Standing Committee on Company Law Reform

The Thirty-Second Annual Report

2015 / 2016

Standing Committee on Company Law Reform (SCCLR)

Thirty-Second Annual Report

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PREFACE

(i)

Terms of Reference of the Standing Committee on Company Law Reform

(1) To advise the Financial Secretary on amendments to the Companies Ordinance and the Companies (Winding Up and Miscellaneous Provisions) Ordinance as and when experience shows them to be necessary.

(2) To report annually to the Financial Secretary on those amendments to the Companies Ordinance and the Companies (Winding Up and Miscellaneous Provisions) Ordinance that are under consideration from time to time by the Standing Committee.

(3) To advise the Financial Secretary on amendments required to the Securities and Futures Ordinance on matters relating to corporate governance and shareholders' protection.

(ii)

Membership of the Standing Committee for 2015/2016

Chairman : Mr John SCOTT, S.C.

Members : Mr Bruno ARBOIT
Mr Stephen BIRKETT (up to 31.01.2016)
Ms Bonnie CHAN Yiting
Mr Rock CHEN Chung-nin, B.B.S., J.P. (up to 31.01.2016)
Professor David DONALD
Ms Roxanne ISMAIL, S.C.
Mr David KIDD
Mr Rainier LAM Hok-chung
Mr Robert LEE Wai-wang (from 01.02.2016)
Professor John LOWRY
Dr Lewis LUK Tei, J.P.
Mr Kenneth NG Sing-yip
Mr Keith POGSON

	Dr. Kelvin WONG Tin-yau, J.P.	(up to 31.01.2016)
	Mrs Natalia SENG SZE Ka-mee	(from 01.02.2016)
	Ms Cynthia TANG Yuen-shun	(from 01.02.2016)
	Ms Benita YU Ka-po	
	Ms Wendy YUNG Wen-yee	

Ex-Officio Members :

Mr David GRAHAM
Chief Regulatory Officer and Head of Listing
Hong Kong Exchanges and Clearing Limited

Mr Stefan GANNON, J.P.
General Counsel
Hong Kong Monetary Authority

Mr Andrew YOUNG
Chief Counsel, Legal Services Division
Securities and Futures Commission

Ms Ada CHUNG, J.P.
Registrar of Companies

Ms Teresa WONG, J.P.
Official Receiver

Mr Patrick HO, J.P.
Deputy Secretary for Financial Services and the Treasury (Financial Services)

Dr Stefan LO
Senior Assistant Law Officer (Civil Law) (Ag.)
Department of Justice

Secretary	:	Mrs Karen HO	(up to 13.10.2015)
		Mr Joseph HUI	(from 14.10.2015 to 30.11.2015)
		Ms Ellen CHAN	(from 01.12.2015)

(iii)

Meeting held during 2015/2016

Two Hundred and Twenty-Fifth Meeting	-	03.12.2015

(iv)

Information Papers circulated during 2015/2016

Legislative Proposal to introduce an Open-ended Fund Company Regime in Hong Kong	20.11.2015
Companies (Winding Up and Miscellaneous Provisions) (Amendment) Bill 2015	20.11.2015

(v)

Discussion Paper circulated during 2015/2016

Issues for further engagement on introduction of a statutory corporate rescue procedure and insolvent trading provisions	20.11.2015

REPORT

The Standing Committee on Company Law Reform ("SCCLR") was formed in 1984. It advises the Financial Secretary ("FS") on amendments to the Companies Ordinance (Chapter 622) ("CO") and the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32) ("CWUMPO") as well as on amendments to the Securities and Futures Ordinance (Chapter 571), on matters relating to corporate governance and shareholders' protection. The SCCLR reports annually to the FS through the Secretary for Financial Services and the Treasury on amendments that are under consideration.

2. The SCCLR received two information papers from the Government during the year on the legislative proposal to introduce an open-ended fund company regime in Hong Kong and the Companies (Winding Up and Miscellaneous Provisions) (Amendment) Bill 2015.

3. From 1 April 2015 to 31 March 2016, the SCCLR held one meeting and considered one discussion paper.

Discussion Paper on "Issues for further engagement on introduction of a statutory corporate rescue procedure and insolvent trading provisions"

Background

4. At the 225th meeting held on 3 December 2015, representatives from the Financial Services and the Treasury Bureau and the Official Receiver's Office presented the discussion paper: "Issues for further engagement on introduction of a statutory corporate rescue procedure and insolvent trading provisions".

5. Members were informed that after the last discussion at the SCCLR[1] in June 2014 on the package of detailed proposals on the new statutory corporate rescue procedure and the insolvent trading provisions, the Government had consulted the Panel on Financial Affairs of the Legislative Council ("FA Panel") as well as some relevant

[1] Please see the SCCLR Annual Report for the year 2014/15 which is available at the Companies Registry's website (www.cr.gov.hk/en/standing/docs/31anrep-e.pdf).

stakeholder groups. The SCCLR, FA Panel and stakeholder groups generally supported the legislative initiative and the relevant proposals. During the consultation, stakeholders drew the Government's attention to some specific issues which should be considered further. After deliberating on those issues, the Government wished to seek SCCLR members' views.

Discussion Outcomes

6. The Government consulted members on the issue of, where a company without any major secured creditor initiated a statutory corporate rescue procedure, whether a safeguard provision should be provided to the effect that during the provisional supervision, on the application of a creditor, the court may make an order for termination of the provisional supervision. For example, it was proposed that the court should be empowered to end the provisional supervision of a company if it was satisfied that the purpose of appointment of provisional supervisor was inconsistent with the statutory objectives of the provisional supervision. Members did not object to the proposed safeguard provision.

7. As regards the issue of whether the initiating party of a corporate rescue procedure should be required to seek consent of all holders of subsequent charges over the whole or substantially the whole of the assets of the company, the Government considered that so long as the charges qualified as being over the whole or substantially the whole of the company's undertaking, all those chargees should have the same legal rights to enforce their charges and therefore should be included within the definition of major secured creditors regardless of their priority. Members noted that other jurisdictions such as the UK and Australia also did not, in general, distinguish between the rights of successive qualifying chargees (equivalent to major secured creditors under the proposed Hong Kong regime) to appoint an administrator based on priority of the charges, and generally considered that the proposed approach of requiring the initiating party to seek the consent of all relevant subsequent charge holders was sensible.

8. Members were advised that the Government was re-considering whether the new corporate rescue procedure regime should be open to non-Hong Kong companies registered under the CO, noting that the existing corporate winding-up and scheme of arrangement regimes mainly applied to Hong Kong companies with an extension to cover non-Hong Kong companies only if the court is satisfied that it is appropriate in the particular circumstances to allow such companies to be wound up in Hong Kong or to enter into an arrangement under the CO. In addition, there would be an issue with respect to the range of decisions the final creditors' meeting of the provisional

supervision may make because the option for creditors of a Hong Kong company to resolve at such meeting to wind up the company voluntarily and thus converting the provisional supervision into a creditors' voluntary winding-up would not be available in those cases involving a non-Hong Kong company, as such companies may only be wound up by the court in the absence of any provision allowing them to be wound up voluntarily in Hong Kong.

9. Many members indicated preference for the proposed corporate rescue procedure regime to be applicable to non-Hong Kong companies which were substantially doing business or had creditors and assets in Hong Kong as well, so as to enable them to have the option of pursuing the statutory corporate rescue procedure if they are in financial difficulties. Members suggested that the Government should explore further whether there could be practical ways to address the relevant legal and operational concerns about extending the new regime to cover non-Hong Kong companies.

10. On the issue of liabilities of provisional supervisors when there was a change in the office holder, the Government briefed members that there had been feedback from relevant stakeholders that the liabilities of an outgoing provisional supervisor should be accorded a higher priority of indemnity over the future liabilities of the incoming provisional supervisor on the ground that in the absence of such provision, an outgoing provisional supervisor would tend to terminate all the contracts for which he was personally liable, in order to crystallise his liabilities at the time of leaving office. The Government explained that the present corporate rescue procedure proposal had already given the outgoing provisional supervisor a measure of protection that upon vacation of office, he could also seek to be indemnified out of the property in his custody. The outgoing provisional supervisor would also only be personally liable for claims in respect of a cause of action which arose during the period the provisional supervisor held office. Therefore, it would not be necessary to accord an outgoing provisional supervisor a higher priority of indemnity. Members did not object to the Government's proposal.

11. The meeting also discussed some technical proposals relating to the new statutory corporate rescue procedure regime. Members agreed with the Government's suggestion that mandatory set-off should be adopted for voting purposes at creditors' meetings as such set-off is also applied under the UK's administration regime and Hong Kong's corporate winding-up regime. In addition, members also supported the following: where a company entered into the corporate rescue procedure which was preceded by a winding-up (i.e. the preceding winding-up) and then the final creditors'

meeting resolved to end the corporate rescue procedure with voluntary winding-up (i.e. the subsequent winding-up), the commencement date of the subsequent winding-up would be the commencement date of the preceding winding-up, and in cases without the preceding winding-up, the commencement date of the winding-up proceeded after the corporate rescue procedure would be the commencement date of the corporate rescue procedure. As explained by the Government, the relating back of the commencement date would in effect give a correspondingly longer claw-back period for voidable transactions and would assist in safeguarding the interests of creditors.

12. In relation to the statutory defence in the insolvent trading provisions, members agreed with the Government that the scope of the statutory defence should be expanded to also cover the situation where the debt in question was incurred in the course of an "arrangement or compromise" under the CO or an informal workout, noting that these were different types of company restructuring procedures and possible measures for directors to take upon insolvency, alongside the proposed corporate rescue procedure.

13. On the questions of whether to provide a "safe harbour" for insolvent trading, members agreed that while it might offer more flexibility to directors for rescuing the company, it should only be available in clear and specified circumstances so as to minimize the risk of abuse and ensure the practical enforceability of the insolvent trading provisions. In general, members preferred an arrangement whereby the court had to be satisfied that the director in good faith believed that the company incurred a debt for returning the company to a state of solvency within a reasonable period of time and there were reasonable grounds for believing that the incurrence of the debt would benefit the company and that the company was likely to return to a state of solvency within a reasonable period of time.

14. The Government would take into account the views of the members and further engage relevant stakeholders on the above specific issues in preparing drafting instructions for the relevant bill.