Yuen-han shared Mr TIEN's view given that the Bill was very complicated despite limited benefit. Miss Margaret NG suggested that a realistic assessment of the work of the Bill be conducted in the coming meeting. Should the Committee consider that the scrutiny of the Bill could not be finished by June 2000, it might be advisable to suspend at an early stage.

34. DS for FS said that the Administration would like to have the Bill passed during the current Legislative Council session so that statutory corporate rescue procedure could be made available to companies in financial difficulties as early as possible. Apart from corporate rescue, there were other provisions in the Bill where technical amendments to various sections of the Companies Ordinance (Cap. 32) had been proposed. In view of members' concerns, she suggested that the Bills Committee should examine the technical amendments first, before scrutinising those parts related to corporate rescue and insolvent trading. Members agreed to the suggestion. The Chairman remarked that the Bill could be divided into two parts in case the scrutiny of the entire Bill could not be finished by June 2000, having the part on technical amendments completed first leaving behind the rest to the next session. DS for FS stressed that the Administration aimed at passing the entire Bill with all its provisions within the current session.

35. Two meetings were scheduled for Monday, 28 February 2000 at 4:30 p.m. and Tuesday, 29 February 2000 at 2:30 p.m. respectively.

36. There being no other business, the meeting adjourned at 4:35pm.

Legislative Council Secretariat
22 May 2000