

The continuing evolution of the Hong Kong Corporate Insolvency regime – news of important amendments and an update on the slow but steady progress towards a corporate rescue law.

Amendments

On 3 June 2016, the **Companies (Winding Up and Miscellaneous Provisions) (Amendment) Ordinance** (“**Amendment Ordinance**”) was gazetted. The effective date is yet to be confirmed but is likely to be the end of 2016 or early 2017.

The Amendment Ordinance follows the “hiving off” of the insolvency provisions from the Companies Ordinance into the **Companies (Winding Up and Miscellaneous Provisions) Ordinance** (Cap. 32) (“**CWUMPO**”) in March 2014. The long awaited amendments are intended to modernise and consolidate the corporate insolvency regime in Hong Kong as well as improve creditor protection and streamline the winding up process.

There follows a brief summary of the significant changes which result from the Amendment Ordinance, which should result in enhanced creditor protections.

> **Transactions at an undervalue:** Following the effective date, the Hong Kong Court of First Instance (the “**Court**”) will have the power to set aside a transaction at an undervalue which is entered into by a company within five years before the commencement of its winding up. A “transaction at an undervalue” is defined as a transaction:

- which involves a gift or is entered into on terms which provide no consideration to the company; or
- where the consideration (in money or money’s worth) is significantly less than the value (in money or money’s worth) of the transaction itself.

This is a welcome addition to the powers of a liquidator to claw back assets which have been improperly removed from a company, for the benefit of creditors.

> **Unfair Preferences:** Previously the unfair preferences provisions of the CWUMPO were incorporated by reference from the Bankruptcy Ordinance (Cap. 6) (which deals with the insolvency of individuals).

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The Amendment Ordinance provides for standalone provisions (including a definition of “unfair preference”).

- > **Extension of the meaning of “associate” for the purposes of voidable transactions:** The CWUMPO previously incorporated by reference the definition of “associate” from the Bankruptcy Ordinance (which was problematic). Following amendment, the CWUMPO will contain a standalone definition of associate which will be expanded, for example, to include the spouse of a director.
- > **Extending the “claw-back” period for floating charges:** Under the existing provisions of Section 267 of the CWUMPO, floating charges created in favour of “persons who are connected with the company” in the 12 months prior to the commencement of winding-up are vulnerable to claw-back by a liquidator. Under the Amendment Ordinance, this period will be extended from 12 months to 2 years prior to the commencement of a winding-up for such persons.
- > **New provisions on powers and duties of liquidators and provisional liquidators:** New provisions will set out more clearly the powers and duties of liquidators and provisional liquidators, in particular:
 - restrictions on the ability of a liquidator or provisional liquidator to tout or offer an inducement for appointment;
 - confirming that a liquidator will still have liability arising from his or her misfeasance or breach of duty notwithstanding that he or she has obtained a court order to be released as liquidator after completion of the winding up;
 - expansion of the list of persons disqualified for appointment as a liquidator or provisional liquidator (including those who have a conflict of interest, persons against whom a disqualification order has been made by a court and persons with mental incapacity);
 - a new requirement for prospective liquidators and provisional liquidators to complete a disclosure statement in relation to any specified relationships between him or her (and their immediate family members) and the relevant debtor company; and
 - new provisions in CWUMPO and the Companies (Winding-up) Rules (Cap. 32H) on the procedures for removal and resignation of a liquidator in a voluntary winding-up.

For clarity, following amendment, the CWUMPO will set out the powers of a liquidator for different types of winding-up procedures in a new Schedule 25 (rather than in Section 199 of CWUMPO as is currently the case).

- > **Promoting additional court-free procedures:** The Amendment Ordinance introduces new provisions which allow committees of inspection (“COIs”) to approve costs of liquidators’ agents and permit liquidators to appoint a solicitor to assist in the liquidator’s duties on notice to creditors, both of which previously required Court sanction.
- > **Streamlining the winding up process:** Changes to the proceedings of COIs including:
 - prescribing the maximum and minimum numbers of members (currently there is no provision in CWUMPO which requires a maximum number of members of a COI for certain winding-up procedures);
 - allowing body corporates to be members of a COI; and
 - removing the requirement for COI meetings every month – meetings can be scheduled as and when necessary.

In addition, there will be a prescribed form of statutory demand for use by a creditor to demand debt payment before seeking a winding up. This will help avoid disputes over the validity of a demand.

Where is the corporate supervision law?

Once the Amendment Ordinance takes effect, there will be one final outstanding piece in Hong Kong’s insolvency reform, namely, the introduction of a statutory corporate rescue procedure and insolvent trading provisions. The Financial Services Branch of the Financial Services and Treasury Bureau (“FSTB”) is in the process of drafting instructions for the amendment bill with a view to introducing an amendment bill for these additional processes into the Legislative Council by 2018.

Progress has been slower than many had hoped due to disparate views on the treatment of employee claims and the impact on secured creditors in the proposed out of court provisional supervision process. These and other issues are being actively addressed and the FSTB hopes to finalise this draft legislation by the end of this year. It is to be hoped that its passage to becoming law by 2018 will be smoother than the previous attempt to introduce corporate rescue law more than ten years ago, which was shelved in the face of intense lobbying from labour and creditor groups. The importance of both the corporate rescue law and the insolvent trading law (which, although less contentious than the corporate rescue law, has been linked to it and similarly delayed) cannot be underestimated. If Hong Kong is to lay claim to having a robust and complete corporate insolvency regime and to challenge Singapore’s recent aspirations to be the region’s “restructuring hub”, these additions to our insolvency laws are essential.

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