

11 February 2010

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**By Fax (2869 4195) &
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Dear Sirs,

RE: **REVIEW OF CORPORATE RESCUE PROCEDURE LEGISLATIVE PROPOSALS – CONSULTATION PAPER (“THE PAPER”)**

We refer to the Paper published by the Financial Services and Treasury Bureau in October 2009. This letter serves as Gall & Lane's answers to the questions in the Paper. Gall & Lane is a specialist dispute resolution law firm with a strong contentious insolvency practice.

COMMENCEMENT OF PROVISIONAL SUPERVISION

1. **Question 1:**

Do you agree with the proposed procedural changes relating to initiation of provisional supervision in paragraph 2.4 to 2.6 above? If not please provide reasons and suggest alternatives.

Answer:

Yes. We agree with the proposed changes relating to initiation of provisional supervision in paragraphs 2.4 to 2.6 of the corporate rescue consultation paper.

2. **Question 2:**

Do you see any need for other changes to the initiation of provisional supervision, including who may initiate the procedure? If so, please elaborate on the suggested changes and reasons.

Answer:

We are of the view that creditors should also have the right to initiate provisional supervision, similar to jurisdictions such as the UK, Australia and Singapore. However, we recommend

that a creditor-initiated provisional supervision can only occur by order of the Court upon application by the creditor.

3. Question 3:

Do you agree that the notice of appointment of provisional supervisor should be published in the local newspapers on the same day as the date on which the last document is filed with the Registrar of Companies? If you prefer additional or alternative means of publishing the notice of appointment, please describe and explain.

Answer:

We agree that the notice of appointment of provisional supervisor should be published in the local newspapers on the same day on which the last document is filed with the Registrar of Companies. There should also be on-line access to the list of companies on government websites, such as the Companies Registry and/or the Official Receiver's Office.

MORATORIUM

4. Question 4:

Do you support an initial moratorium period of 45 days? If not, please suggest alternatives and explain.

Answer:

We are of the view that the moratorium period should be extended to 60 days (instead of 45 days). The proposed period of 45 days may be too short, especially with respect to larger companies where a more complex restructuring may be necessary.

5. Question 5:

Do you support the proposal to allow for extension of the moratorium up to a maximum period of six months from the commencement of provisional supervision, subject to approval by the creditors at a meeting of creditors? If not please explain and suggest alternatives.

Answer:

Yes, we support an extension of the moratorium period of six months from the commencement of provisional supervision, subject to approval by the creditors at a meeting of creditors.

6. Question 6:

Do you agree with the proposal to allow for extension of the moratorium up to a maximum period of six months only upon court approval? If not, please explain.

Answer:

We are of the view that any further extension of the moratorium beyond 6 months should be subject to Court's approval.

7. Question 7:

If your answer to Question 6 is yes, do you agree that any court extension should not exceed a maximum of 12 months from the commencement of provisional supervision? If not please explain and suggest alternatives.

Answer:

No. We are of the view that any extension of the moratorium beyond 12 months should be subject to Court's approval.

8. Question 8:

Does the list of contracts and agreements which should be exempted from the moratorium, as set out at Appendix, need to be revised? If so, please suggest and explain.

Answer:

We do not have any further comments regarding the list set out at the Appendix.

EMPLOYEES

9. Question 9:

Which of the above three options (namely, the 2003 Proposal, Alternative A or Alternative B) would you prefer? Please explain. If you have any suggestion to refine any of the above three options, please describe and explain. If you prefer another alternative, please describe and explain.

Answer:

We prefer Alternative B.

If the original proposal in 2003 is adopted, this approach would unnecessarily restrict the use of provisional supervision, as a company in financial distress may have difficulty in finding sufficient cash to settle the employees' outstanding claims, even though the amount is capped.

If Alternative A is adopted, the whole corporate rescue scheme may be jeopardised by a disgruntled employee.

Alternative B strikes a balance between the interests of the employees and the company in distress.

10. Question 10:

Independent of which of the above options is adopted, what are your views on the treatment of outstanding employers' MPF scheme contributions?

Answer:

MPF scheme contributions should be bundled into "employees' other entitlements." The amounts payable are fixed up to a maximum of HK\$1,000 (per month) and paid within 12 months of the implementation of the corporate rescue regime. This way claims can be resolved with a level of certainty.

PROVISIONAL SUPERVISOR

11. Question 11:

Do you agree with the proposal that solicitors holding a practicing certificate issued under the Legal Practitioners Ordinance (Cap 159) and certified public accountants registered in accordance with the Professional Accountants Ordinance (Cap 50) may take up appointment as provisional supervisors?

Answer:

We are of the view that only accountants (and not lawyers) may take up appointment as provisional supervisors. This is because the work conducted by the provisional supervisor during a restructuring process (such as preparation of a statement of affairs, review of the company's books and record, administration of the company in distress etc.) usually involves extensive accounting experience. Accountants with HKICPA-approved qualifications level with requisite experience will be better candidates to act as provisional supervisor of a company than lawyers during the restructuring process.

12. Question 12:

Do you think that other persons without the above qualifications could also be appointed as provisional supervisors on a case-by-case basis? If so, should such an appointment be made by the OR or the Court? Please elaborate, in particular on the appeal channel in case of aggrieved applicants and on the associated investigatory and disciplinary regime in case of complaints against appointed persons.

Answer:

We are of the view that a licensing system for the appointment of provisional supervisors should be introduced to Hong Kong. Restructuring specialists from other jurisdictions could be considered, i.e. those have prior experience of the role. One must remember that the role of provisional supervisor is new to Hong Kong and outside expertise may be required.

Our view is that professionals from other jurisdictions who has successfully completed the "Diploma in Insolvency" course conducted by the HKICPA or, alternatively, who have the requisite qualifications and experience recognised by the HKICPA may be considered to act as provisional supervisors in Hong Kong. The appointment must be approved by the Official Receiver's Office or the Court.

13. Question 13:

Do you agree with giving creditors the choice to replace the provisional supervisor appointed by the company or its directors or the provisional liquidators or liquidators of the company and approve the remuneration of the provisional supervisor at the first meeting of creditors to

be held within 10 working days from the commencement of provisional supervision? If not, please elaborate on the reasons and suggest alternatives.

Answer:

We are of the view that the creditors can decide the choice and remuneration of the provisional supervisor at the first meeting of creditors. However, any decision to approve remuneration that is higher than current scale fees must be unanimous. Otherwise, it should be approved by Court.

We suggest that creditors should also be able to make an urgent application to the Court any time after the commencement of the provisional supervision to replace the provisional supervisor appointed by the company or its directors. Such application must be supported by sufficient evidence and a good reason as to why the provisional supervisor should be replaced. Any replacement must be approved by Court.

14. Question 14:

Do you support imposing personal liability on provisional supervisors as proposed in paragraphs 5.14 to 5.17 above? If not, please suggest alternatives which would effectively address the issues set out under paragraphs 5.16 (a) to (c).

Answer:

We support the imposition of personal liability on provisional supervisors. The provisional supervisors should be free to obtain insurance cover, subject to his indemnity against the company's assets.

INSOLVENT TRADING

15. Question 15:

Do you support the introduction of insolvent trading provisions? In case you do not, please explain and suggest alternatives to (a) encourage timely initiation of provisional supervision; and (b) deter irresponsible depletion of the company's assets.

Answer:

Yes, we strongly support the introduction of insolvent trading provisions. Given the difficulties in establishing what "a responsible person" has been, an alternative is to adopt the "dishonest" test under section 275 of the Companies Ordinance.

16. Question 16:

Do you agree with the proposed revised formulation of "insolvent trading"? If not, please suggest alternatives.

Answer:

Yes. We agree with the proposed revised formulation of "insolvent trading". As is the case in Australia, we also suggest that the "insolvent trading" provisions be extended to the

holding company of a subsidiary who has the control over the management of the subsidiary's affairs.

SECURED CREDITORS

17. Question 17:

Do you agree with the way that "major secured creditors" was defined in the 2001 Bill? If you think any changes are needed, please elaborate and explain.

Answer:

We agree with the definition of "major secured creditors" in the 2001 Bill.

18. Question 18:

Do you support the proposal to largely follow the 2001 Bill approach with respect to protection of "major secured creditors" and other secured credits' rights? If you think any changes are needed, please elaborate and explain.

Answer:

Major secured creditors should be protected. However, the provisional supervisor must have a means of checking whether major secured creditors that are or are connected to the shareholders, directors, officers and/or senior management of the company hold valid security and not a product of any fraudulent or insolvent trading. Creditors that are connected to the running of the company therefore should be bound by a moratorium in the same way as unsecured creditors.

VOTING AT MEETING OF CREDITORS

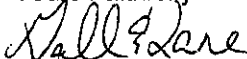
19. Question 19:

What are your views on retaining or removing the "headcount test" in the voting at meetings of creditors (i.e. requirement (a) stated in paragraphs 8.1 and 8.2 above) for resolutions to be passed at meetings of creditors?

Answer:

We consider that the headcount test should be removed. We agree with the suggestions set out in the Paper, in that some creditors may assign their debts to a number of nominees in order to affect the outcome of vote required by the "headcount test" in order to manipulate the results to their satisfaction.

Yours Faithfully



GALL & LANE

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