

A Guide on Employee's Rights in

Bankruptcy, Winding-up and Receivership



Labour Department

Foreword

When an employer becomes insolvent, employees who are owed wages, wages in lieu of notice, pay for untaken annual leave, pay for untaken statutory holidays, severance payment or other statutory/contractual sums would wish to know their rights and protection under the law, and the way to recover the sums that their insolvent employer may owe them. This booklet gives a brief account of what the employees of an insolvent employer may do to recover from their employer or from his assets the payments that may be owed to them.

While every care has been taken in the preparation of this booklet, it is only a guide and therefore should not be regarded as an exhaustive, authoritative legal document on the various legal issues that it deals with.

Section 1: Insolvency of the Employer

Symptoms of insolvency

1.1 The common symptoms of insolvency are:

- a) employer fails to pay his debts including wages when they are due;
- b) plant and machinery or raw materials are removed from the employer's place of work without good reason;
- c) place of work is shut down without prior notice;
- d) employer suddenly disappears;
- e) employer's assets or goods are suddenly seized by court bailiffs.

1.2 If any of these symptoms appear, employees should as soon as possible seek advice and assistance from the Labour Relations Division of the Labour Department. Based on individual case circumstances, the Labour Relations Division will refer the employees to the Labour Tribunal, the Minor Employment Claims Adjudication Board or the Legal Aid Department for further assistance. The Legal Aid Department will consider granting legal aid to eligible employees. Where appropriate, it may assist the employees to institute winding-up or bankruptcy proceedings against the employer. If the employees meet the eligibility criteria of "Protection of Wages on Insolvency Fund", they will also be referred to the Wage Security Division of the Labour Department for application for ex gratia payment from the Fund.

Section 2: Bankruptcy and Winding-up

Bankruptcy and winding-up order

- 2.1** If an employee is owed wages, wages in lieu of notice, pay for untaken annual leave, pay for untaken statutory holidays, severance payment or other statutory/contractual sums, he may, as a creditor, petition the Court of First Instance of the High Court for a bankruptcy order (where the insolvent employer is not a limited company) or a winding-up order (where the insolvent employer is a limited company).
- 2.2** Upon the making of a bankruptcy order or a winding-up order, the provisional trustee or provisional liquidator (who may be the Official Receiver or private sector insolvency practitioner) respectively will take immediate steps to recover and preserve the employer's assets. The assets will normally be sold by the trustee or liquidator and the proceeds of sale, after deduction of the necessary fees and expenses, will be used to pay debts owed to the employer's creditors.
- 2.3** If the employer is not a limited company, apart from the business assets of the firm, the personal assets of the sole proprietor or all partners of the business may be seized by the trustee and utilised to pay the creditors.
- 2.4** If the employer is a limited company, only the assets of the company may be recovered by the liquidator and used to pay the debts of the company. Usually, shareholders and directors of the company will not be personally liable for payment of the debts of the company except in certain circumstances like fraud or misfeasance by shareholders and directors of the company.

Proof of debt

- 2.5** After the making of the bankruptcy or winding-up order, the employees should go to the Official Receiver's Office to complete a proof of debt form. They can each file their own proof, or they can appoint one or more representatives to represent them by completing a single proof of debt. All proofs of debt will be examined and adjudicated by the trustee or the liquidator who may admit or reject part of or the whole of any claim. To safeguard their interests, employees are advised to preserve all available evidence of employment, such as employment contracts or employment letters, pay sheets or pay envelopes, salaries and wages books, leave records, etc., and to produce the same to the trustee or the liquidator to support their claims.

Preferential rights of employees in respect of arrears of wages, wages in lieu of notice, accrued holiday remuneration and severance payment

2.6 Employees are entitled to payment out of the assets of the employer in preference to most other creditors in respect of arrears of wages, wages in lieu of notice, accrued holiday remuneration and severance payment as follows:

if the employer is a limited company

- a) wages up to a maximum of \$8,000 in respect of services rendered to the employer beginning four months next before
 - the passing of a resolution by the company for a voluntary winding-up; or the appointment of a provisional liquidator before the hearing of the petition for the purposes of preserving the company's assets; or the presentation of the winding-up petition and ending on the date of the winding-up order (as the case may be); or
 - the last day of service of any employee who has made an application to the "Protection of Wages on Insolvency Fund" for an ex gratia payment and ending on that last date of service;
(whichever is the earlier)
- b) wages in lieu of notice not exceeding one month's wages or \$2,000, whichever is the lesser;
- c) all accrued holiday remuneration (including but not limited to pay for untaken annual leave and pay for untaken statutory holidays); and
- d) severance payment not exceeding \$8,000.

if the employer is not a limited company

- a) wages up to a maximum of \$8,000 in respect of services rendered to the employer
 - during the period beginning four months immediately preceding the filing of the petition and ending on the date of the bankruptcy order; or
 - during the period beginning four months next before the last day of service of any employee who has made an application to the "Protection of Wages on Insolvency Fund" for an ex gratia payment and ending on that last date of service;
(whichever is the earlier)

- b) wages in lieu of notice not exceeding one month's wages or \$2,000, whichever is the lesser;
- c) all accrued holiday remuneration (including but not limited to pay for untaken annual leave and pay for untaken statutory holidays); and
- d) severance payment not exceeding \$8,000.

2.7 Any wages, wages in lieu of notice or severance payment exceeding the amounts specified above are non-preferential debts and employees will be treated as ordinary creditors when it comes to the distribution of the excess balance of the proceeds of the employer's assets.

2.8 Employees should not assume that the making of a bankruptcy order or a winding-up order will necessarily guarantee payment of their arrears of wages, wages in lieu of notice, accrued holiday remuneration, severance payment and other statutory/contractual sums. It all depends on what money and assets the employer may have or which the trustee or liquidator may be able to recover and sell.

Section 3: Preservation of Employee's Rights

Employer's assets being removed

3.1 If employees know that the assets of the employer are being removed from the business premises without good reason, they should note down the registration number of any vehicle used to transport the assets and if possible, try to ascertain the address to which the assets are being delivered. The employees should without delay inform the Labour Relations Division of the Labour Department. Officers of the Labour Relations Division will provide appropriate advice and assistance, basing on individual case circumstances. If they have already been granted legal aid, the employees should immediately inform the Legal Aid Department.

Employer's goods being seized by court bailiffs on behalf of judgement creditors

3.2 An employer's goods may be seized by court bailiffs if other creditors of the employer have obtained a judgement against the employer for payment of money and the judgement debt has not been paid. If this happens, the employees should promptly approach the Labour Relations Division of the Labour Department where officers will provide appropriate advice and assistance, basing on individual case circumstances. If they have been granted legal aid, the employees should immediately inform the Legal Aid Department. It is because the goods seized by the bailiffs by order of the Court will be sold and the proceeds of sale will be retained in court for 14 days before being paid to the judgement creditor. If a bankruptcy or winding-up petition has been presented to the court before the expiration of this 14-day period, any proceeds of sale held will be "frozen" in court and in all probability will eventually become available to pay the employees/creditors in the order of priorities of their debts.

Employer's goods being seized by way of "distrain" for non-payment of rent

3.3 If the employer has not paid his rent, his landlord may obtain from the court a Distress Warrant directing the court bailiff to seize and sell the moveable assets of the employer in payment of the arrears of rent. When this happens, the proceeds of sale are not frozen in court. However, if the distraint for arrears of rent occurs within three months next before the making of a bankruptcy or winding-up order against the employer, the employees' preferential claims are a first charge on goods seized under the distraint or on the proceeds of sale. The trustee or liquidator may, in such cases, recover from the landlord the employees' preferential claims out of the money received under the distraint.

Employer company being taken charge of by a receiver under debenture

3.4 A company may sometimes mortgage or charge some of its assets to third parties (usually financial institutions) to obtain cash to finance the business of the company. These mortgages, known as "debentures", are required to be registered at the Companies Registry. The debenture holder, that is the lender, has the right to appoint without a court order a receiver to take charge of the assets of the company. The primary duty of the receiver is to recover what is

owing to the debenture holder either out of the existing assets of the company covered by the debenture or out of future earnings of the company (if the receiver decides to manage the company and carry on its business).

- 3.5** A receiver under the debenture is not liable to pay employees their preferential claims out of the fixed assets specifically listed and identified in the debenture. So, the receiver can sell, for example, items of machinery that have been clearly identified in the debenture and use the proceeds of sale to pay off the debenture holder.
- 3.6** The receiver is, however, responsible for payment of the employees' preferential claims in priority to the debenture holder if there are funds available from goods subject to floating charge. These usually include raw materials in the employer's factory, stock in trade and cash receivable by the company from its debtors.
- 3.7** If a receiver has been appointed under a debenture and there is no winding-up order subsequently made, employees should co-operate with the receiver by remaining at work unless the receiver specifically requested them not to do so. They should approach the receiver for payment of their wages and any statutory benefits to which they may be entitled. If payment is not made promptly by the receiver, they should immediately approach the Labour Relations Division of the Labour Department. The employees, as creditors, can still petition the court to wind up the company.

Employer promises to pay

- 3.8** Where an employer promises to pay the employees the wages, wages in lieu of notice, pay for untaken annual leave, pay for untaken statutory holidays and/or severance payment he owes them, the employees should, if they have already been granted legal aid, ask the employer to pay them through the Legal Aid Department. If the employees have approached the Labour Department but not the Legal Aid Department, they should immediately notify the Labour Relations Division of the Labour Department which will assist them in obtaining the correct amount of payment directly from the employer.
- 3.9** In view of the time limit in respect of wages qualifying for preferential payment (see paragraph 2.6), employees are strongly advised not to rely on mere promises by the employer or by some third party to pay arrears of wages at some future date and to delay taking legal action. This may result in employees' loss of entitlement to payment as preferential creditors if the promises to pay are not kept.

Section 4: Protection of Wages on Insolvency Fund

- 4.1** The "Protection of Wages on Insolvency Fund" is administered by the Wage Security Division of the Labour Department. By making ex gratia payments to employees whose employers have become insolvent, the Fund enables employees to obtain, without having to wait until the completion of the time-consuming insolvency proceedings, prompt payment of arrears of wages, wages in lieu of notice, pay for untaken annual leave, pay for untaken statutory holidays and/or severance payment owed to them. Where an ex gratia payment has been made from the Fund to an employee, his rights and remedies in respect of items of claim declared in the application shall, to the extent of that payment, be transferred to and vested in the Protection of Wages on Insolvency Fund Board. The subrogation right of the Fund Board will not affect the rights or remedies of the applicant in respect of other debts, including the balance of wages in lieu of notice and the balance of severance payment. To ensure that their applications do not fall outside the six-month period stipulated in the Protection of Wages on Insolvency Ordinance, employees should approach the Labour Relations Division of the Labour Department as soon as possible in case of insolvency of the employer.
- 4.2** To apply for ex gratia payments from the Fund, each employee should submit to the Fund through the Labour Relations Division an individual application in an approved form supported by a statutory declaration (Form 1) together with copies of all available documents (see paragraph 2.5) supporting his application. Payment from the Fund is subject to verification of applications and the fulfillment of the prerequisite for presentation of a bankruptcy or winding-up petition against the employer. It is best for employees to appoint from amongst themselves representatives who are acquainted with all the relevant facts and can therefore act as spokesmen for all fellow employees in dealing with the Labour Department and the Legal Aid Department.
- 4.3** For details of application for ex gratia payments from the Fund, please refer to the pamphlet "Guide to the Protection of Wages on Insolvency Ordinance and Points to note for making application to the Protection of Wages on Insolvency Fund" published by the Labour Department.

Enquiries

Enquiry Hotline: 2717 1771 (the hotline is handled by “1823”)

Homepage Address: <http://www.labour.gov.hk>

Enquiry in person to Offices of the Labour Relations Division:

<http://www.labour.gov.hk/eng/tele/lr1.htm>

Wage Security Division of the Labour Department

16/F, Overseas Trust Bank Building, 160 Gloucester Road, Wan Chai, Hong Kong Tel:2923 5299

Legal Aid Department

30/F, Revenue Tower, 5 Gloucester Road, Wan Chai, Hong Kong Tel:2594 7909

Official Receiver's Office

10/F, High Block, Queensway Government Offices, 66 Queensway, Hong Kong Tel: 2867 2448

