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## Closing down an insolvent company without going to court

### Slotine explains the steps and stakeholders involved in creditors' voluntary winding-up and directors' voluntary winding-up in Hong Kong.

This is the last article in our series on winding-up in Hong Kong. It follows our first article on **compulsory winding-up** (by the court), available [here](#) and our second article on **members' voluntary winding-up and deregistration** (when the company is solvent), available [here](#).

When a private company limited by shares is insolvent, the usual routes to voluntary dissolution is creditors' voluntary winding-up. Despite its name, creditors' voluntary winding-up is actually initiated by the directors and approved by the members. Alternatively, if the members refuse to go ahead with members' voluntary winding-up and if court winding-up by the creditors is not viable, the directors can place the company in winding-up by following the directors' voluntary winding-up procedure.

### Creditors' voluntary winding-up

A board meeting is held at which the directors decide to place the company in winding-up and can also select an insolvency practitioner to act as provisional liquidator. The directors need to prepare an up-to-date statement of the financial position of the company (statement of affairs). The board must then convene a shareholders' meeting and a creditors' meeting, which are normally held on the same day.

The directors must present the statement of affairs to the shareholders. If the shareholders are satisfied that the company is insolvent, they need to approve the placement of the company into winding-up by a majority of at least 75%. The shareholders can confirm the directors' choice of liquidator or appoint a liquidator of their own and fix its remuneration. The creditors' meeting is usually held immediately after the shareholders' meeting and is chaired by a director. The creditors are presented with the statement of the company's affairs and they may appoint another liquidator (in which case their choice prevails). From that date, the liquidator takes over from the board. The powers of the directors cannot be exercised, unless if it is sanctioned by the liquidator or the shareholders. The members' and creditors' decisions to wind-up the company and appoint the liquidator are filed with the Companies Registry and published in the Gazette (delays are indicated in the chart below).

The liquidator has two missions which are (1) to realise the company's assets to pay the creditors and (2) to investigate the company's affairs in order to understand the circumstances which have led to insolvency. Once the company is fully wound up, the liquidator prepares an account of the winding-up specifying how the procedure has been conducted and presents the account to the shareholders. The liquidator sends a copy of the account and a return of the meeting to the Companies Registry. If there is no quorum at the meeting, the liquidator files a return that the meeting was duly summoned but that no quorum was present. The company is dissolved on the expiration of three months from the

date of registration of the account and return of the meeting with the Companies Registry. The costs and expenses of the winding-up, including the liquidator's fees, are paid out of the company's assets.

### **Directors' voluntary winding-up**

Hong Kong law also allows the directors to initiate a voluntary winding-up without the need to consult the shareholders on the commencement of the procedure. The procedure requires the directors to make a statement that the company cannot continue its business by reason of its liabilities and that it would not be reasonably practicable to wind up the company under another procedure. This procedure is a last resort measure that can only be used in circumstances where emergency makes it impossible or impracticable to convene an extraordinary general meeting to wind-up the company. It cannot be used by the directors to deprive the shareholders of the opportunity to decide the matter.

Under this procedure, the directors appoint the liquidator and convene shareholders' and creditors' meetings, after which the procedure is similar to a creditors' voluntary winding up. The creditors have the right to nominate another liquidator, in which case their choice will prevail.

The steps laid out in this article are by no means exhaustive but simply serve to bring clarity to the process of creditors' voluntary winding-up and directors' voluntary winding-up.



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## The steps involved in creditors' voluntary winding-up

### Board meeting

Directors approve the winding-up and convene shareholders' and creditors' meetings. Directors may also appoint an insolvency practitioner to act as liquidator.

### Creditors' meeting

*Convened with 7 days' notice*

A statement of the company's financial position is presented to creditors who may enquire about the company's affairs, shall appoint the liquidator (their choice prevails) and determine his remuneration and may appoint a committee of inspection.

### Realisation of assets and annual meeting

Realisation of company's assets and payment of creditors. If the winding-up continues for more than a year, the liquidator convenes a shareholders' meeting on the anniversary of the commencement of the winding-up to present an account of winding-up to the shareholders.

### Final meeting of shareholders

Final shareholders' meeting at which the liquidator presents the account of winding-up to the shareholders – showing how it has been conducted and how assets have been realised.

### Dissolution

*3 months after filing with Companies Registry*

Dissolution of the company.

### List of assets and liabilities

Directors establish that the company is insolvent, i.e. that it cannot meet balance sheet test (liabilities exceed assets) and commercial test (inability to pay debts as they fall due) based on up-to-date accounting records and financial statements.

### General meeting

*Convened with 21 days' notice*

A statement of the company's financial position is laid before the shareholders who approve the winding-up by special resolution (75% majority), appoint the liquidator and determine his remuneration (simple majority).

### Formalities

*Within 15 days of the general meeting*

Filing of the winding-up resolution and notice of appointment of liquidator with the Companies Registry and advertisement of notices of winding-up and appointment of liquidator in the Gazette.

### Notice of final meeting

*At least 1 month before the meeting*

Once the affairs of the company are fully wound up, the liquidator convenes a final shareholders' meeting by advertisement in the Gazette.

### Formalities

*Within 1 week of the final meeting*

Filing of a copy of the winding-up account and a return of the shareholders' meeting with the Companies Registry.



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## What happens after the creditors' voluntary winding-up process begins

The winding-up is considered to start on the date on which the shareholders pass the special resolution approving the winding-up of the company. From that date:

- The company must stop carrying on business, except as required for the benefit of the winding-up.
- Every invoice, purchase order or letter issued by the company must state that the company is being wound up.
- Any transfer of shares made without the sanction of the liquidator is void.
- The powers of the directors will end automatically upon the appointment of the liquidator, except if sanctioned by the liquidator or the shareholders in general meeting.

## Conversion of a members' voluntary winding-up into a creditors' voluntary winding-up

A members' voluntary winding-up (the steps and stakeholders of members' voluntary winding-up are set out in [this article](#)) will be converted into a creditors' voluntary winding-up where the liquidator is in the opinion that the company will not be able to pay its debts in full within the period stated in the certificate of solvency. The liquidator will summon a creditors' meeting within 28 days from the day on which he forms such opinion and lay before them a statement of affairs. The members' voluntary winding-up becomes a creditors' voluntary winding-up from the date of the creditors' meeting.



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## The stakeholders: roles and responsibilities

### CREDITORS

- Submit a proof of debt and documents substantiating their debts to the liquidator.
- Attend creditors' meetings provided that their proof of debt has been accepted by the liquidator.
- Vote at creditors' meetings by a majority in value of claims.
- Appoint the liquidator and determine his remuneration (in case of conflict with the shareholders' choice of liquidator, the creditors' choice usual prevails).
- Appoint a committee of inspection comprising 2-5 creditors to assist and supervise the liquidator (optional).
- Receive payment from the liquidator in accordance with their order of priority.

### SHAREHOLDERS

- Approve the placement of the company into winding-up by special resolution passed by a majority of at least 75% of voting rights.
- Appoint the liquidator and determine his remuneration by ordinary resolution passed by a simple majority of the voting rights (but the creditors' choice prevails).
- Sanction certain acts of the liquidators such as any payment of a class of creditors in full or the making of a compromise or arrangement or creditors.
- Attend an annual general meeting to be presented an account of the winding-up (if the winding-up continues for more than a year).
- Liable to pay any amount unpaid on their shares to the company (but no more).
- Receive any surplus available after payment of all the creditors, according to their respective shareholding, if the proceeds of the winding-up are sufficient.

### DIRECTORS

- Must maintain proper accounting records, prepare annual financial statements and lay them before the shareholders timely (among other general statutory and fiduciary duties).
- Prepare a statement of the company's affairs and a list of creditors and the estimated amount of each creditor's claim for presentation to the creditors.
- May be held liable for breach of duties, fraud or lack of fitness under the Companies Ordinance (Cap. 622) and for unfair preference, undervalue transactions, fraudulent trading and failure to keep proper books and records under the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap. 32) (CWUMPO).

### LIQUIDATORS

- Discretionarily accept or reject the proof of debt submitted by each creditor.
- Convene a general meeting on the anniversary of the commencement date of the winding-up to present an account of the winding-up to the shareholders.
- Realise the company's assets and distribute the proceeds to the creditors according to their order of priority.
- Investigate the company's and its directors' affairs.
- Convene a final general meeting to present the final account of the winding-up and send a copy to the Companies Registry for the company to be dissolved.
- May apply to Court for a restoration order in case of transaction at an undervalue or unfair preference, for personal contribution by the directors in case of fraudulence trading or misfeasance or for disqualification order against a director.



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## Special procedure where it is necessary to appoint a liquidator immediately

The CWUMPO contains a special procedure in case the directors consider it necessary to appoint a liquidator immediately to safeguard the assets of the company. Under this special procedure, the directors do not need to consult the shareholders and the creditors on the choice of liquidator. If the directors consider that it would not be reasonably practicable to wind it up under other routes, the steps to the company's dissolution are as follows:

- The directors pass board resolutions by simple majority resolving that (i) the company cannot continue its business by reason of its liabilities, (ii) they consider it necessary that the company be wound-up and that it would not be reasonably practicable to wind it up under other routes and (iii) meetings of the shareholders and creditors will be held within 28 days after the date of delivery of the winding-up statement to the Companies Registry.
- A winding-up statement specifying the reasons for which the directors consider it necessary that the company be wound-up and that it would not be reasonably practicable to wind it up under other routes is signed by one of the directors. If a director makes such statement without having reasonable grounds for believing so, he/she may be liable to a fine and imprisonment.
- The winding-up statement (form NW2) must be filed with the Companies Registry within 7 days of the date the board resolutions are passed.
- The winding-up procedure starts upon filing of the winding-up statement with the Companies Registry.
- The directors appoint an insolvency practitioner as provisional liquidator.
- The appointment of the provisional liquidator must be filed with the Companies Registry within 15 days.
- The start of the winding-up and the appointment of the provisional liquidator must be advertised in the Gazette within 15 days of the filing of the winding-up statement.
- Meetings of the creditors and shareholders must be held within 28 days after the date of filing of the winding-up statement.

Once the creditors' and shareholders' meetings have been held, the process is the same as a creditors' voluntary winding-up.



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## In focus: order of priority for payments made to creditors

During the winding-up procedure, any proceeds available must be distributed by the liquidator in the following order of priority:

1. costs relating to the preservation and realisation of the company's assets subject to a fixed charge;
2. debts owed to secured creditors who have a fixed charge over the assets of the company;
3. costs relating to the preservation and the realisation of the company's assets subject to a floating charge;
4. expenses of the liquidation, notably the liquidator's remuneration;
5. wages owed to employees;
6. debts due to the Hong Kong Government, notably any outstanding taxes;
7. debts owed to secured creditors who have a floating charge over the assets of the company;
8. debts owed to ordinary creditors; and
9. any surplus available to the shareholders.

In case the funds available are not sufficient to pay all the creditors of a given class in full, they must all be paid an equal proportion out of the proceeds available.

*The law in this respect is complex. The information provided in this article does not, and is not intended to, constitute legal advice and should not be relied upon as such.*

*For professional legal advice, please do not hesitate to contact us.*



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