

HONG KONG / JUDGMENT

FRED LEE v. LIU MAN HOO

COURT

Court of First Instance

DECIDED

14 September 2007

CASE / FILE NUMBER

HCB11719/2002

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HCB 11719/2002

IN THE HIGH COURT OF THE

HONG KONG SPECIAL ADMINISTRATIVE REGION

COURT OF FIRST INSTANCE

BANKRUPTCY PROCEEDINGS NO. 11719 OF 2002

Re: LIU MAN HOO

BETWEEN

FRED LEE, trustee of the property of Applicant

LIU MAN HOO, a bankrupt

and

LIU MAN HOO Respondent

Bankrupt

Before: Hon Lam J in Court

Date of Hearing: 28 August 2007

Date of Decision: 28 August 2007

Date of Handing Down Reasons for Decision: 14 September 2007

REASONS FOR DECISION

A bankruptcy order was made against Mr Liu Man Hoo [

] on 10 October 2002. Since then, he had made reasonable efforts in making regular contributions to his estate for the purpose of repaying his creditors. The total amount of provable debts is \$3,654,698. In the four years since the making of the bankruptcy order, Liu had contributed \$1,442,011.05 to his estate. Several dividends were declared in favour of the creditors. Liu had been co-operative with the Trustee since his bankruptcy and full and frank disclosure has been given in respect of his affairs. The Trustee accepted that his post-bankruptcy conducts were satisfactory.

Under Section 30A(1) and (2) of the Bankruptcy Ordinance, a bankrupt is discharged from bankruptcy upon the expiration of the relevant period. In the case of Liu, the relevant period is four years. Liu was therefore hoping that he could be discharged on 10 October 2006.

However, Section 30A(1) is subject to Section 30A(3). Under the latter sub-section, the court may order the relevant period to cease to run for a specified period on the application of the trustee if it is satisfied that a valid objection is made out. The statutory grounds of objection are set out in Section 30A(4).

In the present case, the Trustee took out an application under Section 30A(3) on 11 September 2006. The grounds of objection relied on by the trustee were,

- (a) That Liu is likely within 5 years of commencement of the bankruptcy to be able to make a significant contribution to his estate [Section 30A(4)(a)];
- (b) That the conduct of Liu, in respect of the period before the commencement of the bankruptcy, has been unsatisfactory [Section 30A(4)(d)].

An interim order was made by Master Kwang on 5 October 2006

suspending the running of the relevant period pending the determination of the Trustee's application

. That interim order was continued by Master Hui on 6 March 2007.

The application was heard on 28 August 2007. After hearing submissions, I dismissed the Trustee's application and lifted the suspension. Liu was therefore discharged from bankruptcy in accordance with Section 30A(1).

The following are my reasons for the dismissal of the application.

The discretion under Section 30A(3)

It is necessary to start by examining the relevant statutory provisions. It should be noted at the outset that under Section 30A(3), the court is given a discretion to order the relevant period to cease to run for a specified period if valid grounds of objection are established. Hence, it does not automatically follow from the establishment of a valid ground of objection that there would be a suspension. The grounds of objection have to be established to give the court a jurisdiction to order suspension. But after a ground is established, the court still has to exercise its discretion in accordance with the facts and circumstances of the case. This is clearly spelt out in *Re Hui Hing Kwok* [1999] 3 HKC 683; see also *Fred Lee v Tong Yuk Kin* HCB 22870 of 2002, 20 June 2007 Para.18.

The discretion should be exercised in line with the underlying spirit of our bankruptcy law. In *Re Hui Hing Kwok* [1999] 3 HKC 683, Le

Pichon J (as she then was) referred to the purpose of the automatic discharge provision alluded to in para.17.16 of the Law Reform Commission

s Report on Bankruptcy and succinctly summed up the proper approach as follows,

Rehabilitation in the sense of enabling the bankrupt to resume a normal life in society is a key, if not the key, consideration. It should only be delayed by a bankrupt

s own failings.

In *Lee Fred v Leung Chin Yeung* [2007] 1 HKC 164, Kwan J reiterated that an application to object to discharge is a serious matter and it should not be embarked upon lightly. At para.37, Her Ladyship cited a very helpful dicta of Smithers J in the Federal Court of Australia in *Re Zion* and it is worth highlighting the following,

In my view it is the policy of the law that bankruptcy should in most cases come to an end at three years

Public interest will require that a discharge be delayed or made conditional if the conduct revealed or the character of the bankrupt indicates that the return of the bankrupt to the commercial world in full freedom might involve the unacceptable risk to persons likely to be engaged in commercial relations with him in the future.

Hence Kwan J also held that a trustee should exercise his judgment before deciding whether to object. At para.38(1), Kwan J pointed out that it is not appropriate to object merely because there is a ground which comes within one of the provisions in Section 30A(4). I respectfully agree. Insofar as a trustee has adopted a practice of raising an objection as of course when a ground can be framed under that subsection, such practice should be rectified.

I regret that based on what I was told at the hearing, the Trustee seems to have taken the stance that he was only concerned with presenting a case that falls within Section 30A(4) and it is left to the court to decide whether the discretion should be exercised against the bankrupt. That is clearly not the right approach. I hope it is an oversight on the part of the Trustee since he should have been fully aware of Kwan J

s observations. It is important for a trustee to appreciate that he is performing a public duty (Kwan J described it as

quasi-judicial

obligation) and an application for suspension under Section 30A(3) will necessarily entail costs to be incurred. Apart from the grounds under Section 30A(4), a trustee should consider all other relevant circumstances in the case to see whether there is at least an arguable case that the court should exercise its discretion against the bankrupt.

Further, a trustee should carry out the necessary investigation to inform himself of all relevant facts before he could make a responsible and proper decision on whether it is appropriate to object in the circumstances of the case in question. I find it astonishing that in the present case, the Trustee had not even conducted any interview with Liu regarding his pre-bankruptcy conducts before he decided to raise an objection based on Section 30A(4)(d).

If necessary, the court could inquire into the conduct of a trustee under Section 84 of the Bankruptcy Ordinance.

In Fred Lee v Tong Yuk Kin HCB 22870 of 2002, 20 June 2007, Deputy Judge A To expressed his agreement with the approach of Kwan J. His Lordship however added that the need to preserve commercial morality is also another important consideration underlying the bankruptcy regime. At para.20, the following observation was made,

I think conduct involving fraud or misrepresentation in applying for credit which contributed to bankruptcy would invariably result in an abuse of the bankruptcy regime. Save in exceptional cases, the court

s discretion should be exercised against bankrupts whose bankruptcy was related or contributed to by such conduct.

I agree that the demands of commercial morality is another public interest that have to be safeguarded in the bankruptcy regime and the obtaining of credit by fraudulent conducts is a serious matter. However, it is necessary to draw a distinction between fraudulent misrepresentations and other types of misrepresentations. The culpability of different types of misrepresentations is obviously very different. It is important to have a proper investigation into each alleged pre-bankruptcy misconduct before one can properly decide whether the case warrants a suspension of the relevant period. Thus, the need for a thorough investigation by the trustee before he could properly discharge his public duty in deciding whether to raise an objection to automatic discharge.

As compared with Para.20, I think the approach set out in Para.21 of the judgment of Deputy Judge To is a more balanced one. His Lordship said,

It should take into consideration all the circumstances leading to the bankruptcy and not just the conduct complained of. It should consider the seriousness of the conduct, the bankrupt

s conduct after the commencement of bankruptcy, the degree of co-operation he has shown with the trustee during the relevant period and the effort he has contributed to repaying his debt. In an appropriate case, the court should consider the risk to the commercial community should the bankrupt be allowed to resume full commercial activity. The discretion to suspend the running of the relevant period should not be lightly exercised. But in its balancing exercise, the court should not allow the bankruptcy regime to be abused.

At para.22 of his judgment, Deputy Judge A To made the important point that the purpose of suspension is rehabilitative and it should not to be used as a means of extracting more contribution from the bankrupt for distribution to his creditors. That must be correct insofar as pre-bankruptcy misconducts are concerned. However, regarding cases falling under Section 30A(4)(b),(c),(d) (in respect of post-bankruptcy misconducts), (e) and (h), the purpose of suspension may well be the facilitation of the proper administration of the estate.

Ability to make a significant contribution

Section 30A(4)(a) provides the following as a ground on which an objection can be made,

that the bankrupt is likely within 5 years of the commencement of the bankruptcy to be able to make a significant contribution to his estate

.

The Trustee interprets this ground as meaning that if it can be shown that the bankrupt is able to make a significant contribution to his estate in the fifth year, the ground is made out and the court can suspend the running of the relevant period. Mr Chan cited the decision of Poon J in *Re Hau Po Man Stanley HCB 924 of 2002*, 26 June 2007 to support his contention. However, there was no argument nor discussion in the judgment regarding the points I canvassed below.

That interpretation can lead to the odd result that notwithstanding a bankrupt has diligently made significant contribution to his estate during the four years since his bankruptcy, he would be deprived of the benefit of automatic discharge under Section 30A since it is likely that he would make further significant contribution to the estate in the subsequent years. In other words, a conscientious and diligent bankrupt could end up in a worse position as compared with a bankrupt who is idle and makes no contribution in the relevant period. That is clearly inconsistent with the objective of rehabilitation. If this were the correct interpretation, a bankrupt would be discouraged from working hard to make a decent contribution in the first four years.

Mr Chan accepted that this interpretation may appear to be unfair to a hardworking conscientious bankrupt, but he submitted it is fair to the creditors.

The harshness of this interpretation is compounded by the fact that once a ground of objection is established, subject to the exercise of the discretion, the court can suspend the relevant period for 4 years in the case of a bankrupt who has not previously been adjudged bankrupt (Section 30A(3)(a)). Hence, theoretically speaking, a diligent bankrupt who has been making proper contribution to his estate during the first 4 years since his bankruptcy is at risk of not being discharged until 8 years after the commencement of his bankruptcy.

This problem is highlighted by the position taken by the Trustee at the hearing. When this court asked Mr Chan what would be the appropriate period of suspension if the objection under Section 30A(4)(a) is sustained, Mr Chan said the Trustee would just leave the matter to the court and no argument was advanced regarding how the period of suspension should be considered.

The Trustee apparently regards it as his duty to recover as much as possible from Liu for repaying the indebtedness due to the creditors. If this interpretation were correct, and if the policy underlying this ground of objection is to facilitate the maximum recovery for the benefit of the creditors by way of the bankrupt

s contributions to the estate, it is difficult to see a justification for not suspending the relevant period for the maximum period, viz. 4 years. Once it is satisfied that a bankrupt could make significant contribution in the fifth year out of his regular monthly income, short of a likelihood of material change of circumstances during the fifth to eighth years, it must follow that he would be able to make significant contribution in the sixth year, the seventh year and the eighth year. If the policy is maximum recovery, the natural conclusion is to suspend the period for 4 years.

I do not believe this is the policy of our bankruptcy regime. Though it is one of the duties of a trustee to trace and collect the assets of a bankrupt and to distribute the same amongst the creditors in an orderly manner, it is wrong for him to act as if his prime duty were that of a debt collector for the creditors. Even though a trustee is appointed by a general meeting of the creditors and should have regard to the directions given by resolution of the creditors at general meetings or resolution of the committee, he is not the agent of the creditors. Such resolutions must be subject to the Bankruptcy Ordinance, see Section 82(1). In case of doubts, the trustee should seek the court

s direction, see Section 82(3).

This is particularly so in the context of the performance of his duty to consider whether to raise an objection to automatic discharge. The trustee is obliged to balance the interest of the creditors against that of the bankrupt in his rehabilitation and the public interest underlying our bankruptcy regime. As Kwan J observed, this is a quasi-judicial duty. The trustee should act impartially in forming a view whether the facts of the case warrant the making of an objection to the automatic discharge having regard to guiding principles for the exercise of discretion set out above.

In *Re Maher* (1985) 61 ALR 592, Woodward J had this to say regarding a trustee's role in the materials placed before the court,

Clearly the trustee should not put forward irrelevant information, or intrude on the court

s functions, nor should he take a partisan approach to the application by only putting forward material unfavourable to the applicant and supporting the trustee

s opposition. However, the trustee is under a duty to ensure that the court has before it all material that will assist it in considering an application for discharge

Whilst it is right and proper that a trustee should use reasonable skill and care in procuring a proper contribution from a bankrupt to the estate during the usual four years period, I do not think it is the purpose of the objection mechanism under Section 30A to empower a trustee to extract more contributions by asking the court to suspend the automatic discharge on account of a likelihood of significant contribution in the succeeding years notwithstanding that contribution have already been made by a bankrupt to the best of his ability during the first four years. That would be incongruous with the professed objective of rehabilitation.

Support for my view as to the purpose of the objection can be found in the authorities I have discussed in the context of the discretion under Section 30A(3).

It is to be noted that in para.17.42 of its report, the Law Reform Commission believed that the criteria for objection were there to

provide the trustee and the court with the ability to prevent the discharge of a bankrupt if discharge is not deserved

. It is difficult to see how it can be suggested that a bankrupt is not deserved to be discharged simply because he has the ability to make significant contribution in the future even though he had already made contribution to the best of his ability in the past.

If one examines the grounds of objection set out in Section 30A(4), putting aside sub-section (a) for a moment, all the other grounds were cases where there are some elements of fault on the part of the bankrupt. Hence the reference of *Le Pichon J* in *Re Hui Hing Kwok* [1999] 3 HKC 683 to the bankrupt

s failings.

I believe Section 30A(4)(a) is there to catch those bankrupts who have the ability to make a significant contribution but who choose not to utilize such ability and fail to make a proper contribution during the usual four years period. Such bankrupts are at fault and those cases would warrant a consideration of suspension of the automatic discharge. This was what happened in *McGoldrick v Official Trustee in Bankruptcy* (1993) 119 ALR 253 where the Australian equivalent of our Section 30A(4)(a) was applied.

This construction is reinforced by a comparison of the Australian Bankruptcy Act 1966 with the new provisions in the Bankruptcy Amendment Act 1991. Our Section 30A(4) is primarily taken from the 1966 Act. Section 149(4) in that Act (the equivalent of our Section 30A(4)) was amended in 1991. In the amended version, there is no longer any reference to the ability to make significant contribution or its likelihood. Instead, under sub-section (f), one of the grounds of objection is,

the bankrupt failed to pay to the trustee an amount that the bankrupt was liable to pay under Section 139ZG

.

Section 139ZG has to be read together with Sections 139P and 139Q. They provides for the liability of a bankrupt to make contribution to the estate

at such times and in such amounts as the trustee determines

. That obligation arises

if the income that a bankrupt is likely to derive during a contribution assessment period as assessed by the trustee under an original assessment exceeds the actual income threshold amount applicable in relation to the bankrupt

. The underlying objective of these provisions is to ensure that a bankrupt would make a decent contribution to his estate during the usual bankruptcy period if he has the ability to do so. They appear to be serving the same purpose as the old Section 149(4)(a) but are drafted in greater precision.

Therefore it does not seem to the objective of Section 149(4)(a) to enable a trustee to extract more contribution from a bankrupt who has already made a decent contribution during the relevant period.

The key to the correct construction of Section 30A(4)(a) lies in its reference to the likelihood of the ability of the bankrupt to make a significant contribution within 5 years. If the purpose of the sub-section were to extend the bankruptcy period to facilitate a maximum recovery for the creditors by extracting more contributions in the fifth to eighth years, it needs not refer to the first four years. It would be enough for the legislation to provide under this ground,

That the bankrupt is likely to be able to make a significant contribution to his estate in the 4 years after the expiration of the relevant period provided for under sub-section (2) or any part thereof.

I note that in recommending the adoption of the Australian model in Hong Kong, the Law Reform Commission slightly amended the wordings of this sub-section. The words

is able

in Section 149(4)(a) of the Australian Bankruptcy Act 1966 were deleted.

The reference to the likelihood of the ability to make significant contribution within 5 years implies that one should consider the five years together. If a bankrupt has actually made significant contribution in the first four years, one would not be referring to the likelihood of the ability to do so. It is not a matter of likelihood. It is a fact, a certainty. One only needs to refer to the likelihood of the ability to make significant contribution when no such contribution has been made in the past.

I am of the view that it is a clear case calling for a purposive interpretation of Section 30A(4)(a). There are cogent reasons leading me to the conclusion that the list of objections under Section 30A(4) refers to cases where the bankrupt has been at fault. I do not believe Section 30A (4)(a) is there to enable a trustee to extract further contribution from a bankrupt for the benefit of the creditors when he has not been at fault during the usual 4 years period.

Hence, on proper construction, I hold that Section 30A(4)(a) is not applicable to a case where a bankrupt has already made a contribution to his estate with due diligence during the first 4 years.

In the alternative, if I were somehow wrong on my construction of Section 30A(4)(a), I will hold that the court should place great weight on the due diligence on the part of a bankrupt in making contribution during the first 4 years in the exercise its discretion under Section 30A(3). If the only ground relied upon to object is that such a bankrupt could make further significant contribution in the years to come, in line with the guidance as regards the underlying policy of Section 30A(3), it is unlikely that the court would order any suspension at all.

Given my views on Section 30A(4)(a) and the contributions already made by Liu, it follows that there should not be any suspension under that ground in the present case.

Unsatisfactory conducts

Section 30A(4)(d) provides one of the grounds on which an objection can be made is that the conduct of the bankrupt, either in respect of the period before or the period after the commencement of the bankruptcy, has been unsatisfactory.

In *Lee Fred v Leung Chin Yeung* [2007] 1 HKC 164, all the counsel agreed that it connotes a broad and low jurisdictional threshold (see Para.44).

In Para.45, Kwan J made the following observation regarding excessive borrowing,

In a case involving excessive credit in which loans were obtained when the debtor should have known he would not be able to repay, where the bankrupt has been co-operative with the trustee and made voluntary contributions to the estate, and provided there is no other misconduct, I am inclined to think that the pre-bankruptcy conduct is not such as to warrant suspension of the running of the relevant period.

I agree with Deputy Judge A To that in that paragraph, Kwan J was dealing with how the discretion should be exercised as opposed to whether excessive borrowing can constitute unsatisfactory conduct under Section 30A(4)(d).

In *Fred Lee v Tong Yuk Kin* HCB 22870 of 2002, 20 June 2007, Deputy Judge A To made reference to the law under the old Bankruptcy Ordinance and took the view that in general, the matters set out in Section 30(4) under the old ordinance could be regarded as examples of unsatisfactory pre-bankruptcy conducts (para.14). The protection of the integrity of the automatic discharge system and the prevention of abuse of the bankruptcy regime were identified as the rationale for taking pre-bankruptcy conducts into account (paras.15 and 16). The acid test formulated by the learned judge is as follows (para.17),

Ultimately, the question of whether the conduct is unsatisfactory is whether the conduct is one which the society is prepared to condone without expressing disapproval. This question is to be answered by the reasonable man

s test. This hypothetical reasonable man has to bear in mind the overriding purpose of rehabilitation. He has to take into account whether the debt is a business debt or consumer credit and consider the reasons for which the debt was incurred, the amount of the debt as compared with the bankrupt

s means and station in life, the blameworthiness of the bankrupt and all the circumstances in which the debt arose. In addition, the reasonable man has to take into account human nature, its weakness, its readiness to indulge in extravagant spending and its readiness to engage in speculation and assumption of risk.

This test was adopted and applied by Master Kwang in *Fred Lee v Kwan Kwong Ning* HCB 17846 of 2002, 20 August 2007.

No other test has been urged upon me at the hearing. Subject to what is said below, I am happy to adopt this as the correct test. For my part, I do not think it is necessary to refer back to the old ordinance to identify what are unsatisfactory conducts. Whilst I agree whole-heartedly with the view of Deputy Judge A To that the circumstances under which the debts were incurred were important, it might not be too useful to classify the debts as consumer credit or business debts. The debts might well be incurred for an individual

s investment purposes like buying of flats or publicly listed stocks. Further, one should not be too ready in condemning debts incurred for speculation. In this society, speculation and investment could be a fine distinction in many cases. In some instances, the assumption of high risk on the part of a bankrupt is actually fostered by the staff and the sales tactics of the institutional lenders who should have managed their credit risk better.

Therefore, in order to have a balanced view, a trustee should examine into the circumstances under which the debts were incurred with care and place the relevant information before the court.

In the present case, the Trustee apparently did not conduct any meaningful investigation as regards how the debts of Liu came to be incurred. According to Mr Chan, the Trustee simply extracted the information from the documents filed for proof of debts and the statement of affairs to come to the view that objection should be made. In *Lee Fred v Leung Chin Yeung* [2007]

1 HKC 164 Kwan J referred to the practice of this trustee at para.35 and explained at para.38 why this practice is flawed. At para.38, Her Ladyship alluded to the fact that the Trustee has filed 150 objections out of 360 cases in which he was appointed during June 2002 to January 2003. I have not been told whether the present case is one of those 150 objections. But the Trustee was appointed within that period and the present objection was filed in September 2006. On 5 October 2006, the present application was adjourned pending the decision of Kwan J. in the three test cases. It was restored on 6 March 2007 after the judgment of Kwan J.

In his written answer to a standard questionnaire of the Official Receiver, Liu said that the cause of bankruptcy was failed investments. Given the lack of investigation by the Trustee, bearing in mind the background of Liu and his post-bankruptcy conducts, I am of the view that Liu had truthfully set out the reasons why the debts were incurred.

In the absence of evidence to suggest unreasonable conducts pertaining to the investments, I see no reason why Liu should be condemned for his failed investments.

In paragraph 19 of his 3rd Affirmation, the Trustee set out other matters to support his contention that Liu

s pre-bankruptcy conducts were unsatisfactory. They can broadly be divided into two categories: (a) excessive borrowings; and (b) misrepresentations of existing indebtedness in loan applications.

I accept that in an appropriate case, excessive borrowings can constitute unsatisfactory conducts. On the other hand, there are situations where excessive borrowing arises out of unfortunate circumstances which may escape such condemnation. An example of that is the case before Master Kwang in Fred Lee v Kwan Kwong Ning HCB 17846 of 2002, 20

August 2007.

Regarding the alleged misrepresentations, again I have very little evidence as regards the circumstances under which the loan applications were filled and signed by Liu. The Trustee only relies on the documents. He had not investigated from Liu or the staff of the creditors responsible for handling the applications as regards the circumstances surrounding the completing and submitting of the loan applications. Liu himself did not say much on this issue. In paragraph 8 of his Affirmation, he said he had not dishonestly misrepresented his financial positions. He also said,

All the financial institutions were then keen to lend and they did not ask me all the details about the borrowings I have made. In some cases, the handling staff of these financial institutions even told the information that required were only for routine check.

The Trustee simply relied on the loan application forms, the declarations by Liu contained therein and an affidavit of a bank officer filed in another set of proceedings regarding restriction on sharing of credit information between financial institutions and a statutory declaration from an officer of JCG (one of the creditors) regarding their general practice. I do not find the affidavit and the statutory declaration to be of much assistance in rebutting Liu

s evidence regarding how his creditors secured the loan applications from him. The deponents did not address their minds to these particular transactions. The Affidavit of Mr Constable was filed in HCB 8779 of 2002 and he had nothing to do with the present proceedings. Whatever the general practice or instructions JCG might have adopted and given to its frontline staff, I am not prepared to infer from the statutory declaration that the instructions had been faithfully implemented when the Trustee could have obtained specific evidence from the person who actually handled Liu

s application to deal with his allegation.

As regards the information in the loan application forms and the declarations contained therein, I think one must assess those against the background and circumstances under which these documents came to be signed. I agree they contained misinformation. However, the inaccuracies could be the result of frauds, negligence or even innocent mistakes due to misunderstanding of the effect of the forms. Typically, these loan applications were in very small prints and I have no information as to how much time was given to Liu to read the same carefully before he was asked to sign. Unfortunately, the Trustee did not deem it necessary to place specific information before the court.

I accept Liu

s explanation that he did not act with any fraudulent intention in respect of the omission to give full information in the loan applications. I am not even sure if he was negligent in failing to read the small prints.

On the other hand, I bear in mind the dates of the loans and I think the Trustee did have a valid point that by the time Liu applied for the loans from JCG, UA and SHK, he was effectively insolvent. The three loans were applied for successively within a very short time frame and the total amount was \$120,181. In fact, I can push the time frame a little bit earlier. Starting from the Citic loan of 18 December 2001, it is clear that Liu would not be able to service the repayments and he was just trying to get a new loan to service his old loans whenever he could not make ends meet.

Liu was a lecturer before his bankruptcy. According to the Trustee

s reckoning, Liu had to pay \$65,714 per month for 10 of his 16

loans whilst his monthly income was only \$52,000. On top of that, he had to pay for his credit cards indebtedness.

Even though the predicament of Liu stemmed from investment failure, this is not a case like *Fred Lee v Kwan Kwong Ning HCB* 17846 of 2002, 20 August 2007 where a bankrupt could expect some sympathy for his excessive borrowing.

Having regard to the circumstances as a whole, though I do not think Liu intended to cause financial loss to his creditors, I am of the view that Liu

s pre-bankruptcy conducts were unsatisfactory.

Exercise of discretion

In my judgment, the court must take an overall view of the matter in the exercise of discretion. Whilst there are cases where the unsatisfactory pre-bankruptcy conducts were so serious that it would be difficult for a bankrupt to escape suspension altogether (see Para.17.42 of the Law Reform Commission Report), I am of the view that this case does not fall within such category.

Whilst I acknowledge that it is important to prevent the abuse of our bankruptcy regime, it has to be remembered that suspension of automatic discharge should be the exception rather than the norm. If the court is satisfied that the return of the bankrupt to the commercial world in full freedom does not involve an unacceptable risk to persons likely to be engaged in commercial relations with him in the future, it should be slow to invoke the power of suspension. An over-zealous and widespread use of the power of suspension would not be conducive to the rehabilitation objective of the bankruptcy law. A bankrupt might feel so discouraged that he simply had no incentive to co-operate and make meaningful efforts to be productive to generate contribution to his estate during the post-bankruptcy period.

In this connection, I respectfully concur with Lander J

s observations in the Federal Court of Australia in *Frost v Sheahan* (2005) 3 ABC (NS) 288 at p.294-5,

The purpose of the objection procedure is to provide the trustee with a power by which he can induce the bankrupt to act in accordance with the bankrupt

s obligations.

The trustee should not use the power for the purpose of punishing the bankrupt for acts taken by the bankrupt which cannot be rectified. Rather, the power should be used for the purpose of persuading the bankrupt to discharge the bankrupt

s duties under the Act.

It is a power, however, which must be used sparingly and for the purpose of protecting the interests of creditors and in generally advancing the administration of the estate of the bankrupt.

In a sense, it is a power of last resort when no other form of persuasion will assist to remind the bankrupt of the bankrupt

s obligations.

Hence, the unsatisfactory pre-bankruptcy conducts that would warrant a suspension of automatic discharge in any event must be conducts of exceptional gravity. Based on the materials placed before me, including the very sketchy information the Trustee has in respect of the pre-bankruptcy activities of Liu, I am of the view that it would not be just and equitable to hold that automatic discharge should be suspended no matter how co-operative he had been since bankruptcy.

As I said, Liu

s post-bankruptcy conducts are unassailable. I am satisfied that he had tried his best to make a substantial contribution to his estate.

Having balanced the pre-bankruptcy conducts against the post-bankruptcy conducts of Liu and applying the approach regarding the exercise of the discretion set out above, I do not consider the case warrants any suspension of the automatic discharge.

For these reasons, I dismissed the Trustee

s application and lifted the suspension under the interim orders made by the masters.

The interim orders and the timing of the application

Before I leave this case, I wish to comment on the practice regarding the grant of interim orders and the timing of the application by the Trustee.

As mentioned, the application by the Trustee was filed on 11

September 2006, less than one month before the expiration of the usual four years period. Further, Liu was not given any advanced indication that the Trustee will raise objections under Section 30A(4). The Trustee did not interview him in respect of his pre-bankruptcy conducts at any time during the four years since the commencement of bankruptcy. Hence, Liu had a justifiable sense of grievance and he put it with circumspection in para.7 of his affirmation,

I have provided full and frank disclosure of all my assets, as well as taken all reasonable steps to ensure that I have made available all my possible assets to repay to the estate of bankruptcy. I have not hidden anything nor have I been obstructive in anyway to the trustee

s investigation in this case. In fact, I am doing everything to repay my debt to the best of my ability. The only incentive for me in doing so is my rehabilitation from bankruptcy which is something I have been working hard for and looking forward to. I want to resume a normal life in my family as well as in the society. Thus, to further delay my rehabilitation is totally unfair to me and to my family. I have lost many friends and relatives after they knew I am an adjudged Bankrupt and thus have become a virtual outcast in society.

In *Re Karounos* (1989) 25 FCR 177, Sheppard J said these regarding the finite period of bankruptcy,

There is thus an underlying policy to be discerned from the terms of the section that this area of law is to be attended with a high degree of certainty. That is not an unexpected result when one considers what is involved. Bankruptcy seriously affects the status of persons who are made bankrupt. So long as they are undischarged bankrupts, they continue to suffer the disadvantages and disabilities of bankruptcy.

In the same vein, Sheppard J observed in *Van Reesema v Official Receiver* (1983) 50 ALR 253 at p.264,

A bankrupt knows that at the end of a period of three years after his bankruptcy he will be discharged and thus freed from a number of obligations and disabilities which arise upon bankruptcy. It is true, I think, to say that bankruptcy of itself does not today carry with it the overtones of moral and commercial delinquency which once was the case.

But bankruptcy does carry with it real disadvantages. It is enough to mention the fact that after acquired property, apart from income, continues to vest in the trustee until discharge

and the continuing risk an undischarged bankrupt runs of infringing s

269 of the Act (obtaining credit in the sum of \$500 or more without disclosing bankruptcy). In a society where the obtaining of credit is an every day affair for ordinary people one could not, therefore, at least at first sight, treat non-compliance with provisions [as regards timing and formalities for lodging objection] as a light matter.

It is important that a trustee and the court should appreciate that it is particularly devastating for a bankrupt to learn for the first time during the last few months of the usual 4 years period that there would be an application to suspend the automatic discharge based on pre-bankruptcy conducts notwithstanding that his post-bankruptcy conducts were more than satisfactory.

Because of the timing of the application and adjournment of the matter pending the outcome of the test case heard by Kwan J, this application was not heard until the end of August 2007. Though I dismissed the application immediately after the hearing, there has already been a de facto suspension of the automatic discharge for more than 10

months.

In *Li Tat Kong HCB 741 of 1995*, 2 June 2000, *Le Pichon J* (as she then was) held that the court

s jurisdiction to suspend the automatic discharge was engaged upon the issuance of the summons by the trustee and interim order suspending the automatic discharge pending the final determination of the summons can be made.

On the other hand, there is an Australian authority holding that because of the policy of having a finite period for a bankruptcy and the need to have certainty, an interim order does not come within the scope of Section 149 of the Bankruptcy Act 1966: *Re Karounos* (1989) 25 FCR 177. Though the grounds of objection in our legislation were modelled upon 1966 Australian Bankruptcy Act, the mechanism for objection is different. The point had not been fully argued before me and I do not understand Mr

Lam to be challenging the masters

power to grant interim orders. In the circumstances, although I have raised the point at the hearing, I do not feel confident to express a conclusion. I shall assume that the current practice is valid in terms of jurisdiction.

However, I do not think it right to grant interim orders as of course. In *Re Jacobs* [1999] 1 WLR 619 at p.628, the deputy judge observed that there may be cases in which the court will refuse any extension notwithstanding that there is no court time because it takes the view that the official receiver has acted inappropriately in leaving the matter too late.

It is inherently unfair to a bankrupt if the automatic discharge is suspended due to a late unmeritorious application by a trustee. It is also an abuse of process if a trustee does not conduct any proper investigation during the four years period and leaves it to the last minute to seek to inquire into the affairs of a bankrupt and ask for suspension based on ground (b) under Section 30A(4). Thus in *Frost v Sheahan* (2005) 3 ABC (NS) 288 at p.301-2, Lander J said,

in some cases, the failure to identify those assets and income may be the fault of the trustee. In those circumstances, it may not be appropriate to continue the administration of the estate if the trustee has not discharged his or her obligations in a diligent manner

As explained above, a trustee should have conducted a proper investigation before he can properly decide whether to make an objection. This should include interviewing the bankrupt and ascertaining from him whatever explanations he might have as regards the possible allegations that might be raised against him. It follows that the court is entitled to expect that an application to object would be supported by reasonably comprehensive evidence filed by the trustee. At the call-over hearing, I think the court should form a provisional view on the merit of the application. If the court were of the view that there is a lack of real prospect of achieving any suspension, it should seriously considering dismissing the application if an interim order would have the effect of granting a de facto suspension, particularly if there is no good explanation for the late application.

The Trustee contended that it was reasonable for him to wait until the last moment before he filed an application because he had to take into account of post-bankruptcy conducts. I accept that there could be cases where the reliance on post-bankruptcy conducts entails a late decision to be made regarding the raising of objections. But I do not think this applies to the majority of the cases. Take the facts of the present case as an example, the Trustee should have investigated upon the pre-bankruptcy conducts soon after the filing of the proof of debts. As regards the

evidence regarding the misconceived ground (a), it was based on the stable employment of Liu. Bearing in mind the extent of co-operation of Liu since his bankruptcy, there was no indication that the Trustee would need to rely on post-bankruptcy unsatisfactory conducts. I do not see any reason why the Trustee could not take out an application at the end of the third year. If necessary, the Trustee can file supplemental evidence setting out additional grounds if there were developments subsequent to the filing of the original application that are material.

For most cases, by the end of the third year, with reasonable diligence and proper skill and competence, the trustee should have a good idea whether the bankrupt had been co-operative in the post-bankruptcy stage and whether there are pre-bankruptcy unsatisfactory conducts. The trustee should also be able to assess by then whether a discharge of the bankrupt at the end of the usual four years period would prejudice the administration of the estate. I do not think it is too onerous to expect a trustee to make a decision on whether to raise an objection shortly thereafter in a usual case. After all, in the timescale of a four years relevant period, it must be reasonable to expect the trustee to complete most of his investigation into the affairs of a co-operative bankrupt by that stage.

Mr Chan, for the Trustee, also argued that the provisions in the Bankruptcy Ordinance envisaged late applications for raising objections, see Section 30A(5) and (6). In my judgment, those provisions only set out the deadlines for such steps to be taken. Sub-section (5) refers to

not less than 3 months before the end of the relevant period

and sub-section (6) refers to

not less than 14 days before the end of the relevant period

. One must read those provisions in the light of clear legislative policy under Section 30A(1) and (2) that in a normal case a bankrupt has a legitimate expectation to be discharged at the end of the usual four years period. Whilst the right to be discharged is not absolute, I think it would be against the spirit of the legislation to endorse a practice that would necessitate undue delay to the discharge of a bankrupt even though the court does not find the case warrants any suspension at the end of the day. The facts of the present case serve as a good illustration of the potential abuse.

In *Official Receiver v Chan Kwok Keung* HCB 20722 of 2002, 5 July 2007, Master Au-Yeung (as she then was) ruled that if the court decided that there should not be any suspension, it could order the discharge to take effect as from the end of the usual four years period. If that were correct, that would ameliorate some of the hardship (but not all since the person would still be regarded as a bankrupt during the interim period) that might cause to a bankrupt by interim orders transcending the usual four years period. I understand this decision is under appeal and since the point had not been argued before me, I express no view on the issue. But I can say this: if the court does not have the power to give retrospective effect to the discharge, that would mean that a bankrupt could suffer real prejudice if he has to pay contribution under an income payment order.

Costs

Parties have reserved their arguments on costs pending my reasons for decision. I make an order nisi that the estate shall bear the costs of Liu in this application, such costs is to be taxed if not agreed.

(M H Lam)

Judge of the Court of First Instance

High Court

Mr Osmond Lam, instructed by Messrs Y T Szeto & Co., for the Bankrupt

Mr Chan Man Hon of Messrs Chan, Wong & Lam, for the Trustee

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