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December 2020

At Long Last: Hong Kong's Very Own Corporate Rescue Procedure

The idea of reforming Hong Kong's corporate rescue regime was first floated back in 1996. It was introduced in the form of the Companies (Corporate Rescue) Bill 2001 but got nowhere due to differences of opinion. This was returned to the table subsequently in 2003, 2009 and 2014, but nothing ever came to fruition.

On 2 November 2020, the Government tabled the Companies (Corporate Rescue) Bill (the "Bill") to formally implement a statutory corporate rescue procedure ("CRP") and insolvent trading provisions in Hong Kong. The Bill is expected to be presented to the Legislative Council in the first quarter of 2021, together with subsidiary legislation concerning the operational and logistical matters associated with the CRP (e.g. holding of creditors' meetings, organisation of committee of creditors etc.).

The Current Situation

In the absence of a statutory corporate rescue regime, distressed companies in Hong Kong have historically had very limited options to try to rescue themselves from going under. As the Bill acknowledges, such companies may either:-

1. Attempt to work out a non-statutory workout agreement with its major creditors to restructure its debts; or
2. Implement a scheme of arrangement under the current regime under the Companies Ordinance (Cap. 622) which facilitates a compromise between the company and its shareholders and creditors.

Schemes of arrangement, in particular, are procedurally cumbersome. However, the most notable, and at times fatal, drawback to the current options is that even if these options are implemented, there is nothing stopping the companies' creditors from taking legal action to wind the company up. Unlike the regimes for some other countries such as the United States, the current Hong Kong regime does not impose what is known as a "moratorium", which protects a company from being wound up while it attempts to rescue itself.

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The CRP

The proposed CRP is a procedure aiming to facilitate distressed companies' attempts to rescue themselves from insolvency by introducing a statutory process and moratorium. It is hoped that with statutory assistance, the prospects of the company being able to continue to trade as a going concern could be maximised. The following is an overview of the CRP as proposed by the Bill. The details may be subject to change after the Legislative Council's discussion.

Commencement of the CRP

The CRP is commenced upon the appointment of a Provisional Supervisor (the "PS"). The PS may be appointed by the following persons if they take the view that the company is insolvent or likely to become insolvent, and that provisional supervision is likely to assist the company or its creditors:-

1. The company itself (through a resolution of its members or directors); or
2. The company's liquidator or provisional liquidator, if the company has already entered into winding-up or is subject to a winding-up application.

If the company has major secured creditors ("MSC"), the MSC must be notified in writing of the company's intention to appoint a PS. The MSC will then be given 5 business days to object to the provisional supervision in writing, failing which the process may be initiated by the company.

The provisional supervision period will initially last 45 business days. With the consent of creditors, it may be extended up to 6 months. If the case is particularly complex and more time is needed to formulate a rescue plan, the company may bring an application to the Court for an extension of time lasting more than 6 months.

During the provisional supervision, the company is also placed into a moratorium. Some terms of the moratorium under the CRP include:-

1. No resolutions may be passed for the company to be wound up voluntarily. If voluntary winding up was already commenced, such process will be suspended.
2. No Court applications may be made to wind the company up, and if an application was already made, all proceedings will be suspended.
3. No Court proceedings (except criminal) may be commenced or continued without consent of the PS, or leave of the Court, unless otherwise permitted by the Bill.
4. No enforcement process in relation to the company's property may be commenced or continued without consent of the PS, or leave of the Court, unless otherwise permitted by the Bill.

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The PS

The PS will displace the directors and management of the company and will be vested with an array of powers. The PS must himself be an independent CPA or person qualified to act as a solicitor.

Importantly, the PS will gain control of the company's business, property and affairs, may dispose of or terminate any part of the company's business and property, and may perform any function the company or its officers could perform if the company were not under provisional supervision. These powers are all essential to enable the PS to consider options for rescuing the company and, where appropriate, prepare proposals for a voluntary arrangement ("VA") at the end of the provisional supervision period.

At the end of the Provisional Supervision

At the end of the Provisional Supervision, the PS is required to recommend for the creditors' consideration whether (1) the company should enter into a VA, (2) it should be wound up, or (3) the Provisional Supervision should end.

If a resolution is passed to approve a VA proposal, the company will enter into the VA. During that period, a moratorium also applies to the company to facilitate its restructuring and revival.

Observations

It is important to note that the moratorium under the CRP is Hong Kong-specific. In other words, creditors will be free to commence proceedings against the company in jurisdictions outside Hong Kong, and they may also look to enforce against the company's assets located outside Hong Kong. The terms of the CRP are to be discussed at the Legislative Council, but companies should be aware that they may have to take appropriate legal actions in other jurisdictions in which they have significant assets in parallel to entering into a CRP if they wish to be completely insulated from legal and enforcement actions.

It is still early days and the terms of the CRP are subject to change, but there is no doubt that it will be welcomed as a timely and useful relief for companies in these trying times.

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