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**Paper for the House Committee Meeting
on 16 October 2015**

**Legal Service Division Report on
Companies (Winding Up and Miscellaneous
Provisions) (Amendment) Bill 2015**

I. SUMMARY

- 1. The Bill** The Bill seeks to amend the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) and its subsidiary legislation to:

 - (a) enhance the protection for creditors;
 - (b) streamline the winding up process;
 - (c) strengthen regulation under the winding up regime; and
 - (d) make related, consequential and minor technical amendments.

- 2. Public Consultation** The Administration conducted a public consultation on the legislative proposals from April to July 2013. Comments on the draft provisions of the Bill were sought from an Advisory Group (AG) and relevant stakeholder groups in April and July 2015 respectively. The AG, the Standing Committee on Company Law Reform, and relevant stakeholders indicated support for the legislative exercise. The general public has not expressed any negative views on the exercise.

- 3. Consultation with LegCo Panel** As advised by the Clerk to the Panel on Financial Affairs, the Panel was consulted on 3 May 2013 and 7 July 2014 and members had no objection to the Administration introducing the Bill into the Legislative Council. However, members have raised concerns and enquiries on a number of issues, including safeguards to prevent abuse of section 228A of Cap. 32 by company directors on the director-initiated creditors' voluntary winding-up procedure of a company, measures to ensure protection of employees' interests in the list of creditors during a winding-up, and protection of bona fide undervalue transactions made by a company in good faith.

- 4. Conclusion** In view of Members' concerns raised at the Panel meetings, Members may wish to set up a Bills Committee to study the Bill in detail.

II. REPORT

The date of First Reading of the Bill is 14 October 2015. Members may refer to the LegCo Brief (File Ref.: IB&W/2/1/5/4C) issued by the Financial Services and the Treasury Bureau on 30 September 2015 for further details.

Object of the Bill

2. The Bill seeks to amend the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) and its subsidiary legislation to enhance the protection for creditors, streamline the winding up process, strengthen regulation under the winding up regime, and to make related, consequential and minor technical amendments.

Provisions of the Bill

3. Some of the major proposed amendments are summarized below.

Enhancing the protection for creditors

4. Under the existing regime, the court does not have the power to set aside "transactions at an undervalue"¹ entered into by a company if the company goes into liquidation. The Bill proposes to provide that such transactions are voidable at the discretion of the court if the transaction is entered into by a company within five years before the commencement of its winding-up (new sections 265A to 265E).

5. The Bill also proposes to provide for the liabilities of directors and past shareholders to contribute to the assets of a company which has made payment out of its capital in respect of the redemption or buy-back of any of its own shares in cases where the company is wound up within one year of the relevant payment out of capital (new section 170A and proposed sections 171 and 179).

6. Under section 228A of Cap. 32, after the directors (or the majority of the directors in the case of a company having more than 2 directors) of a company have formed an opinion that the company cannot by reason of its liabilities continue its business, the directors may resolve at a meeting of the directors to commence winding-up of the company by delivering a winding-up statement to the Registrar of

¹ The meaning of "transaction at an undervalue" is provided in new section 265E (introduced by clause 88) : A company enters into a transaction with a person at an undervalue if (a) the company makes a gift to that person, or otherwise enters into a transaction with that person on terms that provide for the company to receive no consideration; or (b) the company enters into a transaction with that person for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the company.

Companies. According to paragraph 6(d) of the LegCo Brief, there is a potential risk of abuse by company directors or a provisional liquidator appointed by the directors in this winding-up procedure. The Bill adds a new section 228B to provide that, among other things, the provisional liquidator appointed under section 228A is required to obtain the sanction of the court to execute certain powers of a liquidator in a creditors' voluntary winding-up.

7. Other amendments relating to enhancing the protection for creditors include prescribing the minimum period of notice for the first creditors' meeting upon the commencement of a creditors' voluntary winding-up to allow sufficient time for the creditors to prepare for the meeting (proposed section 241) and enhancing the effectiveness and flexibility of the provisions relating to floating charges (new section 267A).

Streamlining the winding-up process

8. In a winding-up, a committee of inspection (COI) may be appointed under sections 206 and 243 of Cap. 32 to represent the creditors and contributories² of the company for supervising and giving directions to the liquidator during the course of the winding-up. The Administration proposes to introduce provisions to streamline the proceedings of COI by -

- (a) prescribing the minimum and maximum numbers of members of a COI to be 3 and 7 respectively, which may be varied by an order of the court upon an application by a liquidator (new section 206(3) and (4), and proposed section 243);
- (b) removing the present mandatory requirement that the COI must meet at least once a month if COI fails to specify a time for a meeting and to make related provisions for meetings (new section 206A);
- (c) providing that it is not necessary to fill a vacancy in a COI if the total number of the continuing members does not fall below the prescribed minimum number and the liquidator and a majority of the continuing members agree that, having regard to the position in the winding-up, it is unnecessary for the vacancy to be filled (new section 207(7B));
- (d) enabling COIs to perform their functions and make decisions through written resolutions (new sections 207D to 207K);

² Under section 171 of Cap. 32, "contributory (分擔人)" means every person liable to contribute to the assets of a company in the event of its being wound up, and for the purposes of all proceedings for determining, and all proceedings prior to the final determination of, the persons who are to be deemed contributories, includes any person alleged to be a contributory.

- (e) allowing meetings of COIs to be conducted remotely i.e. in a manner that enables persons who are not present together at the same place to attend it. A person is regarded to be attending the meeting if the person is able to exercise any rights of the person to speak and vote at the meeting (new section 207B); and
- (f) allowing the bills of costs or charges of a person employed by the Official Receiver or the liquidator in a court winding-up to be approved by COI by resolution so that taxation by the court is not required (proposed rule 176(2) of the Companies (Winding-up) Rules (Cap. 32H)).

9. Further, the Bill proposes to provide for a prescribed form of statutory demand for use by a creditor to demand payment of a debt from the debtor-company before petitioning to the court for the winding up of the company (proposed sections 178(1) and 327(4), and new rules 3A, 3B and 3C of, and new Form 1A to the Appendix to, Cap. 32H).

Strengthening regulation under the winding-up regime

10. The Bill proposes amendments in relation to the regulatory measures for liquidators and provisional liquidators to strengthen regulation under the winding-up regime by -

- (a) setting out more clearly the powers, duties, the basis for determining remuneration, tenure of office of a provisional liquidator in a court winding-up, the termination and resignation of a provisional liquidator (proposed sections 193 to 196 and 199, and new sections 199A and 199B);
- (b) providing that a liquidator would not be absolved from liabilities arising from the liquidator's misfeasance or breach of duty or breach of trust notwithstanding that he has obtained a court order releasing him as liquidator after the completion of the winding-up (proposed sections 205 and 276);
- (c) expanding the list of persons disqualified from being appointed or nominated for appointment, and from acting, as a provisional liquidator or liquidator (new sections 262A and 262B);
- (d) requiring disclosure by a prospective provisional liquidator and prospective liquidator of specified relationships between him or his

immediate family members³ and the company being wound up before his formal nomination or appointment (new sections 262C to 262F); and

- (e) making further provisions in relation to the private examination procedure⁴ and public examination procedure⁵ (new sections 286A to 286E, proposed rules 5 and 62 and new rules 51A and 58A and 58B of Cap. 32H).

Related, consequential and minor technical amendments

11. The Bill also proposes certain related, consequential and technical amendments. These amendments include, for example, aligning the time limits for giving notices in the Gazette for certain actions in the commencement of a voluntary winding-up, and repealing superfluous provisions in Cap. 32.

Commencement

12. The Bill, if passed, would come into operation on a day to be appointed by the Secretary for Financial Services and the Treasury by notice published in the Gazette.

Public Consultation

13. According to paragraph 16 of the LegCo Brief, the Administration conducted a three-month public consultation on the legislative proposals from April to July 2013 and published the consultation conclusions in May 2014. The Administration briefed the Standing Committee on Company Law Reform (SCCLR) on the consultation conclusions in June 2014 and sought the views of an Advisory Group (AG) and relevant stakeholder groups (including the Hong Kong Association of Banks, and the legal and accounting professions) in April and July 2015 respectively on the draft provisions of the Bill. The AG, SCCLR, and relevant stakeholders indicated support for the legislative exercise. The general public has not expressed any negative views on the exercise.

³ Under new section 262D(6) (introduced by Clause 85), "immediate family member (家人)", in relation to an individual, means a spouse, parent, child, sibling, grandparent or grandchild of the individual.

⁴ This is the procedure provided in new section 286B where the court may summon the persons concerned to attend before it and be examined on oath.

⁵ This is the procedure provided in new section 286A where the court may direct the persons concerned to attend before it and be publicly examined.

Consultation with LegCo Panel

14. The Clerk to the Panel on Financial Affairs has advised that the Panel was briefed on 3 May 2013 and 7 July 2014 on the legislative proposals in the public consultation document for improving Hong Kong's corporate insolvency law and the outcome of the consultation and refinements to some of the proposals. Members raised concerns and enquiries on a number of issues, including safeguards to prevent abuse of section 228A of Cap. 32 by company directors on the director-initiated creditors' voluntary winding-up procedure of a company, measures to ensure protection of employees' interests in the list of creditors during a winding-up, and protection of bona fide undervalue transactions made by a company in good faith. Members also discussed related issues, including the need to review the level of preferential payments payable to employees in a winding-up under section 265 of Cap. 32, and the Government's timetable for introducing a statutory corporate rescue procedure and protection of employees' interests under the procedure.

Conclusion

15. The Legal Service Division is scrutinizing the legal and drafting aspects of the Bill. In view of Members' concerns raised at the Panel meetings, Members may wish to set up a Bills Committee to study the Bill in detail.

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