

A Procedural Guide to Creditors' Voluntary Liquidation in Hong Kong



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How the Process Starts

A creditors' voluntary liquidation (CVL) usually commences when the directors of the company realise that the company is insolvent and is unable to trade out of its financial difficulties. At this point, the directors take steps to convene meetings of shareholders and creditors.

The directors will usually appoint an Insolvency Practitioner (IP) to assist them in complying with the statutory obligations associated with the convening of the meetings. These include ensuring that all creditors and shareholders are notified of the meetings within the statutory time limits, statutory adverts are correctly placed, and documents are filed with the Companies Registry as necessary. The IP will also assist in ensuring that the meetings run as smoothly as possible.

Shareholders must be given at least 14 days notice of the general meeting (GM) at which a resolution to wind up the company is to be considered. Creditors must be given at least seven days notice of the meeting of creditors. In practice, both meetings are usually held on the same day. If 95 percent or more of the shareholders agree, the GM can be held at less than 14 days notice. This is called a Short Notice.

S.228A Liquidation

The situation sometimes arises where, in order to protect the assets of the company from being dissipated, it is necessary to appoint a liquidator to take office immediately. The person appointed is known as a provisional liquidator and is appointed pursuant to S.228A of the Companies (Winding Up and Miscellaneous Provisions) Ordinance. This appointment is made by the directors of the company, and can be without reference to the shareholders. It is then necessary for the meetings of creditors and shareholders to be held within 28 days of the provisional liquidator's appointment.

The purpose behind taking this course of action is to take steps to safeguard the assets of the company and to avoid them being dissipated in the period between the convening and holding of the meetings of creditors and shareholders.

Meeting of Shareholders

The meeting of shareholders is held first at which resolutions are considered to wind up the company and to appoint liquidators. A majority of 75 percent of shareholders present and/or represented at the meeting is needed to pass the special resolution to wind up. The appointment of the liquidator is by simple majority voting.

Meeting of Creditors

Immediately after the meeting of shareholders is the meeting of creditors. At this meeting the creditors have the opportunity to either confirm the shareholders' nominee as liquidator or alternatively to appoint a liquidator of their own choosing.

Voting is by simple majority based on the value of the creditors' claims admitted to vote at the meeting.

In order to be entitled to vote at the meeting of creditors, a creditor must have filed a claim and a proxy form no later than 4pm on the day before the meeting of creditors. A proxy form is not required if the creditor is an individual and is attending in person.

Committee of Inspection

A Committee of Inspection is a representative body of creditors and sometimes shareholders. Its role is to assist and advise the liquidator in undertaking his duties. It comprises of a minimum of three and a maximum of seven creditors and is appointed at the meeting of creditors.

The Committee is required to meet every month. However, in practice it usually meets either at the request of the liquidator or at the request of one or more members of the Committee. One of the roles of the Committee is to agree the liquidator's remuneration.

A separate guide outlining the role of the Committee is available at www.briscoewong.com.

Role of the Liquidator

The role of the liquidator is to realise the assets of the company, distribute the proceeds to the creditors in accordance with their statutory priority, and to investigate the circumstances surrounding the failure of the company.

Realisation of Assets

The liquidator's job is to realise the assets for the best possible price. It does not necessarily mean that the liquidator must sell the assets of the company immediately following his appointment, but it is often the case that assets can deteriorate in value if they are not disposed of on a timely basis.

Priority of Claims

Preferential Creditors

Certain creditors, i.e. employees and certain government departments, enjoy a priority in respect of their claims against the company. Employees' claims are preferential to the extent of all accrued holiday pay, arrears of wages (HK\$8,000), pay in lieu of notice (HK\$2,000) and severance pay (HK\$8,000).

Employees are also entitled to apply to the Protection of Wages on Insolvency Fund Board ("PWIFB") for an ex-gratia payment, if their employer goes into liquidation. The maximum amounts which will be paid by the PWIFB are HK\$80,000 for arrears of wages; HK\$26,000 for holiday pay; HK\$45,000 for pay in lieu of notice; and HK\$100,000 plus 50 percent of any amount in excess up to a maximum of HK\$245,000, for severance pay.

Secured Creditors

Secured creditors are those creditors who have a legal charge over assets of the company. This is usually a financial institution which has a charge over, for instance, land and buildings or plant and machinery.

The liquidator will investigate the validity of the security. If he is satisfied it is valid then the secured creditor is entitled to the proceeds from the sale of the assets up to and including the amount of capital and interest outstanding. Any surplus is paid over to the liquidator.

Unsecured Creditors

Once the preferential claims have been dealt with and the costs of the liquidation have been paid, the balance is then made available to the unsecured creditors whose claims are paid on a pari-passu basis.

Liquidator's Investigations

As part of his duties, the liquidator is required to investigate the circumstances leading to the failure of the company. In particular, the liquidator will investigate the following:

Unfair Preferences

An unfair preference occurs where a payment has been made to a creditor in the period leading up to the presentation of the petition. The effect of that payment is to put the recipient in a better position than other creditors when the liquidation starts.

The liquidator can investigate transactions which took place in the six months prior to the presentation of the petition to see whether any of them constitute unfair preferences. However, if the transaction involves a connected person i.e. someone who has a relationship with the company and/or its directors, the liquidator can go back as far as two years to overturn transactions of this nature.

Floating Charges

A floating charge is one which attaches to moveable classes of assets such as plant and machinery, stock, work in progress and accounts receivable. If a floating charge has been created within 12 months prior to the passing of the resolution to wind up the company, the liquidator will investigate whether or not it has been validly created. If a floating charge is created in favour of a person or party connected to the company, the liquidator will investigate the period up to two years prior to the commencement of liquidation.

It is often the case that floating charges are created but no money is advanced to the company. In such a case, the liquidator will seek to have the floating charge invalidated by the Court. However, if funds were advanced to the company in return for the creation of the floating charge, it is often the case that the charge is valid. In those circumstances, the floating charge holder is entitled to the proceeds of the disposal of the assets secured by the floating charge, but only after the claims of the preferential creditors have been paid.

Misfeasance

It is possible, in certain circumstances, for the liquidator to apply to the Court for an order that a director or shadow director be ordered to make a contribution to the assets of the company from their personal resources. This occurs where the liquidator is able to show that the party concerned has taken assets of the company and used them for his own purposes.

Sections 212, 286A, 286B, 286C Examinations

Sometimes, when a company goes into liquidation, some of the people associated with the company are unwilling to co-operate with the liquidator or assist him in undertaking his duties.

With that in mind, the liquidators have the power to obtain an order from the Court that directors, professional advisors such as auditors and solicitors and other people associated with the company, or who have knowledge of company's affairs, attend before the Court to be questioned on oath and to provide information relating to the company's affairs.

This is known as an examination and a person cannot refuse to answer questions on the grounds that he may incriminate himself.

This ability to bring uncooperative people before the Court is a power which is now being used more and more frequently by liquidators in Hong Kong. It is a way in which liquidators are able to obtain further information about the affairs of the company, which often leads to the realisation of further assets for the benefit of the company's creditors.

Conclusion of the Liquidation

Once the liquidator has realised all the assets, distributed the funds to creditors and completed his investigations, he will then convene final meetings of creditors and shareholders at which his final report is tabled. The liquidator then reports the outcome of the final meetings to the Registrar of Companies and ceases to act as liquidator. The company will then be dissolved and the liquidation process is complete.

The purpose of this guide is to provide a brief, plain English introduction to the Creditors' Voluntary Liquidation procedure in Hong Kong. It is not exhaustive and is not meant to be an alternative to legal or professional advice on specific issues. However, if you are in doubt regarding any of the matters raised in this guide please do not hesitate to contact us.

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