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29 February 2000

Ms Leung Siu-kum
Clerk to Bills Committee
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong
[Fax: 2869 6794]

Dear Ms Leung,

Companies (Amendment) Bill 2000

Thank you for your letter of 23 February 2000. Our response to the request by Members for further information on the three issues raised is as follows –

(i) to provide explanation on the right of employees or creditors for making application for the winding up of the company to recover debts incurred after the commencement of the moratorium. Please also explain whether the company undergoing corporate rescue will affect the successful application for the winding up

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Insofar as the right of employees or creditors (of a company which has initiated corporate rescue) for making application for the winding up of the company to recover debts incurred **after** the commencement of the moratorium is concerned, clause 168ZD(4)(a) expressly provides that "[the moratorium on legal proceedings] *shall not apply to or in relation to any debt or other liability of the company incurred on or after the relevant date (including any creditor in respect thereof)*".

In other words, there is, legally speaking, **no** moratorium to bind the right of the employee or creditors for making an application for the winding up of the company to recover debts incurred **after** the commencement of the moratorium.

In case where there is a voluntary arrangement reached between the creditors and the company, clause 168ZV(1) provides that "*no creditor bound by the arrangement may commence or continue any winding up proceedings against the company*". Creditors not bound by the moratorium under clause 168ZD(3) will not be bound by the voluntary arrangement. The voluntary arrangement does **not** apply to them if they have no other arrangement/agreement reached with the provisional supervisor as regards their respective debts.

(ii) to provide a list of all the provisions in the Bill which deviate from the recommendations of the Law Reform Commission; and

The provisions in the Bill which deviate from the recommendations of the Law Reform Commission are listed as per the attached.

(iii) to provide information on the effectiveness of the corporate rescue model implemented in Australia and Canada

The Australian Securities Commission (ASC) conducted an extensive statistical survey in 1998, which looked at the number and outcome of voluntary administrations under Part 5.3A of the Corporations Law. The ASC reviewed its database of the 5,760 companies in Australia that entered voluntary administration between 1 July 1993 and 30 June 1997. The survey indicated that when allowing for the outcome of deeds of company arrangement, it appeared that the number of companies resuming normal trading after entering administration is around 20% to 25%.

We are trying to collate data from Canada.

However, we wish to point out that the success, or otherwise, of a voluntary arrangement of a company under administration/rescue is dependent on a number of socio-economic factors, such as creditors' attitude, the prevailing national/regional economic situation, etc. which may vary from place to place. The figures we have obtained from other jurisdiction may or may not be of relevance to the case of Hong Kong.

Yours sincerely,

(L W TING)
for Secretary for Financial Services

b.c.c. OR (Attn: Mr E T O'Connell) 2104 7151
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LD (Attn: Mr Geoffrey Fox, 2869 1302
Miss Shandy Liu)

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**Provisions in the Companies (Amendment) Bill 2000 (the Bill)
on corporate rescue and insolvent trading
which are different from the Law Reform Commission's (LRC) recommendations**

Corporate rescue

Subject & section	Recommendation of LRC	Provisions in the Bill
Application s.168W	Should apply to insurance company. (Para. 2.19 of the LRC Report)	Not to apply to insurance company.
	Should apply to securities & futures industries, including the leveraged foreign exchange industry. (para. 2.22 and 2.23)	Not to apply to registered entities in securities & futures industries and the leveraged foreign exchange industry. Reason: These industries are already regulated under law which empowers the regulator to assume control of the regulated entity or oblige the entity to act in a certain manner in case the entity has financial difficulties. (LegCo Brief para 21 to 23)
Persons who may appoint provisional supervisor (the PS). s.168Y	Receivers should be able to appoint PS. (Para. 4.10)	Receivers excluded. Reason: Conflict of interest in terms of whose interest the PS serves – the creditor who appointed him; the company; or all the creditors of the company. (LegCo Brief para 24 to 26)
Employees' treatment s.168ZA(c)(iv)	Employees to be accommodated under PWIF. Employees' claims enjoy same preferential status as provided for in the Companies Ordinance. (para. 5.42 – 5.47)	Debts owed to Employees laid off by company have to be fully settled before company goes into corporate rescue, or company has to maintain a trust account with sufficient money to pay off all employees' claims up to relevant date. Reason: Results of the public consultation carried out in December 1998 indicated that both employers and employees groups were

		against the use of PWIF in corporate rescue. (LegCo Brief para 17 to 20)
Moratorium s.168ZD	Set off should be allowed. (para. 5.23).	Set off subject to consent of PS. Reason: If set-off were to be allowed, banks might get hold of all the cash of the company by exercising their right to combine accounts and set off debit and credit balances, making the continued operation of the company virtually impossible.
Regulatory powers of the Securities and Futures Commission (the SFC) over listed companies and proceedings of Insider Dealing Tribunal (the IDT) 168ZD(4)(e)&(f).	Not mentioned.	Regulatory powers of SFC expressly preserved and proceedings of IDT not be bound by the moratorium. Reason: It is in the public interest that SFC's regulatory powers and IDT's proceedings not be affected by the moratorium. (LegCo Brief para 27 to 28)
Indemnity s.168ZL(2)	The indemnity should have priority over all claims, whether secured or unsecured other than a fixed charge. (para. 9.17)	The indemnity shall have priority over all claims whether secured or unsecured. Reason: It is impracticable to make the indemnity subject to the claims of the fixed chargees because most assets of companies in financial difficulties would have already been charged by way of fixed charges. To do so would put the PS in a very disadvantaged position particularly when he might be personally liable in respect of certain debts. The result might be that no one is prepared to act as PS.
Removal and resignation of PS s.168ZO(2)	Resignation should be possible without cause shown where majority of creditors and PS agree and replacement available. (para.	Resignation only with the leave of the court. Reason: To allow PS to resign without cause shown even if the majority of

	11.13)	creditors agree could easily lead to abuses because not all creditors will turn up at the meeting called for the purpose. Calling of creditors' meeting to approve the resignation could also be very expensive particularly when large number of creditors are involved. Resignation to be allowed only with leave of court would give certainty and forestall possible abuses.
s.168ZO(10)	OR should have power to apply to court for an order to disqualify the PS from acting as PS and to forward a report to the PS's professional body if it appears to the liquidator following from a provisional supervision that the PS was in breach of his obligations. (para. 11.4)	No power given to OR to apply to court for disqualification order against PS. Reason: Disqualification from acting as PS can be achieved through the panel requirements under 168W (1)(c) and OR refusing to issue a statement of fitness under s.168X(a)(iii)(B). Hence, there is no need to put in a separate provision.
Insolvent Trading		
Funding creditors privilege	Funding creditors should be entitled to receive additional payment. (para. 19.84 – 19.85)	Not included. Reason: The liquidator is already empowered under the present s.265(5B) of the Companies Ordinance to apply to court for an order to give the funding creditors an advantage over others.