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C2/1/12C(2000)X

7 March 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

I refer to your letter of 1 March 2000. Our response to the concerns raised by Members at the meeting of 29 February 2000 is set out below –

(1) Information on the consequences if section 141(7) is not compiled with

Members may recall that the query in relation to section 141(7) was raised during the discussion of the new section 116BA. We consider that a penalty clause is necessary for directors and company secretaries who fail to comply with the new

section 116BA because the resolution will be passed through the unanimous written consent procedure without the need of convening a meeting. If the auditor is not notified in time, he would not have the opportunity to obtain the relevant document at a physical meeting. As a result, the auditor may not be able to carry out his duties. It is therefore necessary to set a more stringent requirement on company's officers if they failed to observe this particular duty.

We would like to clarify that the rights of auditors to have access to general meetings and notices, etc as set out in section 141 and the new section 116BA imposing an obligation on directors and company secretaries to notify auditors of the proposed written resolution are of different nature. It may not be appropriate to draw a direct comparison between them as regards the necessity of a penalty clause. Section 141 specifically confers a right on the auditor to be notified of any general meetings of the company, to receive other communications relating to any general meeting which any members of the company is entitled to receive, etc. If an auditor fails to obtain all the information necessary for the purpose of his audit, he would state that fact in his report.

(2) Clarification on whether resolution agreed to in accordance with the proposed section 116B is still valid when a director or secretary fails to comply with section 116BA(1)

The proposed new section 116BA(4) states "Nothing in this section affects the validity of any resolution." Resolutions are therefore valid even though the directors or secretaries have failed to notify the auditors of the contents of the resolutions at or before the time the resolution is supplied to a member for signature.

(3) Clarification on whether the existing legislation permits meetings conducted via the Internet, and whether resolutions are required to be signed physically

The Companies Ordinance at present does not have any provisions prohibiting the passing of resolutions via the Internet. Members may wish to note that under section 15(3) of the Electronic Transactions Ordinance a resolution will be acceptable in an electronic form if –

(i) the signer or the person to whom signature is given, i.e. the company is not acting on behalf of a government entity;
(ii) the person to whom the signature is given, i.e. the company consents to a digital signature; and

(iii) the signature is supported by a current valid recognised certificate under the Ordinance.

In other words, if both parties consent to the use of Internet for the passing of a resolution, they are permitted to do so under the relevant sections of the Electronic Transactions Ordinance, and these sections are scheduled to come into operation on 7 April 2000.

(4) Consideration be given on providing the director ordered to be examined under the proposed 168IA an opportunity to set aside the order

Every judgment or order of the Court of First Instance in any civil matter is appealable pursuant to section 14 of the High Court Ordinance, Cap 4. Order 59, r.4(1)(b) of the Rules of the High Court provides that the time for doing so is

"in the case of an appeal from an order or decision made

or given in the matter of the winding-up of a company, or in the matter of any bankruptcy, 21 days,"

from the date of the order.

The examination order under the proposed section 168IA (according to Companies (Winding-up) Rules No 51 proposed to be applicable to proceedings under section 168IA by virtue of the new rule no. 57A) is to be made by a judge personally in chambers after hearing the submission made by the Official Receiver and considering the report submitted by him and any further information or explanation which the court may require. The court would only grant such an order if it is satisfied that there is a prima facie case against a certain director of a company that would render him liable to a disqualification order under Part IVA.

Furthermore, such an order is appealable pursuant to section 14 of the High Court Ordinance and Order 59, r.4(1)(b) of the Rules of the High Court and can be set aside if the court considers it appropriate.

Having regard to the foregoing, there is no need for a specific provision be added to the presently proposed section 168IA to give directors an opportunity to set aside the examination order.

(5) Consideration be given to amending the new section 209A(6) so that minority creditors' interests could also be taken into account

Section 209A(2)(a) has expressly put down as a factor which the court must have regard to when considering an application under that section "the wishes of the creditors and contributories of the company, as proved to it by sufficient

evidence." Given this requirement, we see no need to impose another express requirement on the Official Receiver to submit a report pursuant to section 209A(6) on minority creditors' interest.

If the circumstances of the case are such that there are matters falling within section 209A(2), including the wishes of minority creditors, and which the Official Receiver considers it necessary and appropriate to bring to the attention of the court, he should, pursuant to the proposed amended section 209A(6), submit a report to the court.

(6) Clarification on the circumstances in which the Official Receiver would appoint a special manager under section 216(1)

At present, the Official Receiver may under section 216 apply to court for approval on the appointment of a special manager under restrictive circumstances - if he is satisfied that the nature of the estate or business of the company, or the interests of the creditors or contributories generally so require. However, practical experience indicates that there are other circumstances where the Official Receiver may wish to apply to the court requesting the latter to approve the appointment of a special manager to handle certain aspects of work of a compulsory winding-up. This is especially significant when the Official Receiver has been facing an increasing workload and it is anticipated that the Official Receiver will be unable, for reason of resources constraint, to continue to properly perform his duties as liquidators in some cases. The proposed amendment to section 216 has been made with this in mind. The aim is to permit the Official Receiver, when the caseload so dictates, to be able to continue to act as liquidator with the assistance of a special manager in cases where the creditors wish to so appoint him. The

appointment of the special manager would still be subject to approval of the court.

(7) Provision of information on the rationale of the Standing Committee on Company Law Reform for the proposed repeal of section 228A

Section 228A applies where the relevant directors have formed the opinion that the company cannot by reason of its liabilities continue its business. The rationale behind the procedure then was to speed up the appointment of a provisional liquidator in emergency cases and where there are "good and sufficient reasons".

At its 138th meeting, the Standing Committee on Company Law Reform discussed the problems relating to section 228A having regard to practical experience of the use of section in recent years and agreed that it ought to be removed on the following grounds –

(i) in cases whereby the special procedure under section 228A were used, it was difficult to find an emergency in each case which necessitated its use;

(ii) in case of a real emergency, a petition could be presented to the court and an application made for the appointment of a provisional liquidator under section 193;

(iii) the court is unable to exercise control over the conduct of the provisional liquidation appointed under section 228A and there is no procedure for supervising such liquidator; and

(iv) the procedure has been abused to such an extent that

the shareholders are left with a "fait accompli" if the directors have used the section and appointed provisional liquidators in circumstances other than an emergency.

Extract from the minutes of the 138th meeting of the Standing Committee on Company Law Reform related to the discussion on the repeal of section 228A is at Annex.

We wish to add that the Law Reform Commission in its Report on "The Winding-up Provision of the Companies Ordinance" published in July 1999 has also recommended that the section be removed on the grounds that –

(i) it is desirable to cut out any potential within the winding-up provisions for abuse and that while there has been only anecdotal evidence of abuse, the potential remains while this section is in effect; and

(ii) the introduction of statutory procedure to deregister solvent and defunct private companies by the Companies Registry (which has commenced operation on 11 November 1999) would adequately provide for any situation that might arise and which would not provide a "grey" period of time which might be exploited by directors to the detriment of creditors and shareholders.

We would like to inform Members that we intend to move Committee Stage Amendments to -

(a) Clause 14 by stipulating a requirement on companies regarding recording of resolutions passed by the unanimous written consent procedure under the new section 116BA. The company shall cause a record of

the resolution to be entered in a book in the same way as minutes of proceedings of a general meeting of the company. Company's officers will be liable to a fine if they failed to observe the requirement.

(b) Clause 33 by amending the words "sub-section (5)" in sub-section 4(b) to "sub-section (6)".

Members may also wish to note that as per Member's request at the last meeting, we have written to the Small and Medium Enterprises Committee inviting their views/comments on the proposed corporate rescue procedure and insolvent trading provision.

Yours sincerely,

(L W TING)
for Secretary for Financial Services

ANNEX

Extract from the Minutes of the 138th Meeting of the SCCLR held on 24.4.1999

Para. Nos.	Contents	Action with

5.00 **Item 5 of the Agenda : Section 228A (Document No. 138-3)**

5.01 The Secretary asked members to amend Document No. 138-3 by inserting the word "not" after the word "did" in the first line of paragraph 3. The Chairman referred to Annex A which showed an increasing trend in the use of section 228A stating that he found it difficult to accept that there had been an emergency in each case which necessitated its use. Mr Winston Poon said that directors quite often waited until execution had been levied against the property of the company before instituting a creditors voluntary winding-up under section 228A. If there was a real emergency and the directors considered that the assets were in jeopardy, a petition could be presented to the court and an application made for the appointment of a provisional liquidator. The Chairman agreed with Mr Poon and said that, if a provisional liquidator was appointed by the court, a degree of control or supervision could be exercised over his conduct which was not the case under section 228A.

5.02 Mr Gerald Hopkinson was concerned with the removal of the section merely because there was no procedure for supervising the provisional liquidator. He wondered whether it would be preferable to retain the section but to write into the Ordinance

Para. Nos.	Contents	Action with
	supervisory controls over the liquidator's conduct and powers. The Chairman thought that this would be an unnecessary duplication as one could merely apply to the court for the appointment of a provisional liquidator who would be subject to such control and supervision. Mr Winston Poon explained that the section was not necessary as there were other ways to appoint provisional liquidators. It had been enacted initially, as an inexpensive method of appointing provisional liquidators in an emergency. It has, however, been abused to such an extent that the shareholders are left with a "fait accompli" if the directors have used the section and appointed provisional liquidators in circumstances other than an emergency. Members agreed that the section ought to be removed from the Ordinance and the Official Receiver agreed to prepare draft drafting instruction for submission to the Secretary for Financial Services.	Official Receiver