

## **Statutory Investigation into the Affairs of an Insolvent Company Wound-Up by the Court**

The liquidator of an insolvent company is under a duty to carry out statutory investigation of the affairs of a company wound-up by the Court.

The purpose of an investigation is to determine the assets and liabilities of the company and to review the conduct, decisions and actions of the directors. If, during the course of the investigation any apparent right of action comes to light, the liquidator should determine, if necessary with the benefit of legal advice, whether or not any particular action can be taken.

The extent and nature of the investigation work will vary from company to company but should include the following -

### PROCEDURE

#### 1. Questioning the management

At the outset of the winding up, all relevant directors, including directors who held office during the last three years, the company secretary and other senior officials should be questioned as to the company's affairs, including the reasons for failure. The onus is on the liquidator to consider carefully which directors (officers, former directors or shadow directors) are relevant having regard to their accessibility and the information which he believes they may have. The liquidator may also invite creditors to bring his notice to any particular matters which they consider require further investigation.

#### 2. Records

The records of the company covering the period since the date of the last audited financial statements should be examined to ensure that transactions in the final period of trading were made in the normal course of business.

#### 3. Validity of charges

Details of all security held by banks and other parties should be obtained and the liquidator should check registration and consider the possible invalidity of any charge. Where liquidation follows receivership, the validity of the receiver's appointment should also be assessed.

#### 4. Comparison of assets with last balance sheet

For the purposes of discovery of assets, the statement of affairs/supplementary affidavit(s) should be compared with the last audited financial statements. The liquidator should satisfy himself that material movements in fixed and current assets can be properly explained. Where no statement of affairs is provided, the most recent audited financial statements and management accounts should form the starting point for identifying assets owned by the company.

5. Trading losses

Consideration should be given to the preparation of a deficiency account, and possibly also trading, profit and loss accounts, in any case where there is a material difference between the deficiency disclosed in the statement of affairs/supplementary affidavit(s) and the last audited financial statements, after taking into account matters such as writing down asset values.

6. Transactions with persons connected with the company

The books and records of the company should be examined to ensure that any transactions with persons connected with the company were carried out at arm's length and material transactions should be examined in detail. Particular attention should be paid to transactions involving directors, including any reduction in loan accounts and/or reduction in overdrafts supported by personal guarantees. Repayment terms of director loans should be noted and any material acquisitions of assets by or disposals to directors and related parties (including any person connected with the company), or transactions which might constitute the giving of any unfair preference or transaction at an undervalue to that director or related party (including any person connected with the company) should be investigated in detail to determine whether the transactions occurred on commercial terms.

7. Statutory books

The statutory books of the company should be examined, together with the minute book, and compared with a search obtained from the Companies Registry. Particular attention should be given to the identity of directors who held office during the last three years.

8. Conduct of Directors/Offences

- (a) If the liquidator's investigation into the affairs of the company should reveal any offence by any past or present officer (or member) of the company, this should be reported to the Official Receiver ("OR"). The liquidator of a company is required to submit either a report or a return (known as a "Form D1" and "Form D2" respectively) to the OR, concerning the conduct of the directors of the company, within six months of appointment. The OR has issued the following memoranda elaborating on the requirements, ORO Circular No. 6/2014 – *Prosecution of Insolvency Offences* (supplemented by ORO Circular No. 5/2017 - *Prosecution of Insolvency Offences – Supplemental to ORO Circular No. 6 of 2014*) and Circular No. 6/2017 – *Disqualification of Directors*, and the liquidator should refer to these memoranda, any new memorandum on the same subject as well as amendment or supplement to the existing memoranda that may be issued by the ORO from time to time for detailed guidance in completing reports or returns.
- (b) In this respect, the liquidator shall give consent to the OR, as and when required to do so by the OR, for the purposes of any investigation of the company and/or its officers or members, to write directly to any organizations for obtaining information or records in relation to such company and/or its officers or members.

GENERAL

9. The liquidator's investigations into the affairs of the company should aim to identify any rights of action which the company or the liquidator may have against third parties, and the liquidator's attention is drawn to, inter alia, the following provisions:

Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32)

Sections 47A – 48*	Financial assistance
Section 121*	Failure to keep or preserve any books of accounts
Section 156*	Bankrupt acting as a director
Section 157J*	Criminal penalties for contravention of Section 157H (Prohibition of loans, etc., to directors and other persons)
Section 182	Avoidance of dispositions of property of the company after commencement of winding up
Section 190(5)#	Failure to comply with requirements under section 190
Sections 212-214	Uncalled capital
Section 265D#	Transactions at an undervalue (as defined in section 265E)
Section 266#	Unfair preferences (as defined in section 266A)
Sections 266/266B#	Fraudulent / unfair preferences
Section 271	Offences by officers of companies in liquidation
Section 272	Falsification of books
Section 273	Frauds by officers of companies which have gone into liquidation
Section 274#	Failure to keep proper records
Section 275	Fraudulent trading
Section 276#	Misfeasance and misapplication etc. of property
Section 277	Prosecution of delinquent officers and members

\* repealed but continue to apply by virtue of Schedule 11 to the Companies Ordinance (Cap. 622) or section 23 of the Interpretation and General Clauses Ordinance (Cap. 1) or both

# for the transitional and savings provisions regarding amendments made by the Companies (Winding Up and Miscellaneous Provisions) (Amendment) Ordinance 2016, see Schedule 26 to the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) or section 23 of the Interpretation and General Clauses Ordinance (Cap. 1) or both

Companies Ordinance (Cap. 622)

Sections 205-207, 274-275, 277-282, 286- 289	Financial assistance
Sections 373, 374, 377	Failure to keep or preserve accounting records
Section 480	Bankrupt acting as a director

Conveyancing and Property Ordinance (Cap. 219)

Section 60

Voidability of dispositions to defraud creditors

Consideration should also be given to whether any other rights of action are available, for example, in relation to the common law fiduciary duties of directors, breach of constructive trust, etc.

10. The liquidator should obtain the sanction of the Committee of Inspection or the Court in respect of any decision to bring or defend any action or other legal proceedings in the name of and on behalf of the company, which may be appropriate following the outcome of the above investigation work. This sanction is a statutory requirement in a compulsory winding up, and in all cases, the overriding consideration will be the likelihood of any tangible benefit to the creditors.
11. The liquidator should submit a preliminary report to the Court under section 191 of the Companies (Winding up and Miscellaneous Provisions) Ordinance (Cap. 32) -
  - (a) as to the amount of capital issued, subscribed, and paid up, and the estimated amount of assets and liabilities; and
  - (b) if the company has failed, as to the causes of failure; and
  - (c) whether in his opinion, further enquiry is desirable as to any matter relating to the promotion, formation or failure of the company, or the conduct of the business thereof.