HONG KONG SOCIETY OF ACCOUNTANTS
(Incorporated by the Professional Accountants Ordinance, Cap. 50)

香港會計師公會

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BY FAX AND BY POST
(2524 4860)

Your Ref.: L/M No. (7) to SC 101/16/28 30 June 2003
Our Ref.: C/IPC, M

Mr. Christopher C. Chan
Registrar,
Registrar's Chambers,
High Court,
38 Queensway,
Hong Kong

Dear Mr. Chan,

Taxation of the Bills of the Liquidators, Provisional Liquidators and their agents

Thank you for your letter of 30 April 2003 on the above subject, addressed to the Insolvency Interest Group (IIG). The IIG operates under the auspices of the Hong Kong Society of Accountants ("the Society") and this reply to you is therefore issued on behalf of the Society.

Before providing you with our observations on your letter and the attached guides, we note that a meeting is to be held during July at which taxing masters, representatives of the Official Receiver's Office and representatives of the Society will be present. Whilst the proposed meeting relates more specifically to the Panel A scheme and the associated fee scale, we believe that this would represent a timely opportunity to bring together these two matters for a fuller discussion and, hopefully, a satisfactory resolution of the surrounding issues.

Turning to guides, the Society supports the initiative from the High Court to issue procedural guides on the taxation of bills in a liquidation, and we appreciate the opportunity to comment on them. We hope that implementation of such guides will speed up the process of taxation and bring greater efficiency and certainty to the process.

You may wish to know that the Society has been working on the preparation of a standard format for liquidators' fee applications for some months, having regard to the information that the Court has previously indicated to be necessary and to similar formats that have been issued by insolvency bodies overseas, in particular in the United Kingdom. We have also been in correspondence with the Official Receiver ("OR") on this matter with a view to discussing the drafts with the Judiciary. In fact we understand that the OR may have already passed copies of draft formats to you. We have recently made some further adjustments to these and believe that, in terms of the information to be provided, the draft formats are largely consistent with the proposed procedural guides attached to your letter. We have therefore taken the liberty of appending to this reply copies of the latest draft formats for fee applications on which we would welcome your comments.

Our general comments on the proposed requirements and on the detailed provisions of the procedural guides are set out in the paragraphs below.

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A. General comments

(*References are to your letter dated 30 April 2003*)

Part I

The scope of the requirements

We believe that, in accordance with the existing practice, the guides, which relate to taxation/determination by the taxing masters, should not in the normal course be applicable, or at least not in their entirety, to provisional liquidators' fees, which are submitted to the Companies Judge for approval, nor to liquidators' fees as explained below.

Under section 196(2)(a) of the Companies Ordinance, a liquidator's remuneration, including, in our view, the basis and amount, is to be determined by agreement between the liquidator and the committee of inspection ("COI"). Under section 196(2A), if the OR is of the opinion that the remuneration of a liquidator as determined under subsection (2)(a) should be reviewed, the OR may apply to the Court, and the Court may make an order confirming, increasing or reducing the remuneration of the liquidator. It would seem to us, therefore, that if the liquidator and the COI have agreed on the liquidator's remuneration, both the basis and the amount, then, unless the OR makes an application to the Court under section 196(2A), no further approvals should be required in relation to that remuneration. This is also confirmed by the decision of Le Pichon J. in *Re Peregrine Investment Holdings Ltd (No.2)*. On the other hand, where there is no COI, or where no agreement has been reached between the liquidator and the COI, the Court is to decide on the matter (section 196(2)(b)), and the practice has generally been to seek approval from the Companies Judge.

While this is generally the assumption on which our comments are based, the intended scope of the guides does not seem to be entirely clear in this respect. Your letter suggests that, even if the costs (including, it would seem, the liquidator's remuneration) are not assessed by way of taxation, the same level of information will be required for the taxing master to make a determination. Furthermore, paragraph 3.1(C)(i) of the *Procedural Guide for the Taxation/Determination Bills of Provisional Liquidators or Liquidators* requires that one of the documents to be submitted should be a written confirmation as to whether a COI has been appointed and, if so, whether any agreement as to remuneration has been reached pursuant to s196(2)(a).

Under the circumstances we would appreciate your further clarification on this matter.

In your letter, you state that "[t]he word 'determine' can mean the process of gross sum assessment, fixing it with reference to percentage or taxation." (Presumably "percentage" here relates to a percentage of realisations?) However, for the reasons given above, we are not clear as to how and in what circumstances this process of determination would occur. We note that, for example, the provisions of Order 62, r.21 HK(4) of the Rules of the High Court, could provide for a form of "determination" in which the taxing master may "propose to allow" an amount, which may be queried by a person entitled to a hearing, following which an appointment to tax is made. However, this applies only to bills that do not exceed HK$100,000 and it appears to relate primarily to the bills and disbursements of agents. In addition, this provision does not

make it clear which other method of assessment might be applied, or the criteria to be used. It would be helpful therefore to be able to understand the Court's approach in this respect.

Having said this, it would seem to be reasonable and beneficial for all parties, from a practical point of view, to try to standardise, as far as possible, the nature and presentation of information provided to the Court in support of fee applications. Insofar as the guides concern these matters, therefore, we believe that they should be more generally applicable.

Part II

Procedure

The proposal to set up a special counter at the Registry for delivery of bills instead of having bills being sent together with other general correspondence to the Judiciary Administrator is a positive development that should help to reduce any delays.

We would suggest that the term "Notice of Appointment for Taxation" be used throughout the procedural guides rather than the shortened form of "Notice of Appointment". This is to avoid any possible confusion with the title of Form 28 "Notice of Appointment of Liquidators", which is often referred to as "Notice of Appointment" for short.

Part III

Documents

There appears to be an emphasis in the procedural guides on the requirement to provide documents and explanations relating to the recovery of assets. A liquidator is entitled to be remunerated for all necessary work conducted by him, including, for example, investigating into and reporting on the company and directors' conduct, conducting meetings, adjudicating creditors' claims, bookkeeping and dealing with uncooperative company officers and incomplete records. We suggest that this be clarified in a note in the guides.

As regards assets, reference is made only to assets as shown in the statement of affairs of the liquidation. Despite the requirements of the law, it is not uncommon for directors and officers to fail to submit a statement of affairs. Even for cases in which a statement of affairs is produced, the assets stated therein are often substantially different from those a liquidator recovers and realises. For example, recoveries and realisations from avoiding antecedent dispositions and preferences, or other actions, often take up a substantial portion of a liquidator's time and may result in significant realisations for the estate. We suggest that the procedural guides take into account these areas of a liquidator's work.

Source document

With respect to the formalities relating to the submission of the source document by the liquidator, we should like to know whether a letter or statement signed by the liquidator, attaching the document, would be sufficient for the purpose, or whether an affidavit or affirmation would be required.

Part IV

Attendance at taxation hearings

The guides suggest that there will be a taxation hearing for each and every bill submitted, and that someone may need to attend the hearing to answer questions raised by the court. We understand from practitioners that this is substantially different from the current practice. Presently, fees of provisional liquidators are submitted to the Court for approval, in almost all cases, without any physical hearing taking place. Fees of liquidators' agents, and where applicable, those of the liquidators, are submitted to the taxing master for taxation, and again, in almost all cases, without any physical hearing. Any queries that the Court or the taxing master may have are generally dealt with through correspondence. On the assumption that, once guidelines are in place, major queries are less likely to arise, a requirement for compulsory hearings may not be in the best interests of all parties.

Further, the guides also suggest that any representative present at a hearing should be familiarised with the bill and be able to answer queries raised by the taxing officer. In this connection, your clarification is requested on the following matters:

- the circumstances in which a representative will be expected to be present at the taxation hearing, assuming a representative is not required to attend in all cases;

- where a representative attends, whether this should ordinarily be the liquidator or liquidators, or whether a member of staff or an agent could attend on behalf of the liquidator or liquidators;

- whether the only pre-requisites for the representative who attends a hearing are familiarity with the bill and a capacity to be able to answer queries raised by the taxing officer, or whether there are any other formal requirements (e.g. that the representative should be, if not the liquidator, then a qualified solicitor); and

- whether the cost of attending the hearing is a recoverable cost, bearing in mind that providing a representative of an appropriate level at the hearing could be costly.

In our view, the critieria for any representative to be able attend should be that he/she is familiar with the bill and be able to answer any queries that are raised. It should not be necessary for the liquidator to attend or for solicitors to be instructed to attend (although they may need to attend taxation hearings on their own bills). If this is the intention of the guide, perhaps it could be clarified in a note.

B. The detailed provisions of the procedural guides

Our comments on the detailed provisions of the procedural guides are set out below.

Paragraph 3.1(B)(i)

Wherever possible, orders for the appointment of provisional liquidators should make clear provision for the basis of remuneration. If that is not possible, an order as to the calculation of remuneration should be made as soon as possible after the appointment of provisional liquidators.

Paragraph 3.1(B)(ii)

While the new procedural guides should help to streamline and expedite the process of taxation in the future, we request clarification as to the status of bills submitted before the implementation of the new procedures. In particular, we should like to know whether any specific measures will be taken to clear the existing backlog, such as appointing additional masters or allowing the current masters to set aside additional time to complete the outstanding taxations.

If no specific steps are to be taken, there is a danger that while new bills will be dealt with more efficiently by all parties, the backlog of outstanding bills will remain "on the back burner" and will not disposed of in the near future.

Paragraph 3.1(C)(i)

Please see our comments above under the heading *The scope of the requirements* in the "General comments" section of this reply.

Paragraph 3.1(C)(ii)

We support the requirement to include a "brief running narrative". Ideally, the emphasis on the value of assets recovered will lead to the Court adopting a proportionate approach to the verification process. However, we do not consider that a simple "results-based" approach (i.e. no realisations, no fee) should be adopted in view of the work that liquidators are required to perform, which includes duties that are not directly related to asset realisation, as explained above.

We believe that some of the difficulty with the present system arises from the requirement to produce very detailed information (e.g. narratives on the basis of 6-minute intervals and timesheets), even where the cost of doing so is disproportionate to the level of assets and fees and the likely return to creditors.

We believe, therefore, that if the proposal is for court examination of most of the expenses incurred by a liquidator and provisional liquidator, then this is too onerous. We would suggest instead that, in cases where the total amount claimed does not exceed, say, HK$100,000, there should be a more limited, "summary" application of the requirements.

Paragraph 4.1

It is stated in this paragraph 4.1:

"After the documents in paragraph 3 have been lodged, the Listing Officer shall designate a hearing time for the taxation/determination of the bill lodged".

We should to know how the Court will decide upon the time required for the process. If only a short time is allocated, or if the matter cannot be resolved at the first hearing. this may well result in adjournments. Given the pressures being faced by the Court, the adjourned date may be a long time into the future, thus creating both a backlog and further delays in the agreement of remuneration claims.

At present liquidators attend a "call over" at which the taxing master will often try to persuade them to accept a figure in full settlement of the bill to be taxed. This aspect of the current procedure seems to be missing from the guide which envisages going straight to a taxation hearing; that is, unless the reference in paragraph 4.1 to the possibility of "determination" at the hearing is intended to refer to this process and is the equivalent of "assessment" or "allowance". If so, then it would be necessary to be represented at the hearing by someone who is both familiar with the case and file and who can represent the firm.

Paragraph 5.1

Currently, taxation fees are payable only in respect of taxation of costs and expenses as required under r.169 to 177 of the Companies (Winding-up) Rules and are not, for example, payable to the Court in respect of an application under section 196 of the Companies Ordinance for approval of the liquidator's or provisional liquidator's remuneration. We are unclear, therefore, as to what is intended by the references to fees in paragraph 5.1. This question is also related to the issue of the scope of the guide, raised above in the "General comments" section of this reply. However, extending the requirement to pay taxing fees will in principle reduce the amount of funds available for distribution to creditors and, in this respect, it will not be to the benefit of creditors (particularly if this were to be extended to situations in which the remuneration has already been approved by the COI).

Agents' Bills

A number of our comments on liquidators' bills would also apply to the bills of liquidators' agents.

We would appreciate clarification as to the requirement for evidence of scrutiny of the bills of agents by the liquidator. When a liquidator submits bills of his agents, he has to confirm that he approves the bills. We would suggest that it should not also be necessary for liquidators, as professionals and officers of the Court, to be required to provide specific evidence of scrutiny in each and every case in addition to providing a certificate of scrutiny. The liquidator has to use his professional judgment in assessing whether the fees charged for work done by his agents are reasonable in the context of the liquidation administration. Certainly, if asked by the Court, the liquidator should be prepared to substantiate the basis of his concluding that the fees are reasonable. By way of analogy, when auditors present their audit report to the members of a company

at a general meeting, giving their audit opinion, they are not required to supplement the audit report with their working files as evidence to support their opinion.

C. Other matters

Guidance on payments on account

Given the backlog of outstanding invoices, even with the new procedures in place, bills subject to taxation will take time to be paid. We know that demands on cash flow and debt provisions can result from these delays. Payment on account, as of right, of a substantial proportion of the outstanding fees would help to alleviate the problem. Accordingly, we suggest that consideration be given to incorporating appropriate provisions on payments on account into the procedural guides.

Given that one of the objectives of the exrcise is to make the process of taxation more efficient, we would welcome some indication from the Court as to how long it would ordinarily be expected to take for a bill complying with all the requirements of the procedural guides to be approved, and for the liquidator to be notified accordingly.

Preparation of bills for taxation

We should like to clarify the position as regards the cost of preparing bills for taxation. Is it intended that this should be recoverable?

Effective date

We would like to know the proposed date for bringing the procedural guides into effect.

Proposed changes to the law

The requirement that bills exceeding $3,000 in the aggregate must be taxed means in practice that the procedure applies to the vast majority of cases, taking into account the costs incurred on compulsory advertisements in the Gazette and newspapers, etc., even for relatively small amounts of money. We believe that the figure of $3000 needs to be updated and, furthermore, in view of the power of determination given to a COI under section 196(2)(a), that the COI should also be given greater authority to approve disbursements together with the liquidator's remuneration. Approval from the Court should be required only where no COI exists, where approval has not been obtained from the COI, or where the OR, pursuant to s196(2A), considers that a review is called for.

Our position, therefore, is that in principle a COI should be given express authority to approve costs that are currently required to be taxed (including those of agents, solicitors, accountants, etc). We appreciate that this proposal may be beyond the scope of the present exercise as it would require a change in the law and further consultation. However, it would be a more straightforward change, in the meanwhile, to increase the threshold for taxation, under r.176 of the Companies (Winding-up) Rules, from $3,000 to, say, $20,000. We believe that this should be done in order to bring the provision more up-to-date. Both of these proposals, we believe, would help to reduce unnecessary demands on the Court in terms of time and resources.

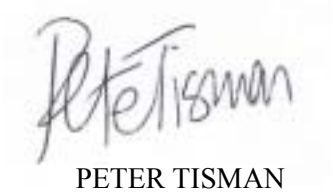
Cost and benefit of approval process

While the Society is cognisant of the legal requirements for various fees, costs, disbursements and expenses in a compulsory liquidation to be approved or sanctioned by the Court, we are also conscious of the requirement, and the commercial demands, upon practitioners, to maximise benefits to the creditors in insolvency administrations, and to do so in a timely manner. In this regard, we understand the concern expressed by practitioners that liquidators are sometimes required to spend a disproportionate amount of time and resources in the process of having their fees and disbursements approved, in situations where, in practice, the claims in question may involve only small amounts of money, either in absolute terms or relative to the size of the estate. The feedback from our members who are insolvency practitioners suggests that in most liquidation cases creditors generally accept and are agreeable to the remuneration charged.

We would hope, therefore, that the procedural guides will help to streamline and alleviate the delays in the approval process.

We trust that you will find our comments to be constructive. As indicated at the beginning of this letter, we hope that we will also be able to discuss some of our concerns on this subject when we meet you in July. Meanwhile, if you have any comments or questions, please feel free to contact me on 2287 7084.

Yours sincerely,



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c.c. Official Receiver (Attn. Mr. Eamonn O'Connell)

Appendix