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7 August 2020

Mr Christopher Hui Ching-yu, JP
Secretary for Financial Services & the Treasury
Financial Services and the Treasury Bureau
24/F, Central Government Offices
2 Tim Mei Avenue, Tamar
Hong Kong

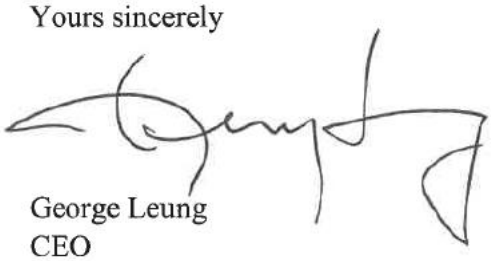
Dear Mr Hui

The Hong Kong General Chamber of Commerce is pleased to submit our views in response to the government's latest proposals to introduce a statutory corporate rescue procedure and insolvent trading provisions in Hong Kong.

Given today's difficult operating conditions, we believe there is a pressing need to provide companies in financial difficulties with an alternative to liquidation. The latest proposals are therefore very timely, and if passed, could also save jobs and put our economy on more solid footing in weathering future challenges.

We hope you will find our comments useful and look forward to the government's final proposals in due course.

Yours sincerely



George Leung
CEO

Encl.

cc: Mr Billy Au, Principal Assistant Secretary (Financial Services), Financial Services Branch, Financial Services and the Treasury Bureau

Financial Services and the Treasury Bureau's "Companies (Corporate Rescue) Bill Proposals" (June 2020)

Response by The Hong Kong General Chamber of Commerce (HKGCC)

HKGCC welcomes this opportunity to comment on the Government's latest proposals to introduce a statutory corporate rescue procedure (CRP) and insolvent trading provisions in Hong Kong.

As we stated in our submission to the Government on 12 February 2012, in response to the Government's earlier proposals on this matter, a CRP would provide a useful option for companies that would otherwise resort to liquidation proceedings, resulting in a loss of jobs which might have been saved, and substantially reducing the amounts which banks and creditors could otherwise recover in due course.

In today's difficult and challenging economic environment, the need for a CRP is particularly pressing, and the latest proposals are therefore very timely.

We set out below our comments to the proposals, as summarised in the Bureau's paper of June 2020. We look forward to having the opportunity to review the full text of the legislative proposals in due course. Our comments below are therefore subject to any views we may have on the full text.

1. Regarding the **objects of CRP**, in paragraph 4, we suggest that the wording of object (a) be amended to read "*to maximise the chances of a company that is or is likely to become insolvent, or as much as possible of its business, continuing in existence as a going concern*".

2. Paragraph 6 states that prior written consent of the major secured creditor (MSC) is required for **initiating provisional supervision**. The feedback we have received from members is that (a) in urgent situations, rather than waiting until the MSC gives its consent, a certain time period should be specified for the MSC to object to the proposal to initiate provisional supervision, failing which the proposal is deemed to be accepted (b) the MSC be allowed to initiate provisional supervision (c) appointment of the provisional supervisor (PS) be subject to the MSC's consent; and (d) in the case of a company without a MSC, although the proposal provides that no prior consent from any creditors should be required, consideration should be

given to unsecured creditors' input into the initiation of the provisional supervision and the selection of a provisional supervisor ("PS"). This is because many companies in Hong Kong are financed by a limited number of banks on an unsecured basis and their input should not be excluded in this process.

3. In the **definition of MSC** referred to in footnote 6 on page 3, it would be useful to define what is meant by "substantially the whole of the company's property". For example, would this be 90 per cent in value of the company's property? We have received mixed views from members on whether MSC should be defined to exclude creditors lower than the second-ranking charge. Those who agree with such an exclusion are of the view that such holders are unlikely to be able to enforce their charges in instances where there are insufficient company assets, and therefore have no real economic interest in the company's property. An exclusion would therefore help avoid a CRP slowdown by carving out those creditors that do not have a reasonable prospect of enforcing their charge from standing in the way of provisional supervision. In contrast, those who agree with such an exclusion believe that the definition of MSC should include the holders of security or quasi security that when taken together constitutes "the whole, or substantially the whole, of the company's property".

4. Regarding **voting at creditors' meetings** (referred to for example at paragraphs 7 and 10) it would be useful to clarify who can vote at such meetings. For example, does it include the MSC? In addition, we suggest that the appropriate threshold be specified for votes to be passed at such meetings. To reconcile the interests of larger creditors, smaller creditors and the company, as well as ensuring that the whole process is expeditious, we suggest that a vote would be deemed as being passed if (a) more than 66.66 per cent of the total value of creditors vote in favour of the resolution, and (b) not more than 50 per cent of the total value of creditors (who are not connected with the company) vote against the resolution.

5. Regarding **qualification to be a provisional supervisor ("PS")** (paragraph 11), we support the Law Reform Commission's recommendation that a panel comprising persons with the suitable expertise, experience and resources ("the suitability criteria") be set up and operated by the Official Receiver. The panel could comprise solicitors holding a practising certificate under the Legal

Practitioners Ordinance (Cap 159) and certified public accountants registered in accordance with the Professional Accountants Ordinance (Cap 50)- provided that they meet the suitability criteria. (For example, such suitability could be evidenced by possession of the HKICPA's Specialist Qualification and Designation in Insolvency). Persons other than solicitors and accountants might also be eligible for appointment if they can demonstrate that they meet the suitability criteria. As a starting point, those who are already on the panel of insolvency practitioners for the winding-up of companies by the court could automatically become members of the provisional supervision panel.

6. Regarding the **powers of the PS** (paragraphs 11 to 14) we suggest that an additional specific power be inserted, namely the power to apply to the court to set aside onerous contracts entered into by the company with associated persons within a certain period of time prior to the commencement of the provisional supervision (for example, six months). In addition, the Bill should contain anti-avoidance provisions to deter those responsible from entering into such contracts on behalf of the company.

7. Our members' views differ on the question of whether it is appropriate or necessary to impose **statutory personal liability on a PS**, as an additional obligation on top of the personal liability that the PS would have to assume under the common law in any event (paragraph 15). On the one hand, it was suggested that such an imposition proposed by the Government on a PS is needed, although there should be a grace period of, say, 14 business days before personal liability is attached to the PS. On the other hand, it was felt that statutory personal liability was unnecessary, and that such a requirement could deter suitable potential candidates from taking up a PS position and therefore interfere with the effective conduct of a provisional supervision.

8. There are also divergent views on paragraph 16, where it is proposed that PS should have the right to be indemnified out of the company's assets for any such personal liability, remuneration and expenses, in priority over the company's unsecured debts and those secured by floating charges. Those who do not agree with giving priority to indemnifying PS in this manner have suggested that this would be contrary to traditional rights of security. It was also suggested that there should be measures in place to scrutinize the PS's costs, such as the PS's costs will be subject to creditors' approval, pending further clarification on this point by the Government. Those supporting the

proposal have suggested that the exceptions to the right of indemnity should be clearly specified. In addition, it was suggested that where there was a change in PS, and given that the company may have insufficient assets to indemnify each PS, there should be a clear statutory priority of indemnities for each PS. In that connection, the Bill should provide that the first PS should be indemnified in full in priority over the second PS, the second over the third, and so on.

9. Regarding **the powers of the court** by way of safeguard measures (paragraph 37), we suggest adding a power of the court, on application by a creditor or group of creditors, to remove and replace a PS, if a conflict of interest arises or they have reasonable grounds for concern as to how the provisional supervision is being conducted.

10. Regarding the statutory defences in the **insolvent trading provisions,** paragraph 40 proposes (at (b)(i)) *good faith* as a defence by a director or directors for debt incurred by the company for the purposes of returning the same to a state of insolvency within a reasonable period. Since good faith is a wide and somewhat subjective concept, we suggest that the Bill includes a list of indicative factors that the court may take into account in determining whether the director(s) has/have acted in good faith.

We hope that these comments are useful, and look forward to having the opportunity to review and comment on the full text of the legislative proposals.

HKGCC Secretariat
August 2020