

# New Companies Ordinance (Chapter 622) – Highlights 新《公司條例》(第622章) – 概要

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Ensure Better Regulation  
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# **New Companies Ordinance (Chapter 622) Highlights**

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## **DISCLAIMER**

The highlights on each part of the new Companies Ordinance (“the New Ordinance”) contained in this booklet are intended to provide general information on the New Ordinance. They do not, and are not meant to, represent a comprehensive description of the New Ordinance. The highlights need to be read in conjunction with the New Ordinance. You are advised to seek independent professional advice before acting on anything contained herein. The Companies Registry does not accept any responsibility or liability for any loss or damage whatsoever arising from the use of or reliance upon any information provided in this booklet.

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# Preface

## The New Companies Ordinance

The commencement of the new Companies Ordinance, Chapter 622 of the Laws of Hong Kong, on 3 March 2014 will herald a new era for Hong Kong's company law.

The new Companies Ordinance ("the New Ordinance"), which consists of 21 Parts, 921 sections and 11 Schedules is, I believe, one of the longest and most complex pieces of legislation ever enacted in Hong Kong.

The New Ordinance will replace the core provisions of the existing Companies Ordinance (Chapter 32 of the Laws of Hong Kong) governing the formation and operation of companies, which will be repealed upon the commencement of the New Ordinance. The remaining provisions of the existing Companies Ordinance, which primarily cover corporate insolvency, winding up, disqualification of directors, receivers, managers and prospectuses, will not be repealed but will remain intact in the existing Ordinance, which will be renamed the Companies (Winding up and Miscellaneous Provisions) Ordinance when the New Ordinance comes into operation.

By way of history, with the support of the Panel on Financial Affairs of the Legislative Council ("LegCo"), the comprehensive rewrite of the Companies Ordinance began in mid-2006. Since then, the rewrite of the Ordinance has been undertaken by a dedicated Companies Bill Team consisting of officers from the Financial Services and the Treasury Bureau and the Companies Registry. In addition to the Standing Committee on Company Law Reform, which contributed significantly throughout the process, four advisory groups and a joint Working Group formed by

the Government and the Hong Kong Institute of Certified Public Accountants<sup>1</sup> were set up to review the law, consider and formulate proposals and recommendations concerning amendments to various areas of the law.

Following five rounds of public consultations and continuous discussions with relevant stakeholders over the years, including the holding of a series of public forums and seminars, the Companies Bill ("the Bill") was finalised and introduced into the LegCo on 26 January 2011.

Owing to the multiplicity and complexity of the issues involved, it took the Bills Committee more than 16 months to scrutinise the Bill and deliberate on the proposed initiatives, policy considerations and drafting technicalities. After 44 meetings lasting a total of more than 120 hours, the Bills Committee completed its clause-by-clause scrutiny of the Bill in June 2012. In the process, the Committee also considered over 850 Committee Stage Amendments, as well as nearly 700 consequential amendments that were required for other laws of Hong Kong.

The more controversial issues deliberated by the Bills Committee included, among others, the "headcount test", clarification of the standard of directors' duty of care, rules concerning directors' conflicts of interests, the introduction of a new offence in respect of omissions in auditor's report and a new formulation of "responsible person" to lower the prosecution threshold, accessibility to information on residential addresses of directors and full identification numbers of individuals and the qualifying conditions for simplified reporting.

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<sup>1</sup> Lists of Members of the Standing Committee on Company Law Reform and the five Advisory Groups are provided in Annex 1.

The passage of the New Ordinance on 12 July 2012 marked the culmination of more than six years' hard work and I was honoured to be among the team who witnessed the completion of this enormously challenging project.

The major objectives of the New Ordinance are to enhance corporate governance, ensure better regulation, facilitate business and modernise the law<sup>2</sup>. We believe that the New Ordinance brings the legal framework for the operation of companies in Hong Kong in line with modern international standards and ensures the infrastructure of Hong Kong's company law will continue to best serve the needs of Hong Kong as an international commercial and financial centre. It also reinforces Hong Kong's competitiveness as a place to do business.

The New Ordinance will come into operation on 3 March 2014. To facilitate the implementation of the New Ordinance, we introduced 12 pieces of subsidiary legislation<sup>3</sup> on technical and procedural matters into the LegCo in early 2013. A Subcommittee was set up by the LegCo to scrutinise the subsidiary legislation in February 2013. Having held a series of meetings to examine the provisions clause by clause, the Subcommittee concluded its work in June 2013, with the entire legislative process completed in July 2013.

The rewrite of the company law has been a tremendous challenge for all involved. As the Registrar of Companies, I must record my heartfelt thanks to all who have contributed to the process including, in particular, members of the legislature,

members of the Standing Committee on Company Law Reform, our five advisory groups, the advisory and drafting teams of the Department of Justice and all those who responded to our consultations for their valuable inputs, active participation and unfailing support.

Last but not least, I am also very much indebted to the great efforts, perseverance and hard work of members of the Companies Bill Team, without whom we would not have been able to resolve all the difficulties and teething problems on the way and accomplish the project as scheduled.

The publication of this booklet, which contains the highlights of each of the 21 Parts of the New Ordinance, seeks to promote understanding of the new legislation and prepare readers for the transition to the new regime. I hope you find the materials contained in this booklet informative and useful.

An electronic copy of the highlights can be found in the "New Companies Ordinance" section of the website of the Companies Registry at [www.cr.gov.hk](http://www.cr.gov.hk). The section also contains comprehensive information on the New Ordinance, including a Table of Origin and a Table of Destination cross-referencing provisions of the New Ordinance and the existing Companies Ordinance.

**Ms Ada LL Chung, JP**  
Registrar of Companies  
Companies Registry  
January 2014

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<sup>2</sup> A list of Major Initiatives introduced under the New Ordinance is provided in Annex 2.

<sup>3</sup> A list of the 12 pieces of subsidiary legislation is at Annex 3.

# Table of Contents

6	<a href="#">Overview</a>	
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## Highlights on the New Companies Ordinance

10	<a href="#">Part 1</a>	Preliminary
13	<a href="#">Part 2</a>	Registrar of Companies and Companies Register
16	<a href="#">Part 3</a>	Company Formation and Related Matters, and Re-registration of Company
22	<a href="#">Part 4</a>	Share Capital
28	<a href="#">Part 5</a>	Transactions in relation to Share Capital
33	<a href="#">Part 6</a>	Distribution of Profits and Assets
35	<a href="#">Part 7</a>	Debentures
38	<a href="#">Part 8</a>	Registration of Charges
44	<a href="#">Part 9</a>	Accounts and Audit
54	<a href="#">Part 10</a>	Directors and Company Secretaries
58	<a href="#">Part 11</a>	Fair Dealing by Directors
65	<a href="#">Part 12</a>	Company Administration and Procedure

76	<a href="#">Part 13</a>	Arrangements, Amalgamation, and Compulsory Share Acquisition in Takeover and Share Buy-Back
82	<a href="#">Part 14</a>	Remedies for Protection of Companies' or Members' Interests
85	<a href="#">Part 15</a>	Dissolution by Striking off or Deregistration
89	<a href="#">Part 16</a>	Non-Hong Kong Companies
92	<a href="#">Part 17</a>	Companies not Formed, but Registrable, under this Ordinance
94	<a href="#">Part 18</a>	Communications to and by Companies
96	<a href="#">Part 19</a>	Investigations and Enquiries
100	<a href="#">Part 20</a>	Miscellaneous
105	<a href="#">Part 21</a>	Consequential Amendments, and Transitional and Saving Provisions

## Annexes

108	<a href="#">Annex 1</a>	Lists of Members of the Standing Committee on Company Law Reform and the five Advisory Groups
114	<a href="#">Annex 2</a>	Major Initiatives
119	<a href="#">Annex 3</a>	List of Subsidiary Legislation

# The New Companies Ordinance (Cap. 622) Overview

The new Companies Ordinance (Cap. 622) (“new CO”) is divided into 21 parts –

- (a) **Part 1 (Preliminary)** sets out the title of the new CO, the commencement provision, and the definitions of various terms and expressions that are used in the new CO.
- (b) **Part 2 (Registrar of Companies and Companies Register)** deals with the general functions and powers of the Registrar of Companies (“the Registrar”). It groups the existing provisions relating to the office of the Registrar and the register maintained by the Registrar. It clarifies the powers of the Registrar to maintain and safeguard the integrity of the register, having regard to the development of the Companies Registry (CR)’s information system which will enable the electronic delivery of documents to or by the Registrar. This Part contains provisions for non-disclosure of residential addresses and full identity card / passport numbers in the register to enhance protection of personal data<sup>1</sup>.
- (c) **Part 3 (Company Formation and Related Matters, and Re-registration of Company)** deals with company formation, registration and related matters. This Part also provides for new requirements for the articles of association of a company following the abolition of the memorandum of association. It also makes the keeping and use of a common seal by a company optional to facilitate business operation.
- (d) **Part 4 (Share Capital)** deals with the core concepts about share capital, its creation, transfer and alteration. In particular, this Part introduces a mandatory no-par regime for all companies with a share capital to modernise the share capital regime.
- (e) **Part 5 (Transactions in relation to Share Capital)** contains the provisions concerning capital maintenance (reduction of capital and purchase of a company’s own shares) and the giving of financial assistance by a company to another party for the purpose of acquiring shares of that company or its holding company. To facilitate business operation, this Part streamlines and rationalises the existing rules by introducing new exceptions based on the solvency test for reduction of capital, buy-backs and financial assistance.
- (f) **Part 6 (Distribution of Profits and Assets)** deals with the distribution of profits and assets to members. The usual form of distribution is through payment of dividends. While there is no fundamental change to the current rules, the modernised language should facilitate easier understanding.
- (g) **Part 7 (Debentures)** deals with a miscellany of matters concerning debentures. This Part covers, for example, the register of debenture holders, rights to inspect and make copies of the register, debenture, trust deed and other documents, and meetings of debenture holders. It introduces new

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<sup>1</sup> See Remarks in Highlights on Part 2.

requirements for registration of the allotment of debentures and filing of a return of allotment, to align with similar requirements for shares.

- (h) **Part 8 (Registration of Charges)** deals with the registration of charges by both Hong Kong and registered non-Hong Kong companies. It sets out the types of charges which require registration, the registration procedures and the consequences of non-compliance. It also contains provisions to regulate related matters, such as requiring companies to keep, and allow inspection of, copies of instruments of charges and registers of charges. It introduces improvements to the current registration system, including revising the list of registrable charges and requiring a certified copy of the charge instrument to be registered and available for public inspection to enhance transparency.
- (i) **Part 9 (Accounts and Audit)** contains the accounting and auditing provisions in relation to the keeping of accounting records, the preparation and circulation of annual financial statements, directors' and auditor's reports and the appointment and rights of auditors. New provisions are introduced to facilitate SMEs to take advantage of simplified accounting and reporting requirements, to require public and large companies to include an analytical business review in directors' reports, and to enhance auditors' right to information. This Part also introduces new sanctions relating to the contents of auditor's reports.
- (j) **Part 10 (Directors and Company Secretaries)** deals with directors and company secretaries of a company. It mainly reorganises, with some modifications, the existing provisions of the Companies Ordinance (Cap. 32) relating to the appointment, removal and resignation of directors and company secretaries. This Part also clarifies the standard of directors' duty of care, skill and diligence.
- (k) **Part 11 (Fair Dealing by Directors)** covers fair dealing by directors and deals with specified situations in which a director is perceived to have a conflict of interest. It governs transactions involving directors or their connected entities which require members' approval (namely loans and similar transactions, long-term service contracts and payments for loss of office), and covers disclosure by directors of material interests in transactions, arrangements or contracts. This Part introduces new statutory provisions requiring members' approval for director's long-term employment by a company. It also requires disinterested members' approval in the case of public companies and subsidiaries of public companies.
- (l) **Part 12 (Company Administration and Procedure)** governs resolutions and meetings, registers (including registers of members, directors and company secretaries), company records, registered offices, publication of company names and annual returns. It introduces a number of changes to enhance shareholders' engagement in and the transparency of the decision-making process of a company. This Part also revises the provisions relating to registers, registered offices and annual returns to suit the needs of the modern community.

- (m) **Part 13 (Arrangements, Amalgamation, and Compulsory Share Acquisition in Takeover and Share Buy-Back)** restates, with some amendments, the provisions of Companies Ordinance (Cap. 32) concerning schemes of arrangement, reconstructions or amalgamations of a company with other companies, and compulsory acquisitions. The “headcount test” for approving a scheme of arrangement that involves a takeover offer or a general offer to buy back shares is replaced by a new requirement that the dissenting votes do not exceed 10% of the votes attaching to all disinterested shares. For other schemes, the headcount test is retained, with a new discretion given to the court to dispense with the test for members’ schemes in appropriate circumstances. It also introduces a court-free statutory amalgamation procedure for wholly-owned intra-group companies.
- (n) **Part 14 (Remedies for Protection of Companies’ or Members’ Interests)** consolidates the existing provisions concerning shareholder remedies under the Companies Ordinance (Cap. 32). The scope and operation of the unfair prejudice remedy are refined.
- (o) **Part 15 (Dissolution by Striking Off or Deregistration)** sets out the provisions on striking off and deregistration of defunct companies, restoration of companies that have been struck off or deregistered, and related matters (including treatment of properties of dissolved companies). It introduces changes which streamline the existing procedures for striking-off and restoration of companies. This Part also imposes new requirements to prevent any possible abuse of the deregistration procedure.
- (p) **Part 16 (Non-Hong Kong Companies)** deals with companies incorporated outside Hong Kong which have established a place of business in Hong Kong. There is no fundamental change to the current rules.
- (q) **Part 17 (Companies Not Formed, but Registrable, under this Ordinance)** deals with companies not formed under the new CO or a former Companies Ordinance but are eligible to be registered under the new CO. There is no fundamental change to the current rules.
- (r) **Part 18 (Communications to and by Companies)** builds on the rules governing communications by a company to another person introduced in the Companies (Amendment) Ordinance 2010. The new rules will also facilitate electronic communications by a company’s members and debenture holders to the company.
- (s) **Part 19 (Investigations and Enquiries)** deals with investigations and enquiries into a company’s affairs by inspectors and the Financial Secretary. It modernises the existing provisions by reference to similar powers under the Securities and Futures Ordinance (Cap. 571) and the Financial Reporting Council Ordinance (Cap. 588). This Part also provides a new power for the Registrar to obtain documents, records and information for the purposes of ascertaining whether any conduct that would constitute specified offences relating to giving false or misleading statement has taken place. This new power will facilitate enforcement and safeguard the integrity of the public register.

- (t) **Part 20 (Miscellaneous)** contains a number of miscellaneous provisions, including miscellaneous offences and the new power for the Registrar to compound specified offences.
  
- (u) **Part 21 (Consequential Amendments, and Transitional and Saving Provisions)** deals with the transitional and saving provisions and consequential amendments that are required for the commencement of the new CO.

# Part 1

## Preliminary

### INTRODUCTION

Part 1 of the new Companies Ordinance (Cap. 622) (“new CO”) is an introductory part that sets out the title of the new CO, its commencement, the interpretation and definitions of various terms and expressions that are used throughout the new CO, including “responsible person”, “subsidiary”, “parent undertaking” and “subsidiary undertaking”, and the types of companies that can be formed under the new CO.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 1 contains initiatives that aim at improving regulation and modernising the law, namely –

- (a) Replacing the formulation of “officer who is in default” with “responsible person” to strengthen the enforcement regime (paragraphs 4 to 7); and
- (b) Streamlining the types of companies that can be formed (paragraphs 8 to 13).

3. Apart from the above changes, Part 1 also provides for the application of the new CO to existing companies and other types of companies (paragraph 14).

Replacing the formulation of “officer who is in default” with “responsible person” to strengthen the enforcement regime (section 3)

Position under the Companies Ordinance (Cap. 32) (“Cap. 32”)

4. A number of offence provisions under Cap. 32 punish not only a company but also officers of the company who are in default. The formulation of “officer who is in default” in Cap. 32 is defined as meaning an officer or shadow director of a company who “knowingly and wilfully authorises or permits the default, refusal or contravention”. However, the “knowingly and wilfully” threshold renders prosecution against officers difficult.

Position under the new CO

5. In the new CO, a new formulation of “responsible person” is adopted to replace “an officer who is in default”, with the aim to enhance enforcement by extending the scope to cover reckless acts / omissions of officers.

Key provisions in the new CO

6. **Section 3(2)** defines a “responsible person” of a company or non-Hong Kong company as an officer or shadow director of the company or non-Hong Kong company who “authorises or permits, or participates in, the contravention or failure”<sup>1</sup>.

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<sup>1</sup> C.f. section 1121(3) of the UKCA 2006 which defines that “an officer is “in default” ...if he authorises or permits, participates in, or fails to take all reasonable steps to prevent, the contravention”.

7. **Section 3(3)** extends the scope of a “responsible person” to cover an officer or shadow director of a body corporate that is an officer or shadow director of a company or non-Hong Kong company. As a result, an officer or shadow director of the body corporate who caused the default will also be liable as a “responsible person” of the company.

### Streamlining the types of companies that can be formed (sections 7 – 12)

#### Position under Cap. 32

8. Under Cap. 32, eight different types of companies can, in theory, be formed according to their capacity to raise funds from outside sources, the ability of members to freely transfer their shares and the methods by which the liability of members is determined. They are –

- (a) private companies limited by shares;
- (b) non-private companies limited by shares;
- (c) private companies limited by guarantee without a share capital;
- (d) non-private companies limited by guarantee without a share capital;
- (e) private unlimited companies with a share capital;
- (f) non-private unlimited companies with a share capital;

- (g) private unlimited companies without a share capital; and
- (h) non-private unlimited companies without a share capital.

#### Position under the new CO

9. To streamline the types of companies that can be formed, the following changes are made –

- (a) unlimited companies without a share capital (whether private or non-private, i.e. (g) and (h) in paragraph 8 above) are obsolete and are abolished because it is very unlikely that such type of companies will be formed in the future and there is currently no such company on the Companies Registry’s register;
- (b) companies limited by guarantee without a share capital (whether private or non-private, i.e. (c) and (d) in paragraph 8 above) have become a separate category of companies. They are generally treated in a manner similar to public companies with appropriate modifications. For example, like public companies, all guarantee companies will be required to file audited accounts; and
- (c) non-private companies are expressly referred to as “public companies” which are defined to mean companies other than private companies or guarantee companies.

10. As a result, the types of companies that may be formed under the new CO are reduced to five. Sections 7 to 12 provide for the definitions whereas section 66 in Part 3 sets out the types of companies that may be formed under the new CO, namely –

- (a) private companies limited by shares;
- (b) public companies limited by shares;
- (c) private unlimited companies with a share capital;
- (d) public unlimited companies with a share capital; and
- (e) companies limited by guarantee without a share capital.

#### Key provisions in the new CO

11. **Sections 7 and 10** provide that a limited company is a company limited by shares or by guarantee, and an unlimited company is a company with no limit on the liability of its members. **Section 8** provides that a company is a company limited by shares if the liability of its members is limited by the company's articles to any amount unpaid on the shares held by the members.

12. **Sections 11 and 12** provide for the definitions of private and public companies. The required characteristics of a private company are the same as those currently provided under section 29 of Cap. 32 (i.e. a company is a private company if its articles restrict members' rights to transfer shares, limit the number of members to 50, and prohibit any invitation to the public to subscribe for any shares or debentures.) A company is a public company if it is not a private company or a company limited by guarantee.

13. **Section 9(1)** provides that a company is a company limited by guarantee if it does not have a share capital and if the liability of its members is limited by the company's articles to the amount that the members undertake to contribute to the assets of the company in the event of its being wound up. **Section 9(2)** makes it clear that a company limited by guarantee and having a share capital formed under Cap. 32 before 13 February 2004 (i.e. the date when such type of company was abolished under section 4(4) of Cap. 32), will be regarded as a guarantee company under the new CO although it has a share capital.

#### **Application of the new CO to existing companies and other types of companies**

##### Key provisions in the new CO

14. **Sections 17 and 18** provide that the new CO applies to an existing company (i.e. a company formed and registered under a former Companies Ordinance) and an unlimited company registered as a limited company pursuant to Cap. 32 or section 58 of Companies Ordinance 1911. The new CO also applies to companies registered but not formed under a former Companies Ordinance (**Section 19**).

## Part 2

# Registrar of Companies and Companies Register

### INTRODUCTION

Part 2 (Registrar of Companies and Companies Register) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to the Registrar of Companies (“the Registrar”), the Companies Register and the registration of documents by the Registrar.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 2 contains initiatives that aim at improving regulation, facilitating business and modernising the law, namely, –

- (a) Clarifying the Registrar’s powers in relation to the registration of documents (paragraphs 4 to 6);
  - (b) Clarifying and enhancing the Registrar’s powers in relation to the keeping of the Companies Register (paragraphs 7 to 10 );
  - (c) Providing expressly for removing information on the Companies Register (paragraphs 11 to 13); and
  - (d) Withholding residential addresses of directors and company secretaries and full identification numbers of individuals from public inspection. [Please see remarks on page 15]
3. The details of the major changes in Part 2 are set out in paragraphs 4 to 13 below.

**Clarifying the Registrar’s powers in relation to the registration of documents (Sections 31, 35 to 38)**

Position under the Companies Ordinance (Cap. 32) (“Cap. 32”)

4. Under section 348 of Cap. 32, the Registrar may refuse to register a document if it is manifestly unlawful or ineffective, or is incomplete or altered; or if any signatures on the document, or digital signature accompanying the document is incomplete or altered. The scope for refusal of registration is not entirely clear.

Position under the new CO

5. The grounds of refusal are clarified to empower the Registrar to refuse to register an unsatisfactory document or to withhold registration of a document pending further amendments or provision of further particulars.

Key provisions in the new CO

6. **Section 31** sets out the situations where a document is considered to be unsatisfactory. It consolidates and clarifies the existing grounds on which the Registrar may refuse the registration of a document. For example, it is expressly provided that a document is unsatisfactory if it is internally inconsistent or inconsistent with the information already on the Companies Register. **Section 35** makes it clear that if the Registrar refuses to accept a document, has not received a document or refuses to register a document, the document is to be regarded as not having been delivered to the Registrar as required under the new CO.

**Section 36** further provides that the Registrar may withhold the registration of an unsatisfactory document and request the person who delivered the document to take certain remedial actions within a specified period, such as producing further information or evidence, amending or completing the document or applying for a court order.

### Clarifying and enhancing the Registrar's power in relation to the keeping of the Companies Register (Sections 39 to 44)

#### Position under Cap. 32

7. At present, the Registrar adopts administrative measures in appropriate cases to accept the filing of "amended" documents to rectify documents which contain errors and to annotate the information on the Companies Register so as to provide supplementary information.

#### Position under the new CO

8. The following powers of the Registrar are put on an express statutory footing and are provided for expressly –

- (a) power to annotate information on the Companies Register to provide supplementary information such as the fact that the document in question has been replaced or corrected; and

- (b) power to request companies or their officers to resolve inconsistencies in information on the Companies Register or to provide updated information.

#### Key provisions in the new CO

9. **Section 39** enables the Registrar to notify a company of an apparent inconsistency in the information relating to the company on the Companies Register and to require it to take steps to resolve the inconsistency within a specified period. **Section 40** empowers the Registrar to require a person to update his or her information on the Companies Register. Under both provisions, failure of the company and every responsible person concerned to comply with the Registrar's requirements is an offence. It is a defence to establish that the person took all reasonable steps to secure compliance with the requirements.

10. **Section 41** gives the Registrar power to, either on her own initiative or on an application by a company, rectify a typographical or clerical error contained in any information on the Companies Register. If the rectification is made upon an application by a company, the Registrar may rectify the error by registering a document showing the rectification delivered by the company. **Section 44** provides that the Registrar may make a note in the Companies Register for the purpose of providing information in relation to such a rectification.

## Providing expressly for the power of the Court to remove information from the Companies Register (Section 42)

### Position under Cap. 32

11. There is no express provision in Cap. 32 on the court's power to order the Registrar to remove inaccurate or forged information from the Companies Register. However, it has been decided by the court that in an appropriate case, the court may direct the Registrar to remove a document from the Companies Register or to accept a document for registration.

### Position under the new CO

12. An express provision has been introduced to provide that the court may order the removal of any information from the Companies Register.

### Key provisions in the new CO

13. **Section 42** provides that the court may, on application by any person, direct the Registrar to rectify any information on the Companies Register or to remove any information from it if the court is satisfied that the information is inaccurate or forged, or derives from anything that is invalid or ineffective or that has been done without the company's authority. When making an order of removal of any information from the Companies Register, the court may make any consequential order that appears just with respect to the legal effect, if any, to be accorded to the information by virtue of its having appeared on the Companies Register.

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### Remarks

As some members of the public have raised concerns about the new arrangement with respect to inspection of directors' personal information on the Companies Register, the Administration has submitted a paper on the proposed way forward to the LegCo Panel on Financial Affairs on 28 March 2013 (LC Paper No. CB(1)788/12-13(01), whereas the Panel has subsequently discussed the matter at its meeting on 8 April 2013. Having regard to the discussion at that meeting and members' views, the Administration will accord priority to the tasks necessary for commencing the new CO in the first quarter of 2014 as scheduled, and consider matters relating to the new arrangement thereafter. The Gazette notice for the commencement of the new CO does not include provisions relating to the restricted disclosure of residential addresses of directors and identification numbers of individuals.

# Part 3

## Company Formation and Related Matters, and Re-registration of Company

### INTRODUCTION

Part 3 (Company Formation and Related Matters, and Re-registration of Company) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to company formation and registration, re-registration of unlimited companies as companies limited by shares and related matters.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 3 contains initiatives that aim at facilitating business operation and modernising the law, namely –

- (a) Abolishing the Memorandum of Association (paragraphs 5 to 11);
- (b) Reforming company re-registration provisions (paragraphs 12 to 14);
- (c) Providing statutory protection for persons dealing with a company (paragraphs 15 to 17);
- (d) Making the keeping and use of a common seal optional and relaxing the requirements for a company to have an official seal for use abroad (paragraphs 18 to 20); and
- (e) Widening the scope of documents an attorney can execute on behalf of a company locally or outside Hong Kong (paragraphs 21 and 22).

3. The details of the major proposals in Part 3 are set out in paragraphs 5 to 22 below.

4. Apart from the above major proposals, Part 3 also provides for a company to appeal to the Administrative Appeals Board instead of to the court against a direction issued by the Registrar of Companies (“the Registrar”) concerning the company’s name (paragraphs 23 and 24 below) as suggested by Members of the Bills Committee on the Companies (Amendment) Bill 2010. In addition, it sets out the types of companies that may be formed. It also incorporates changes introduced through the Companies (Amendment) Ordinance 2010, which provided for an improved company name registration system following the implementation of the new electronic company registration and filing of document services.

#### **Abolishing the Memorandum of Association (“MA”) (Sections 67 to 70, 75 to 85 and 98)**

#### Position under the Companies Ordinance (Cap. 32) (“Cap. 32”)

5. Under Cap. 32, the constitutional documents of a company formed in Hong Kong are the MA and the articles of association (“AA”). The MA used to contain the objects clause of the company. However the objects clause of a company is now less significant given the abolition of the doctrine of ultra vires in relation to corporate capacity in 1997 and all companies now have the capacity and rights of a natural person. As all the information provided on incorporation apart from the objects clause and the authorised

capital<sup>1</sup> (which will be removed following the migration to no par) is contained in the AA and the incorporation form, the need to retain the MA as a separate constitutional document has diminished.

6. Under section 9 of Cap. 32, a company limited by shares may register AA upon incorporation. These may be bespoke AA. Section 11 of Cap. 32 provides that for such a company if no AA are registered, or if registered, in so far as they do not exclude or modify the regulations set out in Table A of the First Schedule to Cap. 32, the said regulations set out in Table A will be the AA of the company. Section 9 of Cap. 32 requires a company limited by guarantee and an unlimited company to register AA on incorporation. Tables C and E of the First Schedule to Cap. 32 provide the statutory forms of AA for these companies.

#### Position and key provisions under the new CO

7. The new CO abolishes the requirement for an MA. **Section 67** states that person(s) may form a company by, amongst other things, delivering to the Registrar for registration an incorporation form in specified form and a copy of the company's AA. **Sections 67 to 70** and **75 to 85** set out the requirements of the incorporation form and the AA respectively. Subject to the amendments in the new CO, these will include all the information currently contained in the MA. These provisions of the new CO provide mandatory AA that a company **must** have.

8. **Section 78** empowers the Financial Secretary ("FS") to prescribe different model AA for different types of companies. These model AA replace Table A and the other tables in the First Schedule to Cap. 32 for companies incorporated after the commencement of the new CO, and will be in addition to the mandatory AA that a company must have. **Section 79** of the new CO provides that a company may adopt as its articles all or any of the provisions of the model AA prescribed for the type of company to which it belongs and **section 80** of the new CO provides that the appropriate model AA will apply in so far as the articles of a company do not exclude or modify the model AA. Therefore, if a company does not register any additional articles upon incorporation, the model AA prescribed for that type of company will apply. The Companies (Model Articles) Notice (Cap. 622H) prescribes model AA for public companies limited by shares, private companies limited by shares and companies limited by guarantee.

9. As a result of the migration to no par, the authorised share capital requirement will be removed but **section 85(2)** provides that a company having a share capital **may** state in its AA the maximum number of shares that it may issue.

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<sup>1</sup> Authorised capital is the maximum amount, usually specified in monetary terms, that a company is permitted by its constitutional document to raise by issuing shares. Shares can but need not be issued up to the authorised level.

10. **Sections 88 and 96** require companies to notify the Registrar of any alterations to the AA, including alterations by an order of the court. **Section 89** allows a company to alter its objects set out in its AA and **section 91(1)** gives members of private companies the right to apply to the court in certain circumstances to object to the resolutions for altering the provisions of the company's AA with respect to its objects. **Section 90** provides for the alteration of Cap. 32 section 25A type conditions in an existing private company's AA and **section 91(3)** preserves the right of members of an existing private company to object to the resolutions for altering such conditions.

11. **Section 98** provides that conditions (i.e. provisions) of the MA of an existing company (i.e. a company formed and registered under Cap. 32 or a former Ordinance), such as objects clause (if any) and members' liability, will be deemed to be regarded as provisions of the company's AA. **Section 98(4)** provides however that any condition contained in the MA of an existing company stating the authorised share capital of the company or dividing the share capital of the company into shares of a fixed amount is regarded as deleted. This is again a result of the migration to no-par.

## Reforming company re-registration provisions (Sections 94 and 95, 130 to 132)

### Position under Cap. 32

12. The provisions concerning re-registration of unlimited companies as limited companies are set out in section 19 of Cap. 32, and the provisions on private companies changing to public companies are set out in section 30 of Cap. 32. The provisions are outdated and unnecessarily detailed. For example, the requirement to file a prospectus or a statement in lieu of prospectus (i.e. the Second Schedule to Cap. 32) under section 30 of Cap. 32 is unduly onerous and serves no useful purpose<sup>2</sup>.

### Position and key provisions under the new CO

13. Part 3 of the new CO simplifies the provisions under Cap. 32. **Section 94** provides for alteration of the AA which changes the status of a private company. The company must deliver to the Registrar within 15 days after the date on which the alteration takes effect a copy of the company's annual financial statement prepared for the financial year immediately preceding the financial year in which the alteration of the AA is made. The requirement to file a statement in lieu of a prospectus has been removed. **Section 95** further provides for alteration of the AA which changes the status of a public company to that of a private company.

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<sup>2</sup> It serves no useful purpose for companies merely re-registering as public companies without going forward to raise funds. In any event, prospectuses would be required in the case of public companies going to raise funds.

14. **Section 130** provides for the matters in section 19(1) of Cap. 32 with the modification that an unlimited company may only re-register as a company limited by shares under the new CO. There must be a statement on the share capital structure, which after re-registration must conform to the requirements in the new CO. **Section 131** deals with how the application for re-registration should be made, and **section 132** provides for a fresh certificate of incorporation to be issued by the Registrar to the company after the re-registration.

### Providing statutory protection for persons dealing with a company (Sections 116 to 119)

#### Position under Cap. 32

15. There are no such provisions under Cap. 32.

#### Position and key provisions under the new CO

16. **Section 116** provides that a company's exercise of powers will be limited by its AA after the elimination of the MA. To supplement the provision, we have made reference to sections 40 to 42 of the United Kingdom Companies Act 2006 ("UKCA 2006") and added **sections 117 to 119** to provide statutory protection for persons dealing with a company in addition to the common law indoor management rule<sup>3</sup>. **Section 117** provides that in favour of a person dealing with a company in good faith, the power of the directors to bind the company will be deemed to be free of any limitation under the AA, any resolutions of the company or any agreement between the members of the company.

17. **Sections 118 and 119** provide that the protection afforded to a person by **section 117** will not apply where the party to a transaction with a company is an "insider" (for example, a director of the company or of a holding company of the company; or an entity connected with such a director); or where the company in question is an exempted company<sup>4</sup>, unless the person is unaware, at the time that the act is done, that the company is an exempted company or unless the exempted company has received full consideration in respect of the act done, and the person is unaware that the act in question is not permitted by any relevant document of the exempted company or is beyond the powers of the directors.

### Making the keeping and use of a common seal optional and relaxing the requirements for a company to have an official seal for use abroad (Sections 124, 125 and 127)

#### Position under Cap. 32

18. Section 93(1)(b) of Cap. 32 stipulates that every company shall have a common seal with the company name engraved in legible characters. Further, for a company to have an official seal for use outside Hong Kong, there must be authorisation by the AA and the company must have objects which require or comprise the transaction of business outside Hong Kong.

<sup>3</sup> Also known as the "rule in *Turquand's case*", i.e. the rule that a third party dealing in good faith with a company is not bound to inquire whether acts of internal management have been regular and is entitled to presume that acts within the company's constitution and powers have been properly and duly performed, see *Royal British Bank v Turquand* (1856) 119 ER 886.

<sup>4</sup> An exempted company refers to a company permitted to be registered by a name without "Limited" as the last word of the name, see section 103 of the new CO, and that is exempt from tax under section 88 of the Inland Revenue Ordinance (Cap. 112). It is essentially the same as a "section 21 company" under Cap. 32.

### Position and key provisions under the new CO

19. To facilitate business, it is necessary to simplify the mode of execution of documents by making the keeping and the use of a common seal optional. **Section 124** states that a company may have a common seal. This gives flexibility to companies and does not prejudice those companies which may still wish to keep and use their common seals. In connection with the change, **section 127** sets out the requirements for execution of documents by a company. In particular, **section 127(3)** allows a company to execute a document (in the case of a company with only one director) by having the document signed by the director or (in the case of a company having two or more directors) by two authorised signatories. **Section 127(5)** also provides that a document signed in accordance with **section 127(3)** and expressed to be executed by the company has effect as if the document had been executed under the company's common seal.

20. **Section 125** states that a company may have an official seal for use outside Hong Kong, removing the current restrictive requirements.

### **Widening the scope of documents an attorney can execute on behalf of a company locally or outside Hong Kong (Section 129)**

#### Position under Cap. 32

21. Under Cap. 32, an attorney can only bind a company in respect of deeds executed by him on its behalf outside Hong Kong. This is unduly restrictive taking into account the increasing volume of local and overseas business activities.

### Position and key provisions under the new CO

22. **Section 129** widens the scope by stating that a company may authorise any person as its attorney to execute a deed or any other document on its behalf in Hong Kong or elsewhere.

### **Allowing a company to appeal to the Administrative Appeals Board instead of to the court (Section 109)**

#### Position under Cap. 32

23. Under Cap. 32, where the Registrar is satisfied that the name of a company gives so misleading an indication of the nature of its activities as to be likely to do harm to the public, or that the name constitutes a criminal offence, or that it is offensive or otherwise contrary to the public interest, the Registrar may direct the company to change its name under section 22A of Cap. 32. The company may apply to the court to set the direction aside.

### Position and key provisions under the new CO

24. At the meeting of the Bills Committee on the Companies (Amendment) Bill 2010, Members suggested that a company should be allowed to appeal to the Administrative Appeals Board, instead of to the court, against a change-of-name direction / notice issued by the Registrar in view of the cost and time involved in court proceedings. The Administration agrees with the suggestion. For local companies, the relevant changes have been incorporated in **section 109**.

## ACTIONS TO BE TAKEN BY STAKEHOLDERS

25. With the deeming provisions set out in the new CO for abolition of the MA, there is no need for companies to do anything in this respect. However, companies may wish to take the opportunity at this time review their current constitutional documents to take advantage of some of the new initiatives set out in the new CO, for example the new provisions making the company seal optional, and to ensure that the provisions of their AA comply with the provisions of the new CO.

26. There are changes in the law as a result of the new CO which may impact upon the provisions of a company's AA. A list of provisions in AA which will be void as a result of the new CO is available at the Companies Registry's website at [www.cr.gov.hk](http://www.cr.gov.hk) under the "New Companies Ordinance" section. If in doubt about any provisions companies should seek their own legal advice.

## TRANSITIONAL AND SAVING ARRANGEMENTS

27. There are no transitional arrangements for abolition of the MA and the deeming provisions as set out in section 98 of the new CO have been explained in paragraph 11 above. This will affect all existing companies as at the date of commencement of the new CO. For other changes made under this Part, the general transitional provisions are that for actions commenced under Cap. 32 and in progress when the new CO commences, Cap. 32 provisions will continue to apply. For actions commenced on or after the commencement date of the new CO, the new CO provisions will apply. For the detailed transitional provisions please refer to **sections 3 to 12 of Schedule 11** to the new CO.

# Part 4

## Share Capital

### INTRODUCTION

Part 4 (Share Capital) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to the core concept of “share capital” and its creation, transfer and alteration.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 4 contains initiatives that aim at modernising the law (subparagraphs (a) and (b) below), enhancing corporate governance (subparagraphs (c) and (d)), ensuring better regulation (subparagraph (e)), and facilitating business operation (subparagraphs (f) and (g)), namely –

- (a) Adopting a mandatory system of no-par for all companies with a share capital (paragraphs 4 to 9);
- (b) Removing the power of companies to issue share warrants to bearer (paragraphs 10 to 12);
- (c) Extending the requirement of shareholders’ consent for allotments of shares to the grants of rights to subscribe for, or to convert securities into, shares (paragraphs 13 to 14);

- (d) Requiring a company to give reasons explaining its refusal to register a transfer of shares upon request (paragraphs 15 to 16);
- (e) Requiring a company to deliver to the Companies Registry (“CR”) a return or notification, including a statement of capital whenever there is a change to its capital structure (paragraphs 17 to 19);
- (f) Clarifying and simplifying the requirements relating to class rights (paragraphs 20 to 23); and
- (g) Simplifying the publication procedures for replacement of lost share certificate of a listed company (paragraphs 24 to 25).

3. The details of the above major changes in Part 4 are set out in paragraphs 4 to 25 below.

#### **Adopting a mandatory system of no-par for all companies with a share capital (Section 135 and Division 2 of Part 4 of Schedule 11)**

#### Position under the Companies Ordinance (Cap. 32) (“Cap. 32”)

4. Par value (also known as “nominal value”) is the minimum price at which shares can generally be issued. Companies incorporated in Hong Kong under Cap. 32 and having a share capital are required to have a par value ascribed to their shares.

### Position under the new CO

5. The par value does not serve the original purpose of protecting creditors and shareholders, and in fact may even be misleading because the par value does not necessarily give an indication of the real value of the shares. The new CO adopts the mandatory system of no-par and abolishes relevant concepts such as nominal value, share premium, and requirement for authorised capital. Deeming provisions are introduced to ensure that contractual rights defined by reference to par value and related concepts will not be affected by the abolition of par (see paragraph 9 below). The deeming provisions will save considerable work, expense and time for companies and reduce the possibility of disputes. It will not prevent individual companies from reviewing their documents and introducing more specific changes having regard to their own circumstances before the new CO comes into force.

### Key provisions in the new CO

6. **Section 135** abolishes the concept of nominal value. Upon the commencement of that section, a company's shares will have no nominal value. This will apply to all shares, including shares issued before that day. It is expected that the new CO will take effect in 2014 after enactment of all subsidiary legislation. The "no-par" regime will take effect at the same time. (Please also see the deeming provisions in paragraph 9 below).

7. **Section 170**, modified from section 53 of Cap. 32, empowers a company to alter its share capital in a number of ways under a no-par environment, e.g. to allow a company to capitalize its profits without issuing new shares and to allot and issue bonus shares without increasing share capital.

8. With the abolition of nominal value, "share premium" will no longer exist. Provisions based on this concept will be modified. **Section 37 of Schedule 11** (Transitional and Saving Provisions) is a legislative deeming provision for the amalgamation of the existing share capital amount with the amount in the company's share premium account (and also capital redemption reserve) immediately before the migration to no-par. **Section 38 of Schedule 11** is to preserve substantially the currently permitted uses of the share premium for the amount standing to the credit of the share premium account before the migration to no-par. As for the position after the migration to no-par, **section 149** of the new CO provides that a company may apply its capital in writing off the preliminary expenses of the company, commission paid or any other expenses of any issue of shares. **Sections 194 to 199** modify the merger and group reconstruction relief under sections 48C to 48E of Cap. 32, so that the two types of relief may operate in a no-par environment.

9. **Sections 35 to 41 of Schedule 11** contain transitional provisions relating to migration from shares having nominal value to shares having no nominal value. The provisions (particularly the statutory deeming provision in **section 40**) are intended to provide legislative safeguards to ensure that contractual rights defined by reference to par or nominal value and related concepts will not be affected by the migration to no-par.

### Removing the power of companies to issue share warrants to bearer (Section 139 and section 14 of Schedule 11)

#### Position under Cap. 32

10. Under section 73 of Cap. 32, a non-private company limited by shares is allowed to issue “share warrants to bearer” (i.e. a warrant stating that the bearer of the warrant is entitled to the shares specified in it, also known as bearer shares)<sup>1</sup>. It is possible for legal title to shares to be transferred merely by physical delivery of the warrant.

#### Position under the new CO

11. Share warrants are rarely issued nowadays and are undesirable from the perspective of anti-money laundering because of the lack of transparency in the recording of their ownership and the manner by which they are transferred. Under the new CO, the power of companies to issue share warrants to bearer is removed.

#### Key provisions in the new CO

12. **Section 139** repeals a company’s power to issue “share warrants to bearer” while providing that share warrants issued prior to the commencement of that section would be grandfathered, so that upon the surrender of such existing share warrants, the bearer’s name will be registered in the company’s register of members. The section partially restates section 97 of Cap. 32 to provide for the surrender of share warrants. **Section 14 of Schedule 11** provides that the records in the register of members in respect of existing share warrants would be preserved until the share warrants are surrendered.

### Extending the requirement of shareholders’ consent for allotments of shares to the grants of rights to subscribe for, or to convert securities into, shares (Sections 140 and 141)

#### Position under Cap. 32

13. The allotment of shares is generally carried out by directors. Under section 57B of Cap. 32, directors are only entitled to do that with prior approval of the company in a general meeting. The requirement of shareholders’ approval is mandatory and notwithstanding any provision in the company’s articles to the contrary. There are only two exceptions to this rule, namely, (a) a rights issue; and (b) an allotment to the founder members (section 57B(1) and (7) of

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<sup>1</sup> “Share warrants to bearer” are different from “warrants” listed on the stock exchange. “Share warrants to bearer” are an alternative form of title document evidencing the ownership of shares. “Warrants” listed on the stock exchange, on the other hand, are instruments which only give an investor the right to buy or sell the underlying shares. Moreover, “share warrants to bearer” enable the shares specified in it to be transferred by delivery of the warrant. “Warrants” listed on the stock exchange may be traded, but their transfer simply gives the transferee a right to buy or sell the underlying shares and does not make him or her a member until the option is exercised.

Cap. 32). However, section 57B only requires shareholders' approval for the allotment of shares, but not the grant of an option to subscribe for shares or a right to convert any securities into shares. It is only the subsequent exercise of the option or the right of conversion that would result in an allotment which would require shareholders' approval.

#### Position and key provisions in the new CO

14. To enhance protection of minority shareholders against dilution, **sections 140 and 141** extend the requirement of shareholders' approval for allotments of shares to the grants of rights to subscribe for, or to convert securities into, shares. If approval is given for the grant of an option, there would not be a need to obtain further approval of the allotment of shares pursuant to that option.

#### **Requiring a company to give reasons explaining its refusal to register a transfer of shares upon request (Section 151(3) and (4))**

##### Position under Cap. 32

15. Section 69(1) of Cap. 32 requires a company which refuses to register transfer of shares or debentures to send a notice of such refusal to the transferor and transferee within two months after the transfer was lodged with the company.

#### Position and key provisions in the new CO

16. Currently, there is no requirement for the notice to be accompanied by the reasons for the refusal. **Section 151(3) and (4)** require companies to give reasons explaining their refusal to register a transfer of shares upon request and within 28 days after receiving the request, so as to enhance transparency and to ensure that directors only exercise their powers for proper purposes.

#### **Requiring a company to deliver to the CR a return or notification including a statement of capital whenever there is a change to its capital structure (Section 201)**

##### Position under Cap. 32

17. A statement of capital is in essence a "snapshot" of a company's total subscribed capital at a particular point in time. Under Cap. 32, the capital structure of a company can only be ascertained by searching through a number of documents on the register, e.g. the annual return, any return of allotment filed since the annual return, any documents filed in relation to, e.g. a permitted reduction of capital. It is therefore not easy to ascertain the capital structure at a specific moment in time without a thorough check of the register.

## Position and key provisions in the new CO

18. Under Cap. 32, information on a company's share capital structure in the public register may not be up-to-date. The new CO requires a company to deliver to the CR such a statement to be contained in a return or notification, whenever there is a change to its capital, e.g. where there is an allotment of shares (**section 142**) or a permitted alteration of share capital (**section 171**). A statement of capital will show the company's share capital information as at the time the company has so changed its share capital.

19. **Section 201** sets out the information to be contained in a statement of capital. This new requirement enhances the requirements under Cap. 32 for notification to the CR of changes of a company's share capital. This will ensure that the public register contains up-to-date information on a company's share capital structure.

## **Clarifying and simplifying the requirements relating to class rights (Sections 176 to 193)**

### Position under Cap. 32

20. Sections 63A and 64 of Cap. 32 set out the requirements for a variation of class rights of shareholders. Cap. 32 does not define the concept of class rights, which gives rise to some uncertainties. Section 63A is also complicated in relation to the procedures for variation, which differ depending on where the class rights are provided for, and whether the articles contain a procedure for variation. Under section 63A, variation of class rights needs to follow any requirements set out in the articles. If the articles do not contain the requirements, then section 63A requires different types of approvals (e.g. approved by members holding 75% of the shares or approval by all members) depending on whether the rights are set out in the memorandum. Cap. 32 is silent in the case of companies without a share capital.

## Position and key provisions in the new CO

21. For companies with share capital, the provisions on class rights under **sections 176 to 184** refer to "rights attached to shares in a class of shares". This clarifies that the concept of class rights is restricted to rights attached to shares. Also, **section 177** clarifies that class rights are the rights conferred on the holder of a share as a member of the company. To provide further guidance on the meaning of a class of shares, **section 178** provides that shares are in a class if the rights attached to them are in all respects uniform, and are not regarded as different only because the shares do not carry the same rights to dividends in the first 12 months immediately after allotment.

22. **Section 180** sets out the procedural requirements for the variation of the rights of a class of members of a company having a share capital, i.e. the rights may be varied in accordance with the articles or with 75% consent or special resolution of the class members. This simplifies the Cap. 32 procedures mentioned in paragraph 20 above. **Section 181** requires the company to notify each class member if the rights of the class are varied. **Section 182** allows members holding at least 10% of the total voting rights of the class to apply to the Court of First Instance to have a variation disallowed. **Section 184** requires the company to notify the CR with a specified form (including a "statement of capital") of a variation within one month after the variation takes effect.

23. **Sections 185 to 192**, mirroring the corresponding provisions in **sections 176 to 184**, provide for variation of class rights for companies without a share capital. This fills the gap in Cap. 32 which is silent in the case of companies without a share capital.

## Simplifying the publication requirements relating to the replacement of lost share certificate of a listed company (Sections 162 to 169)

### Position under Cap. 32

24. Section 71A of Cap. 32 provides that where a person applies to the company for replacement of a lost certificate, the company has to publish a notice before issuing the new certificate. If the value of the shares does not exceed the threshold amount of \$20,000, the notice shall be published once in an English and Chinese newspaper respectively; if it exceeds \$20,000, the notice shall be published in the Gazette once in each of three consecutive months. The listed company is also required to publish a notice in the Gazette after the new certificate is issued.

### Position and key provisions in the new CO

25. Given the cost involved in publishing a notice, some consider that the threshold amount should be raised and the publication requirements streamlined. **Sections 162 to 169** based on section 71A of Cap. 32 simplify the publication requirements, taking account of developments in information technology (e.g. website publication). Under **section 164**, for cases where the value of the shares is below \$200,000 (instead of \$20,000 in Cap. 32), the notice will be published on the listed company's website for one month (instead of newspapers in Cap. 32). For cases where the value of shares is at or above \$200,000, the notice will be published on the listed company's website for three months and once in the Gazette within one month after the company has first published the notice on its own website (instead of publishing the notice in the Gazette once in each of three consecutive months under Cap. 32). For cases where the value of the shares is below \$200,000, the listed company is no longer required to publish a notice in the Gazette after the new certificate is issued. The notice may be published on its website.

## ACTIONS TO BE TAKEN BY STAKEHOLDERS

26. Despite the comprehensive transitional provisions for existing companies, individual companies may wish to review their particular situation before commencement of the new CO to determine whether or not they need to introduce more specific changes to their documents as a result of the migration to the no-par regime. For example companies may review their constitutional documents, contracts entered into by the company, trust deeds involving the company and share certificates issued by the company to see if they require to make any specific changes. Companies are advised to seek independent legal advice as they see fit.

## TRANSITIONAL AND SAVING ARRANGEMENTS

27. The transitional arrangements for migration to a mandatory system of no-par are explained in paragraphs 8 and 9. The transitional arrangements for removing the power of companies to issue share warrants to bearer are explained in paragraph 12. The other major changes described in these Highlights apply to activities carried out after the commencement date of the new CO. For activities which started under Cap. 32 and are in progress when the new CO commences, the Cap. 32 provisions will continue to apply.

# Part 5

## Transactions in relation to Share Capital

### INTRODUCTION

Part 5 (Transactions in relation to Share Capital) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions concerning “capital maintenance” (reduction of capital and purchase of own shares (“buy-backs”)) and related rules (financial assistance by a company for the purpose of acquiring shares in the company or its holding company).

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 5 contains initiatives that aim at facilitating business operation, namely –

- (a) Adopting a uniform solvency test based on cash-flow for different types of transactions under this Part (paragraphs 4 to 8);
- (b) Introducing an alternative court-free procedure for reduction of capital based on a solvency test (paragraphs 9 to 11);
- (c) Allowing all companies to purchase their own shares out of capital, subject to a solvency test (paragraphs 12 to 15);
- (d) Allowing all types of companies (listed or unlisted) to provide financial assistance for acquisitions of the companies’ shares, subject to satisfaction of the solvency test and certain specified procedures (paragraphs 16 to 20); and
- (e) Relaxing the rules on giving of financial assistance for the purposes of employee share schemes (paragraphs 21 to 22).

3. The details of the above major changes in Part 5 are set out in paragraphs 4 to 22 below.

### Adopting a uniform solvency test based on cash-flow for different types of transactions under this Part (Sections 204 to 208)

#### Position under the Companies Ordinance (Cap. 32) (“Cap. 32”)

4. Under Part II of Cap. 32, a solvency test is provided for in respect of –

- (a) buy-backs of its own shares out of capital by a private company (requirements of the solvency test are set out in section 49K(3), (4) and (5)); and
- (b) financial assistance by an unlisted company for the purpose of an acquisition of shares in the company or its holding company (requirements of the solvency test are set out in section 47F(1)(d) and (2)).

5. Both solvency tests are based on cash flow alone, but there are minor differences between them, as follows –

- (a) for buy-backs, under section 49K(5), the solvency statement has to be accompanied by an auditors’ report; and
- (b) for financial assistance, section 47F(1)(d)(i) has an additional requirement for the solvency statement which provides for the situation where the company intends to commence winding up within 12 months of the date of the proposed financial assistance.

### Position under the new CO

6. There is discrepancy in the solvency tests applicable to buy-backs and financial assistance under Cap. 32. It is desirable to adopt a uniform solvency test for buy-backs and financial assistance, and extend its application to the court-free procedure for reduction of capital, for consistency in the law. The new CO adopts the approach for financial assistance set out in section 47F(1)(d) (see paragraph 5(b) above), as it can give clarity and certainty on how the solvency test may apply in different scenarios.

7. Under the new CO, there is no requirement for attaching an auditors' report to the solvency statement. Auditors would not be in a better position than the directors in ascertaining the company's solvency which involves forward-looking business judgments. Directors should be expected to have reasonable grounds in forming their opinion as to the company's solvency and judgment in deciding whether professional assistance is needed. Requiring an auditors' report in every case would add expense and cause delay for relatively little gain.

### Key provisions in the new CO

8. **Section 204** provides that a uniform solvency test will be applicable to all three categories of transactions, namely reduction of capital, buy-backs and financial assistance. **Section 205** sets out the content of the uniform solvency test, which in substance, re-enacts section 47F(1)(d) of Cap. 32. **Section 206** provides for the making of a solvency statement by the directors who have formed the opinion that the company satisfies the solvency test in

relation to the transaction concerned. In forming his or her opinion, a director must inquire into the company's state of affairs and prospects and take into account contingent and prospective liabilities of the company. The solvency statement must be made and signed by all directors for buy-backs and reductions of capital, and made and signed by a majority of directors for financial assistance.

### **Introducing an alternative court-free procedure for reduction of capital based on a solvency test (Sections 215 to 225)**

#### Position under Cap. 32

9. Cap. 32 only allows a reduction of share capital if there is approval by the shareholders via a special resolution and if the reduction is approved by the court (sections 58 to 63). In determining whether to approve the reduction, the court would consider various factors, including whether the reduction is equitable between shareholders and whether creditors' interests are safeguarded. Court approval is not required if the sole purpose of the reduction is to re-designate the nominal value of shares to a lower amount (section 58(3)).

#### Position under the new CO

10. The new CO introduces, as an alternative procedure, a general court-free procedure based on the solvency test which would be faster and cheaper and can be utilised by all companies.

### Key provisions in the new CO

11. **Sections 215 to 225** provide for the said court-free procedure, subject to compliance with the solvency test. The key features of the procedure include –

- (a) all the directors need to sign the solvency statement in support of the proposed reduction (**section 216**);
- (b) the company needs to obtain members' approval by a special resolution (**sections 215 and 217**);
- (c) the company must publish notices with relevant information in the Gazette and newspapers and must register the solvency statement with the Registrar of Companies ("the Registrar") (**section 218**);
- (d) any creditor or non-approving member of the company may, within five weeks after the special resolution is passed, apply to the court for cancellation of the resolution (**sections 220 to 222**). During this five-week period, the company must make available the special resolution and solvency statement for members' and creditors' inspection (**section 219**); and
- (e) the company must deliver after the five-week period (but no later than seven weeks) to the Registrar a return in specified form if there is no court application (**section 224**), or within 15 days after the court makes

the order confirming the special resolution or the proceedings are ended without determination by the court (**section 225**). The reduction of share capital takes effect when the return is registered by the Registrar.

### **Allowing all companies to purchase their own shares out of capital, subject to a solvency test (Sections 257 to 266)**

#### Position under Cap. 32

12. Under Cap. 32, the general rule is that a company can only buy back its shares using distributable profits or using the proceeds of a fresh issue of shares (sections 49A and 49B). This rule is derived from the capital maintenance doctrine. There is an exception for private companies which may fund a buy-back by payment out of capital based on a solvency test (sections 49I to 49N).

#### Position under the new CO

13. Under the new CO, all companies are allowed to fund buy-backs out of capital, subject to a solvency requirement.

#### Key provisions in the new CO

14. **Sections 258 to 266** retain most of the Cap. 32 requirements and procedures applicable to buy-backs by a private company out of capital, and extend them to all companies. The requirements and procedures are similar to the new court-free

procedure for reduction of capital as set out in paragraph 11 above<sup>1</sup>. The redemption or buy-back must be made no earlier than five weeks and no later than seven weeks after the special resolution is passed, unless otherwise ordered by the court.

15. **Section 257** prohibits a listed company from making a payment out of capital in respect of a buy-back of its own shares on a recognised stock market or on an approved stock market because it would be impractical for it to follow all the procedural requirements.

### Allowing all types of companies (listed or unlisted) to provide financial assistance, subject to satisfaction of the solvency test and certain specified procedures (Sections 283 to 289)

#### Position under Cap. 32

16. Section 47A of Cap. 32 prohibits a company and its subsidiaries from giving financial assistance for the purpose of acquiring shares in the company. The broad prohibition is subject to certain exceptions.

#### Position and key provisions in the new CO

17. The rules on financial assistance and the exemptions available under Cap. 32 are fairly complex and there has been general support for reform. **Section 274** retains the definition of financial assistance in Cap. 32. **Sections 277 to**

**282** largely retain the exceptions to the prohibition in section 47C and the special restrictions for listed companies in section 47D. The main change under the new CO is to allow all types of companies (listed or unlisted) to provide financial assistance, subject to satisfaction of the solvency test and one of the three procedures set out in **sections 283 to 289**.

18. The first procedure, set out in **section 283**, provides that a company may give financial assistance if the assistance, and all other financial assistance previously given and not repaid, is in aggregate less than 5% of the shareholders' funds. The giving of the assistance must be supported by a solvency statement and a resolution of the directors in favour of giving the assistance. The assistance must be given not more than 12 months after the solvency statement is made. Within 15 days after giving the assistance, the company must notify its members of the details of the assistance.

19. The second procedure, set out in **section 284**, provides that a company may give financial assistance if it is approved by written resolution of all members of the company. The giving of the assistance must be supported by a solvency statement and a resolution of the directors in favour of giving the assistance. The assistance must be given not more than 12 months after the solvency statement is made.

<sup>1</sup> There are some differences though, to align the registration requirements with those for buy-backs out of profits. For example, instead of requiring the company to deliver to the Registrar a return in specified form after the five-week period (paragraph 11(e) above), the company will instead be required, under section 270, to deliver a similar return, which is applicable to all types of redemption/buy-back of shares (i.e. not limiting to those financed out of capital), within 15 days after the redeemed or bought back shares are delivered to the company.

20. The third procedure, set out in **section 285**, provides that a company may give financial assistance if it is approved by an ordinary resolution. The giving of the assistance must be supported by a solvency statement and the board must resolve that giving the assistance is in the interests of the company. The company must send to each member at least 14 days before the resolution a notice which contains all information necessary for the members to understand the nature of the assistance and the implications of giving it for the company. The assistance may only be given not less than 28 days after the resolution is passed and not more than 12 months after the day on which the solvency statement is made. **Sections 286 to 288** provide that shareholders holding at least 5% of the total voting rights or members representing at least 5% of the total members of the company may, within the 28-day period, apply to the court to restrain the giving of the assistance<sup>2</sup>.

### Relaxing the rules on giving of financial assistance for the purposes of employee share schemes (Section 280)

#### Position under Cap. 32

21. Section 47C(4)(b) of Cap. 32 provides that the prohibition on financial assistance does not apply to employee share schemes, provided that the financial assistance is restricted to the provision of money for the purchase or subscription of fully paid shares.

#### Position and key provisions in the new CO

22. **Section 280** allows financial assistance for all types of employee share schemes if the assistance is given in good faith in the interest of the company for the purposes of an employee share scheme or the giving of the assistance is for the purposes of enabling or facilitating transactions to acquire the beneficial ownership of shares for the employees.

## TRANSITIONAL AND SAVING ARRANGEMENTS

23. The major changes described in these Highlights apply to activities carried out after the commencement date of the new CO. For activities started under Cap. 32 and in progress when the new CO commences, Cap. 32 provisions will continue to apply (**sections 42 to 47 of Schedule 11** to the new CO).

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<sup>2</sup> A threshold (10%) is present in section 47G of Cap. 32, mainly to minimise frivolous claims.

# Part 6

## Distribution of Profits and Assets

### INTRODUCTION

Part 6 (Distribution of Assets and Profits) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions that deal with distribution of profits and assets of a company to members.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 6 does not introduce fundamental changes to the distribution provisions in the Companies Ordinance (Cap. 32) (“Cap. 32”) as the rules under Cap. 32 have generally worked well and provided certainty. It mainly reorganises the provisions in Cap. 32 and proposes some minor technical amendments.

#### Position under Cap. 32

3. The specific provisions on distributions are contained in sections 79A to 79P of Part IIA of Cap. 32. While the usual form of distribution is dividend, under the Cap. 32 regime, “distribution” means every description of distribution of a

company’s assets to its members whether in cash or otherwise, except distribution by way of bonus shares, redemption or buy-back of shares, reduction of capital and distribution in a winding up. Distribution can only be made out of profits available for the purpose. A company’s profits available for distribution are its accumulated, realised profits (so far as previously not distributed or capitalised) less its accumulated, realised losses (so far as not previously written off in a reduction or reorganisation of capital)<sup>1</sup>.

4. There are further restrictions for listed companies<sup>2</sup>. The consequences of unlawful distribution are provided for<sup>3</sup>.

#### Position and key provisions in the new CO

(i) *Reorganising the provisions and modernising the language*

5. Part 6 mainly reorganises, with some modifications, the provisions under Cap. 32 in a more logical, user-friendly and readable way and modernises the language to facilitate easier understanding.

<sup>1</sup> Section 79B(2) of Cap. 32.

<sup>2</sup> Section 79C of Cap. 32: a listed company can only make a distribution if the amount of its net assets is not less than the aggregate of its called-up share capital and undistributable reserves, and to the extent that the distribution does not reduce the amount of those assets to less than that aggregate.

<sup>3</sup> Section 79M of Cap. 32: if the member to whom the distribution is made knows or has reasonable grounds to believe that it is made in contravention of the law he is liable to repay to the company.

6. Part 6 contains provisions relating to the distribution of profits and assets to members. It is divided into four Divisions. Each Division has a specific function. **Division 1** defines or otherwise explains the expressions used in Part 6. **Division 2** deals with the prohibitions and restrictions on distributions by a company to its members. **Division 3** contains provisions supplementary to Division 2, for example **section 302** provides that the amount of a distribution that may be made lawfully is to be determined by reference to certain financial items as stated in the financial statements specified in Division 4. **Division 4** specifies the financial statements for the purposes of **section 302**. The specified financial statements for distribution purpose are the annual financial statements, the interim financial statements and the initial financial statements. These are the same under Cap. 32.

*(II) Technical amendments*

7. There are technical amendments to change the terms used in Part 6 in accordance with the changes made in other Parts of the new CO. For example, the term “accounts” will be replaced by “financial statements” as in Part 9, and the expression “purchase of a company’s own shares” will be replaced by the term “buy-back” as in Part 5. References to “capital redemption reserve” and “share premium account” will be removed in parallel with the introduction of the no-par regime in Part 4.

## TRANSITIONAL AND SAVING ARRANGEMENTS

8. Part 6 applies to a proposed distribution where the referential financial statements cover a period that commences after the commencement of the new CO (**section 295**). If the financial statements are for a financial year or period beginning before the commencement of the new CO, then the financial statements should be prepared according to the Cap. 32 accounting provisions and the distributions proposed on the basis of such financial statements should be made according to Part IIA of Cap. 32.

# Part 7

## Debentures

### INTRODUCTION

Part 7 (Debentures) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions that deal with matters concerning debentures, for example, keeping of the register of debenture holders, rights to inspect and make copies of the register, trust deeds and other documents and convening meetings of debenture holders.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 7 contains initiatives that aim at modernising the law (subparagraph (a) below) and ensuring better regulation (subparagraphs (b) to (d)), namely –
- (a) Improving clarity by separating provisions applicable to debentures from those applicable to shares (paragraph 4).
  - (b) Aligning provisions for keeping of the register of debenture holders with similar provisions for register of members in Part 12 (paragraphs 5 to 7);
  - (c) Introducing new requirements for registration of allotment of debentures to align with similar requirements for shares introduced in Part 4 (paragraphs 8 to 9); and
  - (d) Allowing debenture holders to apply to the Court to order a meeting to be held to give directions to the trustee for the protection of debenture holders (paragraphs 10 to 11).
3. The details of the above major changes in Part 7 are set out in paragraphs 4 to 11 below.

#### Improving clarity by separating provisions applicable to debentures from those applicable to shares (Sections 311, 321 and 323 to 324)

4. Under the Companies Ordinance (Cap. 32) (“Cap. 32”), some of the provisions applicable to both shares and debentures are scattered in different parts. This arrangement is not user-friendly as those interested only in debentures would need to go through the various parts to identify provisions applicable to debentures. To improve clarity, all substantive requirements about debentures are now grouped under Part 7. For example, power to close the register of debenture holders (**section 311**), registration of transfer or refusal of registration (**section 321**), duties of companies with respect to issue of debentures or certificates for debenture stock on transfer (**section 323**) and the Court’s power to order such issue (**section 324**).

## Aligning provisions for keeping of the register of debenture holders with similar provisions for register of members in Part 12 (Sections 308 to 315)

### Position under Cap. 32

5. Cap. 32 sets out the requirements for keeping a register of debenture holders (section 74A) in a manner similar to those for a register of members in respect of shareholding in a company (section 95). However, there is a difference between the two, i.e. only the register of debenture holders is required to detail the occupation or give a description of the debenture holder. Also, under Cap. 32, there are provisions for keeping of a branch register for the register of members (sections 103 and 104) but there are no similar provisions for the register of debenture holders.

### Position and key provisions in the new CO

6. To ensure consistency and to clarify the law in the new CO, the provisions relating to the register of debenture holders are aligned with and mirror those relating to the register of members, including removing the requirement to disclose the debenture holder's occupation (**section 308**), and adding the provisions for keeping of branch registers in respect of debenture holders (**sections 312 to 315**).

7. **Section 308** provides for the keeping of a register of debenture holders. **Section 309** provides for the place where the register of debenture holders must be kept. **Section 310** provides for the right to inspect and request a copy of the register of debenture holders. **Sections 312 to 315** provide for the keeping of branch registers of debenture holders.

## Introducing new requirements for registration of allotment of debentures to align with similar requirements for shares in Part 4 (Sections 316 and 317)

### Position under Cap. 32

8. Cap. 32 requires a company to deliver a return of allotment of shares to the Registrar of Companies ("the Registrar") for registration, but there are no similar requirements in respect of an allotment of debentures. Section 70(1) of Cap. 32 obliges a company to complete and deliver the debentures or certificates for debenture stock within two months after their allotment. However, Cap. 32 does not require an entry to be made in the register of debenture holders after an allotment of debentures.

### Position and key provisions in the new CO

9. **Section 316** provides that within one month after the allotment of debentures (including debenture stock), a company must deliver to the Registrar a return of the allotment in the specified form for registration. **Section 317** provides that as soon as practicable, and in any event within two months after an allotment of debentures, a company must register the allotment in the register of debenture holders. These are new provisions to help protect investors in debentures and align the position of debenture holders with that of members. **Sections 316 and 317** largely mirror similar requirements for shares under sections 142 and 143 of Part 4.

### **Allowing debenture holders to apply to the Court to order a meeting to be held to give directions to the trustee for the protection of debenture holders (Section 331)**

#### Position under Cap. 32

10. Section 75A of Cap. 32 provides that where the debentures or the trust deed or other document securing the debentures or stock provide for the holding of meetings of holders of debentures or stock, then subject to such provisions, such meetings shall be convened subject to the relevant provisions in Cap. 32<sup>1</sup>. In practice, however, section 75A is unlikely to be invoked, because if the debenture documents do not provide for meetings, the provisions in Cap. 32

would be of no assistance. Where the debenture documents do so provide, these documents (if professionally prepared) are likely to have their own provisions which will negate the application of the provisions in Cap. 32.

#### Position and key provisions in the new CO

11. **Section 331** replaces section 75A of Cap. 32 to provide that the Court may order a meeting of debenture holders. The section provides for the right for debenture holders holding 10% of the value of the debentures in total to apply to the Court to order a meeting for giving directions to the trustee. This is subject to any provisions in the debentures, or the trust deeds or other documents securing the issue of the debentures that exclude such right or require a higher percentage of debenture-holdings. This section applies to debentures forming part of a series issued by the company and ranking *pari passu* (i.e. of the same rank) with other debentures of that series, and debenture stock.

## **TRANSITIONAL AND SAVING ARRANGEMENTS**

12. The major changes described in these Highlights apply to activities carried out after the commencement date of the new CO. For activities started under Cap. 32 and in progress when the new CO commences, Cap. 32 provisions will continue to apply (**sections 50 to 61 of Schedule 11** to the new CO).

<sup>1</sup> Sections 113, 114B, 114C, 114D(2) and 114E of Cap. 32.

# Part 8

## Registration of Charges

### INTRODUCTION

Part 8 (Registration of Charges) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions that deal with registration of charges by both Hong Kong and registered non-Hong Kong companies. It sets out the types of charges that require registration, registration procedures, consequences of non-compliance, and other related matters such as keeping and inspection of copies of charge instruments and registers of charges.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 8 basically retains the registration regime under Part III of the Companies Ordinance (Cap. 32)<sup>1</sup>(“Cap. 32”), with the following initiatives that aim at ensuring better regulation by enhancing disclosure and improving the registration system –

- (a) Updating the list of registrable charges (paragraphs 5 to 6);
- (b) Replacing the automatic acceleration of the repayment obligation with a choice given to the lender as to whether the secured amount should be immediately payable where a charge is rendered void for non-compliance with the registration requirements (paragraphs 7 to 8);

- (c) Requiring a certified copy of the charge instrument to be registered and made available for public inspection (paragraphs 9 to 10);
- (d) Shortening the period for delivery to the Registrar of Companies (“the Registrar”) of a certified copy of the charge instrument and the prescribed particulars from five weeks to one month (paragraphs 11 to 12);
- (e) Requiring a certified copy of the written evidence of debt satisfaction or release of a charge to be registered and made available for public inspection (paragraphs 13 to 15);
- (f) Clarifying the effect of a Court order to extend the time for registration as regards criminal liability already incurred (paragraphs 16 to 17); and
- (g) Empowering the Court to rectify the particulars in the registered charge instrument and evidence of discharge (paragraphs 18 to 19).

3. To modernise and clarify the law, Part 8 sets out specific provisions for registered non-Hong Kong companies to deal with charge-related issues. This is an improvement over section 91 of Cap. 32 which is a single lengthy and complicated section that sets out the applicability of relevant charge-related provisions under Part III of Cap. 32 to registered non-Hong Kong companies.

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<sup>1</sup> Sections 80 to 91 of Cap. 32.

4. The details of the above changes in Part 8 are set out in paragraphs 5 to 19 below.

### Updating the list of registrable charges (Section 334)

#### Position under Cap. 32

5. Under Cap. 32, the categories of charges listed under section 80(2) are required to be registered. There are some difficulties with the provision as follows –

(a) Charge on an aircraft or any share in an aircraft

There are uncertainties as to whether particular mortgages over aircrafts are registrable as bills of sale under section 80(2)(c) of Cap. 32<sup>2</sup>.

(b) Instalments due, but not paid, on the issue price of shares

It is unclear whether a charge on calls made but not paid, registrable under section 80(2)(g) of Cap. 32, should also cover a charge on instalments due, but not paid, on the issue price of the shares as these instalments are not calls in the strict sense.

(c) Charges for the purpose of securing any issue of debentures

Charges for the purpose of securing any issue of debentures are registrable under section 80(2)(a) of Cap. 32. Typically, issues of debentures are supported by a floating charge or a fixed charge. Hence, this head is redundant and overlaps with other heads of registrable charges under section 80(2) of Cap. 32.

(d) Lien on subfreights

There are divergent judicial views as to whether a shipowner's lien on subfreights is registrable as a charge on book debts or a floating charge or whether it is a charge at all<sup>3</sup>.

(e) Cash deposits

A charge over cash deposits could arguably be registrable under section 80(2)(e) of Cap. 32 as a charge over book debts.

<sup>2</sup> Some such mortgages could fall within one or more of the exclusions from the definition of "bill of sale" and are therefore not registrable under section 80(2)(c).

<sup>3</sup> There is judicial authority to support the principle that a shipowner's contractual lien on subfreights is a charge on book debts (*Re Welsh Irish Ferries Ltd* [1986] Ch 471) or a floating charge (*The Annangel Glory* [1988] 1 Lloyd's Rep 45) which is registrable under section 80(2)(e) or section 80(2)(f) of Cap. 32. On the other hand, it has also been said that a lien on subfreights is not a charge at all but merely a personal right to intercept freight before it is paid to the owner (Lord Millett in *Re Brumark Ltd: Agnew v Commissioner of Inland Revenue* [2001] 2 AC 710, at paragraph 41).

## Position and key provisions in the new CO

6. To remove the ambiguities and dispense with redundant items, the following changes have been made in the new CO –

(a) Charge on an aircraft or any share in an aircraft

**Section 334(1)(h)** expressly provides that a charge on an aircraft or any share in an aircraft is registrable.

(b) Instalments due, but not paid, on the issue price of shares

**Section 334(1)(f)** expressly makes a charge on instalments due, but not paid, on the issue price of shares registrable.

(c) Charges for the purpose of securing any issue of debentures

Under the new CO, this head of registrable charge is removed.

(d) Lien on subfreights

As charterparties are usually negotiated by shipbrokers (not lawyers) and are of relatively short duration, requiring a lien to be registered is inconvenient from a commercial perspective. **Section 334(4)** clarifies that a shipowner's lien on subfreights shall not be regarded as a charge on book debts or as a floating charge and is therefore not registrable.

(e) Cash deposits

**Section 334(3)(b)** stipulates that if a company maintains a deposit of money with another person, a charge on the company's right to repayment is not a charge on book debts of the company. It is based on the fact that such charges are normally taken over credit balances with financial institutions in the form of charge-backs with the depository banks. Third party creditors would not be misled by the absence of registration since bank accounts are usually operated confidentially and it is reasonable to expect the depository bank to have a superior claim to the credit balance. Moreover, as a charge-back, such charges would have the effect of a set-off which of itself does not require registration.

## **Replacing the automatic acceleration of repayment obligation (Section 337(6))**

### Position under Cap. 32

7. Section 80(1) of Cap. 32 states that where a charge becomes void for not being registered with the Registrar within the specified time limit, the money secured by it would automatically become immediately payable. This statutory acceleration of repayment may create problems for banks, as the acceleration arises automatically.

### Position and key provision in the new CO

8. **Section 337(6)** replaces the “automatic” acceleration provision with a “discretionary” acceleration provision, giving a choice to the lender as to whether the secured amount is to become immediately payable.

### **Requiring a certified copy of the charge instrument to be registered and made available for public inspection (Sections 335, 336 and 338 to 340)**

#### Position under Cap. 32

9. Cap. 32 requires a charge instrument (if any) together with the prescribed particulars of the charge in a specified form<sup>4</sup> to be delivered to the Registrar for registration. However, only the prescribed particulars are required to be registered and made available for public inspection<sup>5</sup> by the Registrar. The charge instrument itself, which is delivered for the purpose of enabling the Registrar to verify the contents of the prescribed particulars, does not appear on the Register for public search.

#### Position and key provisions in the new CO

10. Under the new CO, more detailed information as to the charges would be made available to those who search the Register. **Sections 335(1) and (2), 336(1) and (2), 338(2), 339(3) and 340(2) and (3)** provide that both a

certified copy of the charge instrument (if any) and the prescribed particulars of the charge are registrable and available for public inspection<sup>6</sup>. The availability of a certified copy of the charge instrument will give rise to constructive notice of all the terms in the charge instrument, including negative pledge clauses, to those who may reasonably be expected to search the Register, such as banks, financiers and relevant professionals.

### **Shortening the period for delivery to the Registrar of a certified copy of the charge instrument and the prescribed particulars from five weeks to one month (Sections 335, 336 and 338 to 340)**

#### Position under Cap. 32

11. Cap. 32 requires delivery of a charge instrument (if any) and its prescribed particulars to the Registrar for registration within five weeks. It is therefore possible that the prescribed particulars will only be visible on the public register at the end of the five-week period.

#### Position and key provisions in the new CO

12. To minimise the period during which the particulars of a charge could be invisible to outside parties, **sections 335(5), 336(6), 338(3), 339(4) and 340(5)** shorten the delivery period to one month.

<sup>4</sup>The prescribed particulars are contained in Form M1.

<sup>5</sup>Only those prescribed particulars as set out in section 83(1) of Cap. 32 are required to be entered in the public register kept by the Registrar and made available for public inspection.

<sup>6</sup>The particulars of a charge required for registration under the new CO are to be contained in a specified form of “Statement of Particulars of Charge”. The statement will contain fewer details than as required under Cap. 32, since a certified copy of the charge instrument itself will be registered. Where a registrable charge created by the company is not registered in time, the charge will be void as against the liquidator and creditors (section 337(4)), as is the case under section 80 of Cap. 32.

## Requiring a certified copy of the written evidence of debt satisfaction or release of a charge to be registered and made available for public inspection (Section 345)

### Position under Cap. 32

13. Under Cap. 32, if a debt secured by a registered charge has been satisfied, an application in the specified form (Form M2) may be made to the Registrar for entering on the Register a memorandum of satisfaction. Likewise, where a property or undertaking has been released from a registered charge or has ceased to form part of the company's property or undertaking, the Registrar will, upon application, enter on the Register a memorandum of release or cessation. Such applications have to be accompanied by evidence of discharge, usually in the form of a deed of release or discharge.

14. Only the memoranda of satisfaction or release are open for public inspection, but the evidence of discharge is neither registered nor available for public inspection.

### Position and key provision in the new CO

15. **Section 345(4)** provides that a certified copy of the evidence of discharge also has to be registered and made available for public inspection.

## Clarifying the effect of an order made by the Court to extend the time for registration in respect of criminal liability already incurred (Section 346)

### Position under Cap. 32

16. Under section 86(2) of Cap. 32, if the Court grants relief to extend the time for registration of a charge, the Court can direct that the relief will not relieve the company or its officers from the criminal liability incurred under section 81 of Cap. 32 for their failure to register. It is, however, unclear in section 86(2) whether in the absence of any court direction, the relief granted would automatically relieve the company and its officers from the criminal liability.

### Position and key provisions in the new CO

17. To remove the abovementioned uncertainty, **section 346(4) and (5)** states that such criminal liability incurred<sup>7</sup> would be extinguished provided that registration is effected within the extended time.

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<sup>7</sup> For offences under sections 337(2), 338(5), 339(6), 340(7), 341(7) or 343(1) of the new CO, or sections 81, 82 or 91(6) of Cap. 32.

## Empowering the Court to rectify the particulars in the registered charge instrument and evidence of discharge (Section 347)

### Position under Cap. 32

18. Section 86(1) of Cap. 32 allows the Court to rectify an omission or misstatement of the particulars of a charge or in the memoranda of satisfaction or release that have been registered.

### Position and key provisions in the new CO

19. As the new CO will make a certified copy of the charge instrument (if any) and evidence of discharge registrable and open to public inspection, **sections 347(1)(a)(i) and (iii)** empower the Court to also rectify an omission or misstatement of the particulars in the registered charge instrument and evidence of discharge. **Section 347(4)** specifies that such powers of rectification will be subject to the common law rules and equitable principles applied to registration of documents, i.e. to the extent that the instrument has failed to accurately record the intention of the parties<sup>8</sup>.

## TRANSITIONAL AND SAVING ARRANGEMENTS

20. In respect of registration of charges created before the commencement of the new CO, the general transitional provisions apply and the provisions of Cap. 32 are relevant. However to ensure a smooth transition in the registration process, it is considered necessary to have a cut off date after which all documents delivered to the Registrar comply with the requirements of the new CO. It is therefore provided that for a charge created before the commencement of the new CO but presented for registration after the expiry of 8 weeks from the commencement of Division 2 of Part 8 of the new CO, the new specified form together with a certified copy of the instrument creating the charge (i.e. the documents required to be registered under the new CO) should be delivered for registration. Detailed saving and transitional provisions are set out in **sections 62 to 75 of Schedule 11** to the new CO.

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<sup>8</sup>The remedy of rectification is available not for the purpose of altering the terms of the agreement, but for that of correcting a document which does not reflect accurately the true agreement of the parties: *Agip SpA v Navigazione Alta Italia SpA* [1984] Lloyd's Rep 353 at 359.

# Part 9

## Accounts and Audit

### INTRODUCTION

Part 9 (Accounts and Audit) of the new Companies Ordinance (Cap. 622) (“new CO”) contains the accounting and auditing requirements, namely provisions in relation to the keeping of accounting records, the preparation and circulation of annual financial statements, directors’ and auditors’ reports and the appointment and rights of auditors. New provisions are introduced to facilitate small and medium-sized enterprises (“SMEs”) to take advantage of simplified accounting and reporting, to require public and other large private companies to include an analytical business review in directors’ reports, and to enhance auditors’ right to information.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. This Part contains initiatives that aim at business facilitation, namely –

- (a) Relaxing the criteria for companies to prepare simplified financial and directors’ reports i.e. the “reporting exemption” (paragraphs 5 to 10); and
- (b) Making the summary financial report provisions more user-friendly and extending their application to all companies (paragraphs 32 to 36).

3. There are also initiatives to enhance corporate governance, namely –

- (a) Requiring public companies and other companies that do not qualify for simplified reporting to prepare a “business review” within the directors’ report, whilst allowing private companies to opt out by special resolution (paragraphs 17 to 21);
- (b) Empowering auditors to obtain information from a wider range of persons for the performance of their duties (paragraphs 22 to 26); and
- (c) Improving transparency with regard to circumstances of cessation of office of an auditor (paragraphs 27 to 31).

4. This Part also modernises and improves the law by –

- (a) Clarifying the financial year of a company, requiring companies to hold annual general meetings (“AGMs”) and requiring public companies or companies limited by guarantee to file annual returns in respect of every financial year of the company (paragraphs 11 to 16); and
- (b) Streamlining disclosure requirements that overlap with the accounting standards (paragraphs 37 to 41).

## Relaxing the criteria for companies to prepare simplified financial and directors' reports i.e. the "reporting exemption" (Sections 359 to 366 and Schedule 3 to the new CO)

### Position under the Companies Ordinance (Cap. 32) ("Cap. 32")

5. Section 141D of Cap. 32 provides that a private company (other than a company which has a subsidiary or is a subsidiary of another company and certain companies specifically excluded, such as insurance and stock-broking companies) may, with the written agreement of all its shareholders, prepare simplified accounts and simplified directors' reports in respect of one financial year at a time. According to the Small and Medium-sized Entity-Financial Reporting Framework ("SME-FRF") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), a Hong Kong company qualifies for reporting based on the SME-Financial Reporting Standard ("SME-FRS") if it satisfies the requirement under section 141D. The SME-FRF is not applicable to groups of companies or guarantee companies at all under Cap. 32.

### Position under the new CO

6. The original draft Companies Bill ("CB") allowed private companies and groups of private companies meeting the size criteria that qualify for financial reporting under the current SME-FRF (i.e. two out of three of the following eligibility limits : HK\$50 million assets, HK\$50 million revenue and 50 employees) to be automatically qualified for the preparation of simplified financial and directors' reports. The Bills Committee of

the Legislative Council noted the support for relaxation of the size criteria and the suggestion to extend the use of SME-FRS to private companies / groups of any size when members holding certain voting rights in the company approve and no member objects.

7. The Bills Committee supported allowing private companies / groups meeting a higher size criteria to prepare simplified reports if members of the company so resolve.

8. The criteria for simplified reporting are therefore relaxed by doubling the eligibility limits for automatic qualification, introducing a higher size criteria for private companies / groups that opt for simplified reporting and retaining the exception in section 141D of Cap. 32.

### Key provisions in the new CO

9. **Sections 359 to 366 and Schedule 3** set out the qualifying conditions for companies to prepare simplified financial and directors' reports along the following lines –

- (a) A "small private company" or a private company that is the holding company of a "group of small private companies" that satisfies any two of the following conditions is automatically qualified for simplified reporting –
- (i) total (or aggregate total) annual revenue of not more than HK\$100 million;
  - (ii) total (or aggregate total) assets of not more than HK\$100 million;
  - (iii) no more than 100 employees.

(for a small private company : sections 359(1)(a)(i), 361, Schedule 3 section 1(1), (2));

for a group of small private companies : sections 359(2)(a),(b) and (c)(i), 364, Schedule 3 section 1(7), (8) and (9))

- (b) An “eligible private company” or an eligible private company that is the holding company of a “group of eligible private companies” that satisfies any two of the following conditions and has the approval of members holding at least 75% of the voting rights with no other members objecting, is qualified for simplified reporting –

- (i) total (or aggregate total) annual revenue of not more than HK\$200 million;
- (ii) total (or aggregate total) assets of not more than HK\$200 million;
- (iii) no more than 100 employees.

(for an eligible private company : sections 359(1)(c), 360(1), 362, Schedule 3 section 1(3) and (4);

for a group of eligible private companies: sections 359(2)(a),(b) and (c)(ii), 360(2), 365, Schedule 3 section 1(10), (11) and (12))

- (c) A “small guarantee company” or a guarantee company that is the holding company of a “group of small guarantee companies” is automatically qualified for simplified reporting if its total annual revenue or aggregate total annual revenue (as the case may be) does not exceed HK\$25 million.

(for a small guarantee company : sections 359(1)(a)(i), 363, Schedule 3 section 1(5) and (6);

for a group of small guarantee companies: sections 359(3), 366, Schedule 3 section 1(13) and (14))

- (d) The option under section 141D of Cap. 32 available to a private company not having any subsidiary and not being a subsidiary of another company to adopt simplified reporting with unanimous members’ written agreement is retained in section 359(1)(b).

10. Companies which are qualified for simplified reporting are referred to in the new CO as companies “falling within the reporting exemption”. The reporting exemptions are in respect of the specific requirements relating to the preparation of financial statements and directors’ reports. The exemptions are set out in the following sections –

- **Section 380(3)** (no requirement to disclose auditor’s remuneration in financial statements).
- **Section 380(7)** (no requirement for financial statements to give a “true and fair view”).
- **Section 381(2)** (subsidiary undertakings may be excluded from consolidated financial statements in accordance with applicable accounting standards).
- **Section 388(3)(a)** (no requirement to include business review in directors’ report).
- **Section 406(1)(b)** (no requirement for auditor to express a “true and fair view” opinion on the financial statements).
- **Sections 3(3A), 4(3), 8(3) and 10(7) of Companies (Directors’ Report) Regulation (Cap. 622D)** (no requirement to disclose in the directors’ report the following : directors’ interests in arrangements to enable directors to acquire benefits by the acquisition of shares or debentures; donations; directors’ reasons for resignation or refusal to stand for re-election and material interests of directors in transactions, arrangements or contracts of significance entered into by a specified undertaking of the company).

- **Section 23 of Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap. 622G)** (no requirement to disclose in the notes to financial statements the material interests of directors in transactions, arrangements or contracts of significance entered into by the company).

Under **section 380(4)(b)**, the financial statements of a company must be prepared in compliance with the applicable accounting standards. The intention is that the accounting standards that will be applicable to a company falling within the reporting exemption is the SME-FRS and FRF issued or specified by the HKICPA which is the body prescribed in the Companies (Accounting Standards (Prescribed Body)) Regulation (Cap. 622C) for issuing or specifying the applicable accounting standards under **section 380(8)(a)**. The accounting standards applicable to companies that prepare simplified financial reports are less onerous than the Hong Kong Financial Reporting Standards (“HKFRS”) applicable to listed, public or other companies not qualified for simplified reporting. Audit of the financial statements is still required for all companies, except dormant companies (**section 447**), under the new CO.

**Clarifying the financial year of a company, requiring companies to hold annual general meetings (“AGMs”) and requiring public companies or companies limited by guarantee to file annual returns in respect of every financial year of the company (Sections 367 to 371, 610, 662(3), (4))**

#### Position under Cap. 32

11. Cap. 32 does not provide for a company’s accounting reference period. Section 122 of Cap. 32 requires accounts to be made out every year and to be laid before the company at its AGM, and those accounts must be made up to a date falling not more than a specified number of months before the date of the AGM. The

financial year is defined in section 2(1) of Cap. 32 as the period in respect of which the accounts so laid are made up. Section 111 of Cap. 32 requires every company to hold an AGM in each year and not more than 15 months is to elapse between the date of one AGM and the next but there are no rules on shorter accounting periods. In addition, there is no provision to regulate the first accounting period, except that the first AGM has to be held within 18 months of incorporation.

12. Section 109(1) of Cap. 32 provides that, except where the company is a private company having a share capital, the annual return is required to be filed within 42 days after the AGM for the year. Section 109(3) of Cap. 32 further provides that, except where the company is a private company, the annual return shall include certified copies of the company’s balance sheet and reports laid before the company in general meeting to which the return relates.

#### Position under the new CO

13. The new CO provides for the determination of the financial year of a company which is the same as the accounting reference period. It also provides for alteration of the accounting reference period.

14. Unless exempted under sections 611, 612 or 613, companies are required to hold an AGM within 6 months (for public companies) or 9 months (for private companies not being subsidiaries of public companies at any time during the financial year or companies limited by guarantee) after the end of the accounting reference period. With regard to the annual return of a public company or company limited by guarantee, the requirement to file the annual return within 42 days of the AGM under section 109(1) of Cap. 32 is changed as an AGM may be dispensed with under Part 12 (section 612(2)) of the new CO. Instead, the annual return is to be filed within 42 days after the company’s return date i.e. 6 months (for public companies) or

9 months (for companies limited by guarantee) after the end of the company's accounting reference period. The annual return is no longer required to be filed in each calendar year. There is no change to the requirement to file annual returns of private companies under section 109(1A) of Cap. 32 (section 662(1), (2) of new CO), which requires the annual return of a private company to be completed within 42 days after the anniversary of the date of its incorporation and filed forthwith.

#### Key provisions in the new CO

15. **Section 367** provides for the beginning and end of a company's first financial year after the new CO comes into operation, and that of subsequent financial years, by reference to a company's first accounting reference period. The accounting reference period is the period by reference to which the company's financial statements are to be prepared. Every subsequent accounting reference period is a period of 12 months beginning immediately after the end of the previous accounting reference period and ending on its accounting reference date, unless it is shortened or extended by alteration of the accounting reference date (**section 368(3)**). The accounting reference date is defined in **section 370**. It can be altered by a directors' resolution pursuant to **section 371**. In the case of alteration of an accounting reference date of a public company or a company limited by guarantee, notice of the new accounting reference date must be delivered to the Registrar of Companies ("the Registrar") for registration within 15 days after the date of the directors' resolution (**section 371(2)**).

16. **Sections 610 and 662(3) and (4)** respectively set out the requirements for companies to hold AGMs, and for public companies or companies limited by guarantee to file annual returns, in respect of every financial year of a company.

#### **Requiring public companies and other companies that do not qualify for simplified reporting to prepare a "business review" within the directors' report, whilst allowing private companies to opt out by special resolution (Section 388 and Schedule 5 to the new CO)**

##### Position under Cap. 32

17. The directors' report is basically a report of the company's information that people may wish to know about but is not included in the accounts. Section 129D of Cap. 32 sets out the detailed information required. The report must be approved by the board of directors. A copy of the report must be sent to every member and debenture holder of the company together with a copy of the accounts and auditors' report.

##### Position under the new CO

18. All companies (except those qualified for simplified reporting) are required to prepare, as part of the directors' report, a business review which is more analytical and forward-looking than the information required under Cap. 32. Private companies not qualified for simplified reporting may opt out of the requirement to prepare a business review if so approved by a special resolution.

19. The business review will provide additional information for members and help assess how the directors have performed their duties. In particular, the requirement to include information relating to environmental and employee matters that have a significant impact on the company is in line with international trends to promote corporate social responsibility.

### Key provisions in the new CO

20. **Section 388 and Schedule 5** provide for the directors' duty to prepare a directors' report and the detailed requirements of a business review. The business review consists of a fair review of the company's business; a description of the principal risks and uncertainties facing the company; particulars of important events affecting the company that have occurred since the end of the financial year; and an indication of likely future development in the company's business. To the extent necessary for an understanding of the development, performance or position of the company's business, a business review must include an analysis using financial key performance indicators; a discussion on the company's environmental policies and performance and the company's compliance with the relevant laws and regulations that have a significant impact on the company; and an account of the company's key relationships with its employees, customers and suppliers and others that have a significant impact on the company on which the company's success depends. The exemptions from preparation of a business review are set out in **section 388(3)** which include wholly-owned subsidiary companies. The holding company of such companies will prepare the business review unless it is exempted on other grounds.

21. To encourage meaningful reporting and to limit directors' civil liability for statements or omissions in the directors' report, **section 448** provides a "safe harbour" so that directors are liable to the company only in respect of loss suffered by it as a result of any untrue or misleading statements or the omission of anything required to be included. The directors are only liable if they knew, or was reckless as to whether, a statement was untrue or misleading, or an omission was dishonest concealment of a material fact.

### **Empowering auditors to obtain information from a wider range of persons for the performance of their duties (Section 412)**

#### Position under Cap. 32

22. To ensure that an auditor will be in a position to perform his oversight functions in an effective manner, it is important for him to have access to the relevant information regarding the state of affairs of the company. The auditors' rights to information as set out in sections 133(1) and 141(5) of Cap. 32 are considered to be too restrictive.

#### Position under the new CO

23. The provisions under the new CO empower auditors to require a wider range of persons, including persons holding or accountable for accounting records, to provide them with information and explanation as they reasonably require for the performance of their duties.

#### Key provisions in the new CO

24. Under **section 412**, the persons who will be required to provide information or explanation to auditors are –

- an officer of the company;
- a Hong Kong subsidiary of the company;
- an officer or auditor of such a subsidiary;
- a person holding or accountable for any of the accounting records of the company or such a subsidiary; and
- any of the above persons or subsidiary at the time to which the information or explanation relates.

25. The auditor of a holding company may also require the company to obtain information or explanation from its subsidiary undertaking that is not a Hong Kong company, the officers and auditor of such a subsidiary undertaking, persons holding or accountable for any of the accounting records of such a subsidiary undertaking and any of these persons at the time to which the information or explanation relates.

26. Failure to comply with the requirement to provide information or explanation to the auditors will be subject to criminal sanctions under **section 413**.

### Improving transparency with regard to circumstances of cessation of office of an auditor (Sections 421 to 427)

#### Position under Cap. 32

27. Under section 140A(2) of Cap. 32, a resigning auditor is required to make a statement in the notice of resignation as to whether there are any circumstances connected with his resignation that he considers should be brought to the notice of the members or creditors of the company, and if so, a statement of any such circumstances ("statement of circumstances"). Auditors who ceased office owing to other reasons, e.g. removal or not being re-appointed after retirement, are not required to make such a statement.

#### Position under the new CO

28. To improve transparency and corporate governance, an outgoing auditors' duty to make a statement of circumstances is extended to an auditor who has been removed and a retiring auditor who has not been reappointed.

#### Key provisions in the new CO

29. **Sections 424 and 425(1)** provide for the auditor's duty to make a statement of circumstances connected with the resignation or the termination of appointment due to removal from office or retirement without reappointment. Within 14 days of receipt of the statement, the company must send a copy of the statement to the members or apply to court for an order directing copies of the statement not to be sent to the members (**section 426(1)**). **Section 427** provides that the court may order the statement not to be sent if it is satisfied that the outgoing auditor has abused the use of the statement or is using it to secure needless publicity for defamatory matter.

30. If the outgoing auditor has not received notice of an application to the court within 21 days of the company receiving the statement, the auditor must send a copy of the statement to the Registrar for registration within a further 7 days (**section 426(5)**). The outgoing auditor is also required to do so if he/she receives notice that the court does not grant the application not to send the statement to the members (**section 427(5)**).

31. **Section 410** is new and gives an auditor qualified privilege for statements made in the course of performing duties as auditor of the company. In particular, in the absence of malice, an auditor is not liable for defamation in respect of any statement given by the auditor connected with his or her cessation of office.

### Making the summary financial report provisions more user-friendly and extending application to all companies (Sections 437 to 446)

#### Position under Cap. 32

32. Under sections 141CA to 141CH of Cap. 32, a listed company may send a summary financial report to the members and debenture

holders in place of the accounts, directors' and auditors' reports required to be sent under section 129G of Cap. 32 provided that it has obtained the agreement of those persons. Very few listed companies have offered the alternative of providing summary financial reports to members under those sections partly due to cost considerations and partly because the company has to obtain the members' consent by complying with complex rules for sending notification to and receiving a response from the members.

33. There is also no exemption for listed companies incorporated in Hong Kong not to send out accounts and reports or summary financial reports. However, in some other jurisdictions, those documents need not be sent if the members so request.

#### Position under the new CO

34. The summary financial report provisions in the new CO are applicable to all companies (other than those qualified for simplified reporting) rather than being only applicable to listed companies as in Cap. 32. Unlike Cap. 32, members' consent is not required before a company can send a copy of a summary financial report to its members.

#### Key provisions in the new CO

35. **Section 441** provides companies (other than those falling within the reporting exemption) with a choice of sending a copy of the summary financial report instead of a copy of the full "reporting documents" (defined in **section 357(2)** to mean the financial statements, directors' report and auditors' reports) to their members. This will avoid the complex rules which require a company to ask its members in advance before it can send them a copy of the summary financial report. Members receiving summary financial reports may request a copy of the full reporting documents from the company (**section 445**).

36. Under **section 442**, the company may at any time ascertain the wishes of its members or potential members through a "notification" which allows them to elect to receive a copy of the reporting documents, or a copy of the summary financial report in hard copy form, or electronic form, or by making it available on a website; or not to receive any copies of the documents.

### **Streamlining disclosure requirements that overlap with the accounting standards (Schedule 4 to the new CO)**

#### Position under Cap. 32

37. There are certain inconsistencies between the accounting requirements under Cap. 32 and the accounting standards, particularly in respect of the simplified accounting requirements in section 141D of Cap. 32. Compared with the requirements under section 141D, the SME-FRS requires a more complete set of accounts and more disclosures. For example, pursuant to section 141D(1)(e), the auditors' report of a company which applies section 141D covers only the balance sheet but not the profit and loss account.

38. Cap. 32 also provides for certain disclosure requirements as to the contents of the accounts in the Eleventh Schedule (for companies that apply section 141D) and the Tenth Schedule (for other companies) which overlap with the disclosure requirements in the SME-FRS and HKFRS respectively. As accounting standards are constantly evolving, it is very difficult to keep the statutory requirements up-to-date. This can give rise to potential conflict between the two.

## Position under the new CO

39. To avoid any potential conflict between the Tenth Schedule and HKFRS and between the Eleventh Schedule and SME-FRS, both Schedules are repealed, with only a small number of public interest disclosure requirements not covered by the HKFRS or SME-FRS being retained in **Schedule 4**. The HKFRS and SME-FRS are given indirect statutory recognition, as financial statements are required to comply with the applicable accounting standards issued or specified by the HKICPA under the Companies (Accounting Standards (Prescribed Body)) Regulation (Cap. 622C) (section 380(4)(b) & (8)(a)).

## Key provisions in the new CO

40. **Schedule 4** includes the following public interest disclosures –

- (a) the aggregate amount of any outstanding loans to directors and employees to acquire shares in the company authorised under sections 280 and 281 of the new CO (required under paragraphs 9(1)(c) and 5 respectively of the Tenth and Eleventh Schedules to Cap. 32);
- (b) information regarding a company's ultimate parent undertaking (required under section 129A of Cap. 32); and
- (c) auditors' remuneration (applicable to companies not qualified for simplified reporting, required under paragraph 15 of the Tenth Schedule to Cap. 32).

41. **Section 4 of Part 1 of Schedule 4** further requires a statement to be made in the financial statements as to whether they have been prepared in accordance with the applicable accounting standards, and to give the particulars of, and the reasons for, any material departure from those standards.

## TRANSITIONAL AND SAVING ARRANGEMENTS

42. Transitional and saving arrangements are set out in **sections 76 to 87, 107(2) to (5) and 121 of Schedule 11** to the new CO and are basically as follows –

- **Financial year and related matters**

Sections 127 and 141D of, and the Eleventh Schedule to, Cap. 32 continue to apply in relation to a financial year beginning before the commencement of Division 3 of Part 9 and ending on or after that commencement.

- **Accounts and directors' report**

(1) Sections 122, 123, 124, 125, 126, 128, 129, 129A, 129B, 129C, 129D, 129G, 141C, 161, 161A, 161B, 161BA and 161BB of, and the Tenth Schedule to, Cap. 32 continue to apply in relation to accounts for a financial year beginning before the commencement of Subdivision 3 of Division 4 of Part 9 and ending on or after that commencement.

(2) Despite subparagraph (1) above, section 122(1B) of Cap. 32 continues to apply in relation to accounts for a financial year beginning before the commencement of Subdivision 3 of Division 4 of Part 9 and ending on or after that commencement as if paragraph (b) of subsection (1B) were omitted.

(3) If the court makes an order under section 122(1B) of Cap. 32 under subparagraph (2) above, the accounts to be laid at the meeting concerned must be made up to the company's primary accounting reference date under section 369(1)(b) of the new CO.

(4) Sections 129D, 129E, 129F and 141C of Cap. 32 continue to apply in relation to a directors' report for a financial year beginning before the commencement of Subdivision 4 of Division 4 of Part 9 and ending on or after that commencement.

- **Auditors' report**

(1) Sections 141(1), (2), (3), (4), (5) and (6), 161(8) and 161B(12) of Cap. 32 continue to apply in relation to a financial year beginning before the commencement of Subdivision 3 of Division 5 of Part 9 and ending on or after that commencement.

(2) Section 141(7) and (8) of Cap. 32 continues to apply in relation to a general meeting of which notice is given before the commencement of Subdivision 4 of Division 5 of Part 9.

- **Removal and resignation of auditor**

(1) Sections 131(6), (7) and (10) and 132 of Cap. 32 continue to apply in relation to a removal of a person appointed as auditor for a financial year beginning before the commencement of Subdivision 6 of Division 5 of Part 9 and ending on or after that commencement.

(2) Sections 140A and 140B of Cap. 32 continue to apply in relation to a resignation of a person appointed as auditor for a financial year beginning before the commencement of Subdivision 6 of Division 5 of Part 9 and ending on or after that commencement.

- **Summary financial report**

Sections 141CA, 141CB, 141CC, 141CD, 141CE and 141CF of Cap. 32 and the Companies (Summary Financial Reports of Listed Companies) Regulation (Cap. 32 sub.

leg. M) continue to apply in relation to a summary financial report for a financial year beginning before the commencement of Division 7 of Part 9 and ending on or after that commencement.

- **Voluntary revision of accounts etc.**

Section 141E of Cap. 32 and the Companies (Revision of Accounts and Reports) Regulation (Cap. 32 sub. leg. N) continue to apply in relation to accounts for a financial year beginning before the commencement of section 449 and ending on or after that commencement.

- **Annual general meetings**

If a company is required to lay at its AGM an account or a balance sheet in accordance with section 122 of Cap. 32, section 111(1), (5) and (6) of Cap. 32 continues to apply in relation to an AGM at which the account or balance sheet is to be laid.

- **Annual return**

(1) Except where the company is a private company having a share capital, if the financial year (as defined in section 2(1) of Cap. 32) of the company begins before the commencement of section 662 and ends on or after that date, sections 107 and 109 of Cap. 32 continue to apply for that financial year.

(2) If the company is a private company having a share capital, sections 107 and 109 of Cap. 32 continue to apply in relation to the company's annual returns made up to a date before the commencement of section 662.

# Part 10

## Directors and Company Secretaries

### INTRODUCTION

Part 10 (Directors and Company Secretaries) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to directors and company secretaries.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 10 contains initiatives that aim at enhancing corporate governance, improving regulation and modernising the law. The initiatives that aim at enhancing corporate governance include –

- (a) restricting corporate directorship in private companies (paragraphs 6 to 8);
- (b) clarifying the standard of directors’ duty of care, skill and diligence (paragraphs 9 to 13); and
- (c) requiring ratification of conduct of directors by disinterested members’ approval (paragraphs 14 to 16).

3. The initiatives that aim at improving regulation and modernising the law include –

- (a) enabling the Registrar of Companies (“the Registrar”) to give directions to a company relating to the appointment of directors and company secretaries (paragraphs 17 to 19); and
- (b) clarifying the rules on indemnification of directors against liabilities to third parties (paragraphs 20 to 22).

4. Apart from the above major changes, this Part also restates a miscellany of provisions in the Companies Ordinance (Cap. 32) (“Cap. 32”) concerning directors and company secretaries, including directors’ vicarious liability for the acts of their alternates (**section 478**), the avoidance of acts done by a person in a dual capacity as director and company secretary (**section 479**), prohibition of undischarged bankrupt from acting as director (**section 480**) and the keeping of minutes of proceedings at directors’ meetings (**sections 481 and 482**).

5. The details of the major changes in Part 10 are set out in paragraphs 6 to 22 below.

#### Restricting corporate directorship in private companies (Section 457)

##### Position under Cap. 32

6. Cap. 32 prohibits all public companies and private companies which are members of a group of companies of which a listed company is a member from appointing a body corporate as their director. There is no restriction for other private companies.

##### Position under the new CO

7. **Section 456** of the new CO maintains the restriction in corporate directorship in public companies, companies limited by guarantee and private companies which are members of a group of companies of which a listed company is a member. As for other private companies, they are required by the new CO to have at least one director who is a natural person to enhance transparency and accountability.

### Key provisions in the new CO

8. **Section 457** restricts corporate directorship by requiring a private company (other than one within the same group as a listed company) to have at least one director who is a natural person.

### Clarifying the standard of directors' duty of care, skill and diligence (Sections 465 and 466)

#### Position under Cap. 32

9. There is no provision on directors' duty of care, skill and diligence in Cap. 32 and the common law position in Hong Kong is not entirely clear. The standard in old case law which focuses on the knowledge and experience which a particular director possesses (which is generally called the subjective test), is considered to be too lenient nowadays. There is a judicial trend in other comparable jurisdictions towards the use of a mixed objective and subjective test in the determination of the standard of care, skill and diligence expected of directors. The adoption of a mixed objective and subjective test in overseas jurisdictions has occurred through both the decisions of the courts on the common law and through confirmation of that test under statute. In light of overseas developments in the common law, it is likely that Hong Kong courts would also adopt the mixed objective and subjective test. However, there remains some uncertainty because of the absence of a clear case authority in Hong Kong.

### Position under the new CO

10. With a view to providing clear guidance to directors, the standard for company directors' duty of care, skill and diligence is clarified in the new CO to incorporate a mixed objective and subjective test.

#### Key provisions in the new CO

11. **Section 465(2)** sets out a mixed objective and subjective test for the standard in carrying out a director's duty to exercise reasonable care, skill and diligence under **section 465(1)**. The test requires the acts of a director to be judged both objectively and subjectively. In deciding whether a director of a company has breached the duty of care, skill and diligence owed by him to the company, his conduct is compared to the standard that would be exercised by a reasonably diligent person having –

- (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company (objective test in **section 465(2)(a)**); and
- (b) the general knowledge, skill and experience that the director has (subjective test in **section 465(2)(b)**).

12. **Section 465(4)** further provides that the duty has effect in place of the corresponding common law rules and equitable principles. **Section 465(5)** provides that the duty applies to a shadow director. It is considered appropriate to subject shadow directors to the same duty as a duly appointed director, because anyone

who interferes in the affairs of a company to the extent that makes him fall within the definition of a shadow director must take on the same responsibilities and duties as those of a director.

13. **Section 466** preserves the existing civil consequences of breach (or threatened breach) of the duty. The remedies for breach of the duty will be exactly the same as those that are currently available following a breach of the common law rules and equitable principles that the said duty replaces.

### Requiring ratification of conduct of directors by disinterested members' approval (Section 473)

#### Position under Cap. 32

14. There is no specific provision in Cap. 32 on ratification by members' approval of acts or omissions of directors and the ratification of acts or omissions of directors is subject to common law rules, which generally require members' approval in a general meeting to release the directors from their fiduciary duties. Ratification would have the effect of barring the company from bringing actions against the director for damages it suffered as a result of the ratified act or omission, albeit it might not prevent dissenting minorities from pursuing unfair prejudice claims or statutory derivative claims. Under the Cap. 32 regime, conflict of interest may arise in situations where the majority shareholders are directors or are connected with the directors.

#### Position under the new CO

15. The new CO requires the conduct of directors to be ratified by disinterested members' approval to prevent conflicts of interest and possible abuse of power by interested majority shareholders in ratifying the unauthorised conduct of directors.

#### Key provisions in the new CO

16. **Section 473** provides that any ratification by a company of conduct by a director amounting to negligence, default, breach of duty or breach of trust in relation to the company must be approved by resolution of the members of the company disregarding the votes in favour of the resolution by the director, any entity connected with the director and any person holding shares of the company in trust for the director or for the connected entity. **Section 473(7)(b)** preserves existing common law rules which restrict ratification.

### Enabling the Registrar to give directions to a company relating to the appointment of directors and company secretaries (Sections 458 and 476)

#### Position under Cap. 32

17. Cap. 32 requires a private company to have at least one director and a public company at least two directors. In the event of contravention, the company and every officer in default are liable to a fine. In addition, every company should appoint a company secretary though there is no offence provision for failure to appoint one.

#### Position under the new CO

18. For better enforcement of the statutory requirements to have directors and company secretaries, the new CO empowers the Registrar to issue directions to a company to appoint directors and company secretaries.

#### Key provisions in the new CO

19. **Sections 458 and 476** give the Registrar the power to issue a direction to a company where it appears to the Registrar that any of the requirements in **section 453(2), 454(1) or 457(2)** regarding the appointment of director

or in **section 474(1) or (4) or 475(2) or (3)** regarding the appointment of company secretary is contravened. Non-compliance with the direction is an offence. The company and every responsible person of the company will be liable to a fine.

### Clarifying the rules on indemnification of directors against liabilities to third parties (Sections 467 and 469 to 472)

#### Position under Cap. 32

20. The law regulating a director's right to be indemnified against liabilities to third parties is currently found in case law, which is fairly difficult for lay directors to understand. In particular, the scope of the right of directors to be indemnified against liabilities to third parties is not clear. The uncertainty over the right to be indemnified against liabilities to third parties may deter competent persons from accepting directorships.

#### Position under the new CO

21. To remove such uncertainty, the rules on indemnification of directors against liabilities to third parties are clarified.

#### Key provisions in the new CO

22. **Section 469** permits a company to indemnify a director against liability incurred by the director to a third party if the specified conditions are met. Certain liabilities and costs must not be covered by the indemnity, such as criminal fines, penalties imposed by regulatory bodies, the defence costs of criminal proceedings where the director is found guilty and the defence costs of civil proceedings brought against the director by or on behalf of the company or an associated company in which judgment is given against the director. To enhance transparency, a company which provides any permitted indemnity to its or its associated

company's directors must disclose the indemnity provision in the directors' report (**section 470**) and make it available for inspection by any member on request (**sections 471 and 472**).

## TRANSITIONAL AND SAVING ARRANGEMENTS

23. Transitional and saving arrangements are set out in **sections 88 to 94 of Schedule 11** to the new CO. The transitional provisions in respect of the major changes are as follows –

- **Section 89, Schedule 11 –**

For existing private companies with no natural person director, there will be a grace period of 6 months after the commencement of the new CO for the companies to comply with the new requirement to have at least one director who is a natural person in **section 457(2)** of the new CO. There is an exemption for existing dormant companies, but they are required to comply with the requirement when they cease to be dormant.

- **Section 90, Schedule 11 –**

Section 157 of Cap. 32 continues to apply in relation to the validity of acts of a person acting as a director done before the commencement of **section 461** of the new CO.

- **Section 92, Schedule 11 –**

So far as it relates to directors, section 165 of Cap. 32 continues to apply in relation to any relevant exemption or indemnification provision existing immediately before the commencement of **sections 468, 469 and 470** of the new CO.

# Part 11

## Fair Dealing by Directors

### INTRODUCTION

Part 11 (Fair Dealing by Directors) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to fair dealing by directors, particularly in situations in which a director is perceived to have a conflict of interest. It governs transactions involving directors or their connected entities which require members’ approval (namely loans and similar transactions, payments for loss of office and directors’ long-term employment), and covers disclosure by directors of material interests in transactions, arrangements or contracts.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 11 contains initiatives that aim at enhancing corporate governance, facilitating business and modernising the law. The initiatives that aim at enhancing corporate governance include –

- (a) expanding the prohibitions on loans and similar transactions to cover a wider category of persons connected with a director (paragraphs 5 and 6);
- (b) requiring disinterested members’ approval for various prohibited transactions (paragraphs 7 to 10);
- (c) expanding the prohibitions on payments for loss of office (paragraphs 11 to 13);
- (d) requiring members’ approval for directors’ employment exceeding 3 years (paragraphs 14 and 15); and

- (e) widening the ambit of disclosure currently required under section 162 of the Companies Ordinance (Cap. 32) (“Cap. 32”) (paragraphs 16 and 17).

3. The initiatives that aim at facilitating business and modernising the law include –

- (a) introducing new exemptions from prohibitions on loans and similar transactions in favour of directors and connected entities (paragraphs 18 to 23);
- (b) modifying the scope of private companies that are subject to more stringent restrictions similar to a public company (paragraphs 24 to 27); and
- (c) removing the criminal sanction for breach of the provisions on prohibition of loans and similar transactions in favour of directors and connected entities (paragraphs 28 and 29).

4. The details of the major changes in Part 11 are set out in paragraphs 5 to 29 below.

#### **Expanding the prohibitions on loans and similar transactions to cover a wider category of persons connected with a director (Sections 486 to 488)**

##### Position under Cap. 32

5. To avoid potential conflict of interests between a company and its directors, section 157H of Cap. 32 prohibits a company from entering into loans or other similar transactions with a director or persons connected with the director. In respect of a listed company or a

private company that is within the same group as a listed company, section 157H(8) and (9) extends the references to “director” to a spouse, child and step-child (including illegitimate child) under the age of 18, and specified categories of trustees and partners; and section 157H(2)(c), (3)(c) and (4)(c) extends the prohibitions to a company in which a director (or the above categories of persons) holds a controlling interest. These Cap. 32 references are not sufficient to cover all parties who are closely associated with directors.

#### Position and key provisions in the new CO

6. The prohibition is expanded to cover a wider category of persons connected with a director. **Sections 502 and 503** prohibit a specified company from making a loan or quasi-loan to, or enter into credit transaction as creditor for an entity connected with a director without prescribed approval of members. **Sections 486 to 488** provide for the coverage of an entity connected with a director. It covers, on top of those in Cap. 32 –

- (a) an adult child, adult step-child, adult illegitimate child or adopted child of any age;
- (b) a parent;
- (c) a cohabitee;
- (d) a minor child, minor step-child, minor illegitimate child or minor adopted child of the cohabitee who lives with the director;
- (e) an associated body corporate as defined in section 488;
- (f) a trustee of a trust which includes the director’s minor adopted child; and
- (g) a business partner of the director’s minor adopted child.

#### **Requiring disinterested members’ approval for various prohibited transactions (Sections 496, 515, 518 and 532)**

##### Position under Cap. 32

7. Except for some specified transactions (most of which relate to purchase or redemption of a company’s own shares), there is no provision in Cap. 32 restricting members’ rights to vote or requiring members to abstain from voting in relation to transactions in which they have an interest.

##### Position and key provisions in the new CO

8. In the new CO, there is a new requirement for disinterested members’ voting for connected transactions. The requirement will be applicable to public companies for various prohibited transactions, and to a private company or company limited by guarantee that is a subsidiary of a public company for loans and similar transactions.

9. **Various sections in Divisions 2 to 4 of Part 11**, which set out the requirements for members’ approval for the three types of prohibited transactions covered by Part 11 (i.e. loans, quasi-loans and credit transactions; payments for loss of office; and directors’ long-term employment), have incorporated the disinterested members’ voting requirement for public companies. For loans, quasi-loans and credit transactions, the disinterested members’ approval requirement is extended to a private company or company limited by guarantee that is a subsidiary of a public company (**sections 491, 496(2)(b)(ii) and 515(1)(b)(ii)**). If a company is

subject to the disinterested members' approval requirement, the resolution at a general meeting of such a company is passed only if every vote in favour of the resolution by the interested members is disregarded (sections 496(2)(b)(ii) and (5), 515(1)(b)(ii) and (4), 518(2)(b)(ii), (4) and (5) and 532(2)(b)(ii) and (4)).

10. In general, the members whose voting rights may be restricted include the relevant directors or former directors, relevant connected entities and any person who holds any shares in the company in trust for these persons/entities. The votes of other persons are restricted in the following circumstances –

- (a) in the case of a resolution for affirming a contravening loan or similar transaction (i.e. where the company elects to adopt the transaction despite the contravention), any other director who authorised the contravening transaction;
- (b) in the case of a payment for loss of office, the proposed recipient of the payment for loss of office, if he is not the relevant director or former director;
- (c) in the case of a payment for loss of office which is made in connection with a share transfer resulting from a takeover offer, the person who makes the takeover offer and his associates; and
- (d) any person who holds any shares in the company concerned in trust for the above categories of person.

## Expanding the prohibitions on payments for loss of office (Sections 516 to 529)

### Position under Cap. 32

11. It is unlawful under sections 163 to 163D of Cap. 32 to make payments to directors or former directors of a company, as compensations for loss of office or as consideration for retirement from office, without the company's prior approval. There are potential loopholes under these provisions –

- (a) payments may be made indirectly via other parties; and
- (b) the coverage may not be wide enough as the restriction on payment for loss of office to a director in connection with a transfer of a company's undertaking or property, or in connection with certain types of transfer of shares (sections 163A and 163B) do not cover transfers in respect of a subsidiary's undertaking or shares in the subsidiary.

### Position and key provisions in the new CO

12. To plug any potential loophole, the loss of office payment provisions are extended by **section 516(3)** to include –

- (a) payment to an entity connected with the director; and
- (b) payment to a person made at the direction of, or for the benefit of the director or an entity connected with the director.

13. Further, **section 521(2)** extends the prohibition to include payment by a company to a director or former director of its holding company. **Section 522(2)** extends the provisions to include the payment made in connection with a transfer of the undertaking or property of the company's subsidiary. By virtue of **section 516(1)** (definition of "takeover offer") and **section 523(1)**, the prohibitions in connection with a share transfer are extended to include all transfers of shares in the company or in its subsidiary resulting from a takeover offer.

### Requiring members' approval for directors' employment exceeding 3 years (Sections 530 to 535)

#### Position under Cap. 32

14. There is no provision in Cap. 32 requiring members' approval for long-term employment of a director. There is a risk that a director may arrange for himself long-term employment with his company which entrenches him in office or makes it too expensive for the company to remove him from office before his contract expires (as the director might be entitled to damages for the company's breach of contract arising from the early termination).

#### Position and key provisions in the new CO

15. The new CO requires members' approval for directors' long-term employment. **Section 534** requires the approval of the members of a company for any contracts under which the guaranteed term of employment of a director with the company exceeds or may exceed 3 years.

### Widening the ambit of disclosure as set out under section 162 of Cap. 32 (Sections 536 to 542)

#### Position under Cap. 32

16. Section 162 of Cap. 32 requires a director, who has a material interest, directly or indirectly, in a contract or proposed contract with the company which is of significance to the company's business, to disclose to the board of directors the nature of such interest at the earliest meeting of directors that is practicable. The current application of the section is relatively narrow and there is a need to widen the ambit.

#### Position and key provisions in the new CO

17. **Division 5 of Part 11 (sections 536 to 542)** restates the provisions of section 162 of Cap. 32 with modifications to keep in line with the relevant provisions of other common law jurisdictions such as the United Kingdom, and to widen the ambit of the section as follows –

- (a) the ambit of disclosure is widened to cover "transactions" and "arrangements" instead of just "contracts" (**section 536(1) and (2)**);
- (b) for a public company, the ambit of disclosure is widened to include disclosure by a director of any material interest of entities connected with him, except that a director is not required to declare an interest if he is not aware of the interest or the transaction in question (**section 536(2) and (4)(a)**);
- (c) a director is required to disclose the "nature and extent" of the interest instead of just disclosing the "nature" of the interest (**section 536(1) and (2)**); and
- (d) the disclosure requirements are extended to shadow directors (**section 540**).

## Introducing new exemptions from prohibitions on loans and similar transactions in favour of directors and connected entities (Sections 500 to 504, 505, 507 and 508)

### Position under Cap. 32

18. The decision whether to make a loan is normally taken by the directors. Section 157H of Cap. 32 prohibits, subject to certain exceptions, a company from entering into any direct or indirect loan transactions in favour of its directors, directors of its holding company or any of their connected persons. These rules are intended to protect shareholders and creditors. There are exemptions from prohibitions under section 157HA of Cap. 32 which apply to all companies. In addition, a private company which is not a member of a group which includes a listed company is exempted from the prohibitions if the loan transaction is approved by members in general meeting (section 157HA(2)).

19. Members' approval is a simple method of ensuring compliance but is currently applicable only to private companies which are not within the same group as a listed company. The narrow application of the members' approval exception is arguably too restrictive.

### Position and key provisions in the new CO

20. To facilitate business operation, the new CO extends the members' approval exception to all companies. Nevertheless, this new exception contains appropriate safeguards for minority shareholders. In the case of a public company and a private company or company limited by guarantee that is a subsidiary of a public company, the transactions must be approved by disinterested members.

21. **Sections 500 to 504** provide generally that a company must not make loans, and a company which is a public company or a private company or company limited by guarantee that is a subsidiary of a public company must not make quasi-loans or enter into credit transactions, in favour of a director of the company or of its holding company unless with the prescribed approval of members. The requirements for "prescribed approval of members" are set out in **section 496**. The prohibitions on loans are extended to a body corporate controlled by a director of the company or of its holding company and the prohibitions on quasi-loans and credit transactions are extended to entities connected with a director of the company or of its holding company.

22. Two new exceptions to the prohibitions on loans and similar transactions have been introduced –

- (a) exception for loan, quasi-loan and credit transaction of value not exceeding 5% of net assets or called-up share capital (**section 505**);
- (b) exception for funds to meet expenditure, incurred or to be incurred by a director, on defending proceedings or in connection with an investigation or regulatory action (**sections 507 and 508**).

23. Modifications have been made to the existing exceptions in section 157HA of Cap. 32 –

- (a) in the case of the exception for expenditure on company business, the conditions concerning company's approval and discharge of liability set out in section 157HA(4) as well as the financial limit with reference to 5% of the company's net assets are removed;

- (b) in the case of the exception for home loan, the financial limit of not exceeding 80% of the value of the premises has been removed and the financial limit with reference to 5% of the company's net assets has been relaxed;
- (c) in the case of the exception for leasing goods and land etc., the financial limit with reference to 5% of the company's net assets has been relaxed; and
- (d) in the case of the exception for transaction in ordinary course of business, the financial limit of \$750,000 and the further financial limit with reference to 5% of the company's net assets have been removed.

### Modifying the scope of private companies that are subject to more stringent restrictions similar to a public company (Sections 491, 501 to 504)

#### Position under Cap. 32

24. A private company that is a member of a group of companies which includes a listed company ("relevant private company") is in essence treated in the same manner as a public or listed company in Cap. 32 in respect of prohibitions on loans, quasi-loans and credit transactions in favour of a director of the company or of its holding company, or another company controlled by one or more of its directors. Under Cap. 32, public companies and relevant private companies are subject to more stringent restrictions than other private companies in the following aspects –

- (a) they are subject to additional prohibitions relating to quasi-loans and credit transactions (section 157H(3) and (4));

- (b) the prohibitions are extended to making loans or quasi-loans to or entering into credit transactions with persons connected with a director (section 157H(8)); and
- (c) they are not eligible for the members' approval exception in section 157HA(2) under which other private companies may be exempted from the prohibitions on making loans to a director if the transaction is approved by members at a general meeting.

25. A relevant private company under Cap. 32 may be a subsidiary, holding company or fellow subsidiary of a listed company.

#### Position and key provisions in the new CO

26. The new CO relaxes the prohibitions on public companies and companies limited by guarantee in respect of loans and similar transactions by extending the members' approval exception to all companies including public companies and companies limited by guarantee. As a safeguard for minority shareholders, specified companies (as defined in **section 491**) are subject to more stringent restrictions in respect of loans and similar transactions.

27. The expression "specified company" means a public company or a private company or company limited by guarantee that is a subsidiary of a public company. Therefore, a private company and a company limited by guarantee will only be subject to the tighter restrictions if they are subsidiaries of a public company, whether listed or non-listed. The more stringent restrictions relating to loans to entities connected with directors and quasi-loans and credit transactions in favour of directors or connected entities in **sections 501 to 504** of the new CO and the requirement of disinterested members' approval only apply to specified companies. Private companies will generally continue to be subject to less stringent regulations.

## Removing the criminal sanction for breach of the provisions on prohibition of loans and similar transactions in favour of directors and connected entities

### Position under Cap. 32

28. Section 157J of Cap. 32 provides for criminal sanction where there is a breach of section 157H (prohibition of loans, etc., to directors and other persons) and imposes the penalty of a fine and imprisonment. The liability extends to the company and directors who wilfully permitted or authorised the transaction and other persons who knowingly procured the company to enter into the transaction.

### Position and key provisions in the new CO

29. The criminal sanction provisions in section 157J of Cap. 32 are repealed by the new CO as it is considered that the civil consequences under **section 513** for contravention of the provisions on loans and similar transactions are sufficient. The rationale is that there is a danger of over-deterrence if criminal sanctions are attached to general directors' duties of loyalty rather than closely defined wrongdoing, and that enforcement of such duties should be a civil matter for the companies.

## TRANSITIONAL AND SAVING ARRANGEMENTS

30. Transitional and saving arrangements are set out in **sections 95 to 97 of Schedule 11** to the new CO. The transitional provisions in respect of the major changes are as follows –

- **Section 95 of Schedule 11 –**

If a company has dispensed with the holding of an annual general meeting in accordance with section 613 of the new CO, the condition specified in section 157HA(4)(b) of Cap. 32 in respect of a transaction described in section 157HA(3)(a) of Cap. 32, which is still outstanding on the commencement of Division 2 of Part 11 continues to apply as if it provided that –

- (a) the approval of the company is required on or before the last date on which the company would otherwise have been required to hold an annual general meeting; and
- (b) any liability falling on any person in connection with the transaction must be discharged within 6 months after that date if that approval is not forthcoming.

- **Section 96 of Schedule 11 –**

Sections 163, 163A, 163B, 163C and 163D of Cap. 32 continue to apply in relation to a loss of office or retirement specified in those sections that occurred before the commencement of Division 3 of Part 11. A loss of office or retirement occurred in the case of a directorship, when the person ceased to be a director, or in the case of any other office, when the person ceased to hold the office.

# Part 12

## Company Administration and Procedure

### INTRODUCTION

Part 12 (Company Administration and Procedure) of the new Companies Ordinance (Cap. 622) (“new CO”) governs resolutions and meetings, keeping of registers, company records, registered offices, publication of information relating to companies and annual returns.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 12 contains initiatives that aim at enhancing corporate governance, facilitating business and modernising the law. The initiatives that aim at enhancing corporate governance include –
  - (a) Introducing a comprehensive set of rules for proposing and passing a written resolution (paragraphs 5 to 8);
  - (b) Requiring a company to bear the expenses of circulating members’ statements relating to business of, and proposed resolutions for, Annual General Meetings (“AGMs”) (paragraphs 9 to 12); and
  - (c) Reducing the threshold requirement for members to demand a poll from 10% to 5% of the total voting rights (paragraphs 13 to 14).
3. The initiatives that aim at facilitating business include –
  - (a) Permitting a general meeting to be held at more than one location by using technology that enables members apart to listen, speak and vote at the meeting (paragraphs 15 to 16);
  - (b) Allowing companies to dispense with AGMs by unanimous members’ consent (paragraphs 17 to 20); and
  - (c) Updating the provisions relating to keeping and inspection of company records (paragraphs 23 to 32).
4. The initiatives that aim at modernising the law include –
  - (a) Clarifying the rights and obligations of proxies and enhancing the right to appoint proxies (paragraphs 21 to 22);
  - (b) Requiring public companies or companies limited by guarantee to file annual returns in respect of every financial year and requiring the annual return of a listed company to include particulars relating to members who held 5% or more of the issued shares (paragraphs 33 to 36); and
  - (c) Empowering the Financial Secretary (“FS”) to make regulations to require a company to display its name and related information in certain locations and to state prescribed information in documents or communications (paragraphs 37 to 38).

## Introducing a comprehensive set of rules for proposing and passing a written resolution (Sections 548 to 561)

### Position under the Companies Ordinance (Cap. 32) (“Cap. 32”)

5. Section 116B of Cap. 32 provides that anything which may be done by a company by resolution in a general meeting may be done, without a meeting and without any previous notice, by a resolution signed by all members of a company. There is widespread use of such written resolutions, especially by small and medium-sized enterprises, for their decision-making process but there are no established statutory rules for proposing and passing a written resolution.

### Position under the new CO

6. The new CO provides the procedures for proposing, passing and recording written resolutions. The new procedures facilitate the use of written resolutions for decision-making, which is more expeditious and less costly than passing a resolution in a general meeting.

### Key provisions in the new CO

7. **Subdivision 2 of Division 1** of Part 12 provides the procedures for proposing, passing and recording written resolutions. **Section 549** provides that the directors or a member of a company may propose a resolution as a written resolution. A member of the company who proposes the resolution may request the company to circulate with the resolution a statement of not more than 1 000 words on the subject matter of the resolution (**section 551**). Once a written resolution is proposed, the company has a duty to circulate the resolution to every member for agreement if it has received requests from members representing not less than 5% of the total voting rights or a lower percentage specified

in the company’s articles (**section 552**). The circulation may be effected by sending the copies in hard copy form or electronic form or by making the copies available on a website (**section 553**). The period for agreeing to the proposed written resolution is 28 days or such period as specified in the company’s articles (**section 558**). Members may signify their agreement to a proposed written resolution and send it back to the company either in hard copy form or electronic form (**section 556**). If a resolution is passed as a written resolution, the company must send a notice of that fact to every member and the auditor of the company within 15 days (**section 559**).

8. The new procedures will not replace the common law doctrine of unanimous consent or so-called *Duomatic* principle that, if all the members of a company actually agree on a particular decision which can be made at a general meeting, the decision is binding and effective without a meeting (**section 547(3)** which restates the law under section 116BB(2) of Cap. 32). A company’s articles may also set out alternative procedures for passing a resolution without a meeting, provided that the resolution has been agreed by the members unanimously (**section 561**).

## Requiring a company to bear the expenses of circulating members’ statements relating to business of, and proposed resolutions for AGMs (Sections 580 to 582, 615 and 616)

### Position under Cap. 32

9. Section 115A of Cap. 32 enables members representing at least 2.5% of the total voting rights of a company or 50 or more members who have paid up an average sum of not less than \$2,000 per member, to request the company to circulate a proposed resolution for the next AGM or a statement of not more than 1 000 words

relating to any proposed resolution or business to be dealt with at any general meeting. A company is not bound to circulate a statement where the court is satisfied that the right is being abused to secure needless publicity for defamatory matter. Under section 115A(1), members making the requisition need to bear the expenses unless the company resolves otherwise. This may hinder minority shareholders from making such requisition.

#### Position under the new CO

10. To enhance the right of minority shareholders, the expenses of circulating members' proposed resolutions for AGMs, and members' statements relating to the proposed resolution or other business to be dealt with at AGMs will be borne by the company, if the required threshold for requests to circulate such documents are received in time for sending with the notice of the meeting. The criteria for not requiring the circulation of a members' statement is changed to abuse of the right to require circulation or where such right is being used to secure needless publicity for defamatory matter.

#### Key provisions in the new CO

11. **Section 580** provides members a power to request circulation of statements concerning the business to be dealt with at general meetings along the lines of section 115A of Cap. 32. **Section 581** imposes a duty on the company to circulate members' statements in the same manner as the notice of meeting. Under **section 582**, if the meeting concerned is an AGM and the required requests for circulation of a members' statement is received in time for sending with the notice of the meeting, the expenses will be borne by the company. Otherwise, the expenses will be paid by the members concerned. **Section 583** provides that a company is not required to circulate a statement if the court is satisfied that the rights given by **section 580** are being abused or used to secure needless publicity for defamatory matter.

12. **Sections 615** and **616** contain similar provisions in respect of members' proposed resolutions for AGMs. The required circulation requests must be received by the company not later than 6 weeks before the AGM, or if later, before the time at which notice of meeting is given. The company is obliged to circulate the resolution at the company's expense, which is a new requirement.

#### **Reducing the threshold requirement for members to demand a poll from 10% to 5% of the total voting rights (Section 591)**

#### Position under Cap. 32

13. Under section 114D of Cap. 32, members have the right to demand a poll and such a right cannot be excluded by the articles. It may be exercised on any question, except the election of the chairman of the meeting or the adjournment of the meeting, if the demand is made by –

- (a) not less than 5 members having the right to vote at the meeting;
- (b) members representing not less than 10% of the total voting rights; or
- (c) members holding not less than 10% of the total paid up share capital of the company carrying the right to vote at the meeting.

A proxy has the same right as the member for whom he is proxy to join in demanding a poll.

#### Key provision in the new CO

14. In line with the provision in section 113 of Cap. 32 that shareholders holding not less than 5% of the voting rights are able to requisition an extraordinary general meeting, the threshold requirement for demanding a poll is lowered from 10% to 5% of the total voting rights under **section 591**.

## Permitting a general meeting to be held at more than one location by using technology that enables members apart to listen, speak and vote at the meeting (Section 584)

### Position under Cap. 32

15. With the development of electronic communications, it is not uncommon for a company to hold its general meeting at two or more venues with advanced technology. However, Cap. 32 does not have express provision permitting a general meeting to be held at two or more places.

### Key provision in the new CO

16. To keep up with technological development and subject to any provision of the company's articles, **section 584** permits a company to hold a general meeting at two or more places using any technology that enables the members of the company who are not together at the same place to listen, speak and vote at the meeting. A company may set out rules and procedures for holding a dispersed meeting in its articles.

## Allowing companies to dispense with AGMs by unanimous members' consent (Sections 612 to 614)

### Position under Cap. 32

17. Every company is required to hold AGMs under section 111 of Cap. 32. A company may however dispense with holding AGMs if everything that is required or intended to be done at the meeting is done by written resolutions in accordance with section 116B of Cap. 32, and a copy of each of the documents (including any accounts or records) which under Cap. 32 would be required to be laid before the meeting is provided to each member of the company (section 111(6)). For many private companies, the

obligation to hold AGMs could be redundant and potentially burdensome.

### Position under the new CO

18. To simplify the decision-making process, a company may dispense with the requirement for holding of AGMs and a single member company is not required to hold an AGM at all.

### Key provisions in the new CO

19. **Section 613** allows a company to dispense with the requirement for holding of AGMs by passing a written resolution or a resolution at a general meeting by all members. Under **Section 622**, the company is required to deliver a copy of the resolution to the Registrar of Companies ("the Registrar") for registration within 15 days after it is passed. After passing the resolution, the company will not be required to hold any AGMs for the financial year or for subsequent financial years to which the resolution relates. The financial statements and reports originally required to be laid before an AGM will still need to be sent to the members under **section 430(3)** of Part 9. Any member may request the company to convene an AGM for a particular year under **section 613(5)**. The company may also revoke the resolution by passing an ordinary resolution to that effect under **section 614**. For a single member company, **section 612(2)(a)** provides that such a company is not required to hold an AGM at all.

20. In practice, it is unlikely for a public or a guarantee company to dispense with holding an AGM by unanimous members' consent but the possibility could not be ruled out. The written resolution procedure under section 111(6) of Cap. 32 is therefore retained in **section 612(1)** in case a company might wish to dispense with an AGM on a specific occasion by a written resolution. This provision also provides flexibility for private companies which do not wish to dispense with AGMs under **section 613**.

## Clarifying the rights and obligations of proxies and enhancing the right to appoint proxies (Sections 588, 591, 596, 602 to 605)

### Position under Cap. 32

21. The system of proxy voting helps ensure that the views of members who are unable to attend a meeting in person will still be voiced and considered. There are a number of limitations in Cap. 32 concerning proxies –

- (a) unless the articles otherwise provide, a proxy is not entitled to vote on a show of hands (section 114C(1A)(a));
- (b) there is no statutory provision expressly providing that a proxy may be elected as a chairman of a meeting;
- (c) there is no requirement for a proxy to vote on a poll according to the terms of appointment;
- (d) there is no express provision for the revocation of the appointment of a proxy if the appointor attends and votes at the meeting;
- (e) members of a company limited by guarantee may have a right to appoint a proxy only if it is provided in the company's articles (section 114C(1A)). It is noted that some guarantee companies may wish to exclude non-members from attending their meetings and from being appointed as proxies; and
- (f) unless the articles otherwise provide, the number of proxies that may be appointed by a shareholder to attend on the same occasion is limited to two (section 114C(2)). Such a default cap on the maximum number of proxies that a shareholder may appoint on the same occasion is considered to be unnecessarily restrictive.

### Key provisions in the new CO

22. The rights and obligations of a proxy are clarified in the following manner –

- (a) **Section 596** provides that a member of a company is entitled to appoint a proxy and **section 596(2)** provides that a company limited by guarantee may confine proxies to members of the company in its articles;
- (b) **Section 596(3)** allows multiple proxies in the case of a company having a share capital. Multiple proxies can only vote on a poll. They are not entitled to vote on a show of hands because it would go against the basis upon which the show of hands mechanism was premised, thus distorting the result (**section 588(2)**);
- (c) **Section 596(1)** provides that a proxy may exercise all or any of the member's rights to attend and to speak and vote at a general meeting (i.e. including voting on a show of hands, multiple proxies excepted) and **section 591(3)** authorises a proxy to demand a poll;
- (d) **Section 602** expressly provides that a proxy may be elected as the chairperson of the general meeting, subject to any provisions of the company's articles;
- (e) Where a proxy put forward by a company is appointed by a member to be his proxy, **section 603(2)** requires the proxy to vote in the way specified in the appointment of the proxy. This is to overcome the possibility of a member being disenfranchised by a person, who is put forward by the board as a proxy, deliberately failing to vote in accordance with the member's instructions; and

- (f) **Section 605(1)** provides that the appointment of a proxy will be revoked if the appointor attends in person and votes at the meeting.

## Updating the provisions relating to keeping and inspection of company records

### Position under Cap. 32

23. There are rights to inspect certain records which are required to be kept by companies under Cap. 32. Copies of the records may also be provided in some cases. Such records comprise registers, minutes, copies of resolutions and other documents required to be kept by a company and include –

- Register of debenture holders (section 75)
- Register of charges (section 90)
- Register and index of members (sections 95, 96, 98, schedule 14) and branch registers (sections 103, 104)
- Register of quasi-loans and credit transactions (section 161BB)
- Written resolutions of members, records of minutes of proceedings of meetings of members and decisions of a sole member (sections 116B, 116BC, 119, 119A, 120)
- Books of accounts (section 121)
- Management contracts (section 162A)
- Register of directors and secretaries (sections 158, 158A).

24. Section 348C of Cap. 32 applies generally to the form in which such records are required to be kept by a company. Specifically, where records are kept by the company otherwise than in legible form, inspection of a reproduction of such records in legible form is required (section 348C(3)). The arrangement for inspection and provision of copies

of individual types of records, such as the time allowed for inspection, the number of days within which a copy of the requested records should be sent, and the maximum fees payable, vary. These requirements are prescribed individually for each type of record in the respective sections or schedule.

25. Under section 103 of Cap. 32, a company must apply to the Chief Executive for a licence for keeping a branch register of members outside Hong Kong and pay an annual licence fee. However, it is considered that the licence system is out of date and may discourage Hong Kong companies from listing their shares on an overseas stock exchange.

26. As regards the period of time for keeping the records, section 95(1)(c)(ii) of Cap. 32 provides in respect of the register of members that entries relating to a former member of a company may be destroyed after 30 years. Cap. 32 is otherwise silent on the period for keeping other records such as records of resolutions and meetings. The period of 30 years for keeping records of former members is considered too long compared to comparable overseas jurisdictions and taking into account that accounting records are only required to be kept for 7 years under section 121 of Cap. 32 (restated in section 377(2) of the new CO).

### Position under the new CO

27. While the main provisions concerning the rights to inspect and obtain copies of records are retained in the new CO, the detailed provisions concerning the arrangement for inspection and provision of copies and related matters will be provided for by subsidiary legislation. The relocation of provisions consolidates the arrangements for different types of company

records, and allows a consistent and comprehensive approach covering different types of company records, thus facilitating compliance by companies and timely updating of the detailed arrangements in future to meet changing needs.

28. The new CO contains provisions that apply to all “*company records*” which is defined in **section 654** to mean any register, index, agreement, memorandum, minutes or other document required by the new CO to be kept by a company, but does not include accounting records (which are governed by sections 373 to 378). To cater for the relocation, **section 657** provides that the detailed requirements concerning inspection and provision of copies of company records may be provided by regulations.

29. The licence system and fee for keeping a branch register outside Hong Kong is abolished and replaced by a notification system which requires companies that keep a branch register to notify the Registrar of the address where the branch register is kept and of any change in the address or discontinuation of the register.

30. The 30-year period provided in section 95 of Cap. 32 for keeping entries of former members in the register of members is reduced to 10 years in the new CO. Incidental to that change, the 30-year time limit prescribed in section 102(2) of Cap. 32 for adducing evidence to challenge the accuracy of an entry in the register of members is removed. Removal of the 30-year time limit has the effect of removing any limitation on admissibility of evidence for the purpose of rectification of the register by the court. As regards other records e.g. records of resolutions and meetings of members, the new CO provides a minimum period of 10 years for keeping such records.

#### Key provisions in the new CO

31. **Sections 618, 619 and 620** provide that a company must keep its records of resolutions and meetings of members, etc. available for inspection at the company's registered office or a prescribed place. The prescribed place, manner of inspection and the fees payable in respect of the records are set out in the regulations that the FS is empowered to make under **section 657** (i.e. Company Records (Inspection and Provision of Copies) Regulation (Cap. 622I)). Similar requirements apply to other company records, for example, the company's register of members (**sections 627, 628 and 631**), the register of directors (**sections 641 and 642**) and the register of company secretaries (**sections 648 and 649**) which are required to be kept separately under the new CO. **Section 655(4)** allows inspection of company records kept in electronic form to be inspected by electronic means if so requested by the person inspecting the records.

32. **Sections 636 to 639** provide for new requirements in relation to the keeping of a branch register of members outside Hong Kong. The requirement for a company to keep records of resolutions and meetings of members, etc. and entries relating to former members in the register of members for 10 years is provided in **sections 618 and 627** respectively. **Section 635** provides that the register of members is prima facie evidence of the matters therein. No time limit for adducing evidence to challenge the accuracy of an entry in the register is specified in the new CO.

**Requiring public companies or companies limited by guarantee to file annual returns in respect of every financial year and requiring the annual return of a listed company to include particulars relating to members who held 5% or more of the issued shares (Sections 662, 664 and section 2 of Schedule 6 to the new CO)**

Position under Cap. 32

33. Section 122 of Cap. 32 requires accounts to be made out every year and to be laid before the company at its AGM, and those accounts must be made up to a date falling not more than a specified number of months before the date of the AGM. Section 111 of Cap. 32 requires every company to hold an AGM in each year and not more than 15 months is to elapse between the date of one AGM and the next. Section 109(1) of Cap. 32 provides that, except where the company is a private company having a share capital, the annual return is required to be filed within 42 days after the AGM for the year. Section 109(3) of Cap. 32 further provides that, except where the company is a private company, the annual return shall include certified copies of the company's balance sheet and reports laid before the company in general meeting to which the return relates.

Position under the new CO

34. With regard to the annual return of a public company or company limited by guarantee, the requirement to file the annual return within 42 days of the AGM under section 109(1) of Cap. 32 is changed as an AGM may be dispensed with under **section 612(2)** of the new CO. The annual return is no longer required to be filed in each calendar year. There is no change to the requirement to file annual returns of private companies under section 109(1A) of Cap. 32 (section 662(1), (2) of new CO), which requires

the annual return of a private company to be completed within 42 days after the anniversary of the date of its incorporation and filed forthwith.

Key provisions in the new CO

35. **Section 610** sets out the requirements for companies to hold AGMs. In the case of a public company or a company limited by guarantee, **section 662(3) and (4)** provides that the annual return is to be filed within 42 days after the company's return date i.e. 6 months (for public companies) or 9 months (for companies limited by guarantee) after the end of the company's accounting reference period. Sections 368 to 370 in Part 9 of the new CO provide for the determination of the accounting reference period of a company.

36. **Section 664(3)** provides that an annual return must contain the information specified in Schedule 6. **Section 2 of Schedule 6** provides that in the case of a listed company, the particulars relating to members and share capital required in the annual return are limited to those relating to members who held 5% or more of the issued shares in any class of the company's shares as at the date of the return.

**Empowering the FS to make regulations to require a company to display its name and related information in certain locations and to state prescribed information in documents or communications (Section 659)**

Position under Cap. 32

37. Under section 93(1) of Cap. 32, every company must display its name on the outside of every office or place in which its business is carried on and mention its name in the documents specified in that section (e.g. business letters, notices, official publications, and contracts).

## Position under the new CO

38. There are changes to the rules on publication of company names. As the rules involve technical details and may change with developments in technology, they are stated in the subsidiary legislation to facilitate future amendments. **Section 659** empowers the FS to make the relevant regulations which are contained in the Companies (Disclosure of Company Name and Liability Status) Regulation (Cap. 622B).

## TRANSITIONAL AND SAVING ARRANGEMENTS

39. Transitional and saving arrangements are set out in **sections 98 to 121 of Schedule 11** to the new CO and are basically as follows –

- **Written resolution**

Sections 116B (except subsections (7), (8), (9) and (10)), 116BA and 116BB of Cap. 32 continue to apply in relation to resolutions sent or circulated to a member before the commencement of **Subdivision 2 of Division 1 of Part 12**.
- **Members' statements**

In so far as it relates to the circulation of any statement in relation to an AGM, section 115A of Cap. 32 continues to apply in relation to requisitions made to a company under section 115A(1)(b) of Cap. 32 before the commencement of **Subdivision 6 of Division 1 of Part 12**.
- **Voting at meetings**

Sections 114A(1)(e), 114D, 114E and 116(2) of Cap. 32 continue to apply to meetings of which notice was given before the commencement of **Subdivision 8 of Division 1 of Part 12**.
- **Proxies and corporate representatives**

Sections 114C and 115 of Cap. 32 continue to apply to meetings of which notice was given before the commencement of **Subdivision 9 of Division 1 of Part 12**.
- **Annual general meetings**
  - (1) The repeal of section 115A of Cap. 32 does not affect its application in relation to a requisition under section 115A(1)(a) of Cap. 32 made to a company before the repeal.
  - (2) If a company is required to lay at its AGM an account or a balance sheet in accordance with section 122 of Cap. 32, section 111(1), (5) and (6) of Cap. 32 continue to apply in relation to an AGM at which the account or balance sheet is to be laid.
  - (3) In so far as it relates to giving notice of a resolution in relation to an AGM, section 115A of Cap. 32 continues to apply in relation to requisitions made to a company under section 115A(1)(a) of Cap. 32 before the commencement of **sections 615 and 616** of the new CO.
- **Records of resolutions and meetings**
  - (1) Sections 116B(7), (8), (9) and (10), 116BC, 119, 119A and 120 of Cap. 32 continue to apply in relation to resolutions passed, meetings held or decisions taken before the commencement of **sections 617 to 621**.
  - (2) A company is not required to keep a record or the minutes that have been entered into a book in accordance with section 116B(7), 116BC(3) or 119(1) of Cap. 32 if the record or the minutes have been kept for at least 10 years from the date of the resolution, meeting or decision, as the case may be.

- **Right to inspect records of resolutions and meetings**

Sections 120(1), (3) and (4) and 348C(3) of Cap. 32 continue to apply in relation to –

- (1) a request received by the company before the commencement of **section 620** for inspecting the books containing the minutes of proceedings of any general meeting of the company;
- (2) a request received by the company before the commencement of **section 620** for inspecting the record made in accordance with section 116B(7) of Cap. 32; and
- (3) a request received by the company before the commencement of **section 620** for inspecting the record made in accordance with section 116BC(3) of Cap. 32.

- **Right to obtain copies of records of resolutions and meetings**

Sections 120(2), (3) and (4) and 348C(3) of Cap. 32 continue to apply in relation to –

- (1) a request received by the company before the commencement of **section 620** for a copy of the books containing the minutes of proceedings of any general meeting of the company;
- (2) a request received by the company before the commencement of **section 620** for a copy of the record made in accordance with section 116B(7) of Cap. 32; and
- (3) a request received by the company before the commencement of **section 620** for a copy of the record made in accordance with section 116BC(3) of Cap. 32.

- **Register of members**

- (1) A register of members kept under section 95 of Cap. 32 is to be regarded as a register of members kept for the purposes of **section 627**.
- (2) Sections 98(1), (3) and (4) and 348C(3) of Cap. 32 continue to apply in relation to a request received by the company before the commencement of **section 631** for inspecting a register of members or index of members' names.
- (3) Sections 98(2), (3) and (4) and 348C(3) of Cap. 32 continue to apply in relation to a request received by the company before the commencement of **section 631** for a copy of a register of members (or any part of it).
- (4) Section 99 of Cap. 32 continues to apply in relation to a closure of a register of members if the notice for the closure was given before the commencement of **section 632**.
- (5) Section 104 of Cap. 32 continues to apply in relation to a register of members kept under a licence issued under section 103 of Cap. 32.

- **Inspection of register of directors and secretaries**

Sections 158(7), (8) and (9) and 348C(3) of Cap. 32 continue to apply in relation to a request received by the company before the commencement of **sections 642 and 649** for inspecting a register of directors and secretaries.

- **Register of directors**

A register of directors and secretaries kept by a company under section 158(1) of Cap. 32, in so far as it relates to the company's directors or reserve directors, is to be regarded as a register of directors kept for the purposes of **section 641**.

- **Register of company secretaries**

A register of directors and secretaries kept by a company under section 158(1) of Cap. 32, in so far as it relates to the company secretary or joint company secretaries of the company, is to be regarded as a register of company secretaries kept for the purposes of **section 648**.

- **Annual return**

(1) Except where the company is a private company having a share capital, if the financial year (as defined in section 2(1) of Cap. 32) of the company begins before the commencement of **section 662** and ends on or after that date, sections 107 and 109 of Cap. 32 continue to apply in relation to the company for that financial year.

(2) If the company is a private company having a share capital, sections 107 and 109 of Cap. 32 continue to apply in relation to the company's annual returns made up to a date before the commencement of **section 662**.

# Part 13

## Arrangements, Amalgamation, and Compulsory Share Acquisition in Takeover and Share Buy-Back

### INTRODUCTION

Part 13 (Arrangements, Amalgamation, and Compulsory Share Acquisition in Takeover and Share Buy-Back) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to schemes of arrangement or compromise with creditors or members, reconstructions or amalgamations of companies, and compulsory acquisitions of shares following a takeover offer or following a general offer for a share buy-back.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. This Part largely restates the relevant provisions under the Companies Ordinance (Cap. 32) (“Cap. 32”). However the following changes that aim at facilitating business have been introduced –

- (a) revising the definitions of “property” and “liabilities” in the provisions for facilitating reconstructions and amalgamations (paragraphs 15 to 17);
- (b) introducing a new court-free statutory amalgamation procedure for wholly-owned intra-group companies (paragraphs 18 to 22);
- (c) clarifying the meaning of “takeover offer”, “shares already held by the offeror” and “shares to which the offer relates” in a takeover (paragraphs 23 to 27);

- (d) introducing new provisions to allow a revised offer to be treated as the original offer so long as certain specified conditions are met (paragraphs 28 to 29); and
- (e) introducing new provisions to allow an offeror in a takeover offer or share buy-back offer to apply to the court for an authorisation to give squeeze out notices (paragraphs 30 to 32).

3. The “headcount test” for approving a scheme of arrangement that involves a general offer or a takeover offer is replaced with the requirement that the votes cast against the scheme do not exceed 10% of the voting rights attached to all disinterested shares. The test is retained for other schemes but the court is given a new discretion to dispense with the test for members’ schemes that retain the test (paragraphs 5 to 14).

4. The details of the major changes in Part 13 are set out in paragraphs 5 to 32 below.

### Replacing the “headcount test” for approving certain schemes of arrangement with a new test and giving the court a new discretion to dispense with the test for members’ schemes that retain the test (Sections 673, 674 and 676)

#### Position under Cap. 32

5. Section 166 of Cap. 32 provides that where a scheme is proposed between a company and its members or creditors or any class of them, the court may order a meeting of the members or

creditors or a class of them to be summoned. The section also provides that if a majority in number (“headcount test”) representing three-fourths in value (“share value test”) of the creditors or members (or classes of creditors or members) present and voting at the meeting agree to the proposed scheme, the scheme shall, if sanctioned by the court, be binding on all members or creditors and the company.

6. The court has the discretion not to sanction a scheme even though it has been approved under both the share value test and the headcount test (for instance, where there is doubt that the process has been unfairly administered, such as where the approval under the headcount test was achieved by share splitting). Nevertheless, the court does not have the jurisdiction to sanction a scheme where the headcount test had not been passed even in the event that share splitting has increased the headcount of members opposing the scheme.

#### Position under the new CO

7. There were divergent views expressed by the respondents during the public consultation on the draft Companies Bill (“CB”) regarding the abolition or retention of the headcount test for members’ schemes. In particular, there is concern that the abolition may undermine the protection of the interests of minority shareholders. For public and listed companies, while the Code on Takeovers and Mergers (“Takeovers Code”) offers some protection for minority shareholders, it is intended to supplement, but not substitute, the statutory protection in Cap. 32. Rule 2.10(b) of the Takeovers Code stipulates that the number of votes cast against the resolution

shall not be more than 10% of the voting rights attached to all disinterested shares, i.e. shares not held by the controlling shareholders or their connected parties.

8. The Bills Committee on the CB of the Legislative Council held in-depth discussions on the headcount test and invited deputations to give views on the test. The majority view among the deputations is to abolish the headcount test. The main concerns are that the test is contrary to the “one share, one vote” principle and it has inherent problems, such as vote manipulation through share splitting and the difficulty to reflect the wish of the overwhelming majority of listed shares held in the names of nominees and custodians.

9. On the other hand, there is also a general consensus that, given the binding nature of these schemes, there should be adequate safeguard to protect the interest of the minority shareholders. If the headcount test is abolished without any replacement safeguard, the only test will be the share value test. In terms of the level of statutory protection for minority shareholders, this is incommensurate with the binding nature of the schemes.

10. To strike a reasonable balance, the headcount test is replaced with a new test based on the concept of the 10% objection rule of the Takeovers Code for certain members’ schemes. For other members’ schemes that retain the headcount test, the court is given a new discretion to dispense with the test in special circumstances, such as where there is evidence that the result of the vote has been unfairly influenced by share splitting.

11. As for creditors' schemes, the concern for vote manipulation and problems arising from nominee shareholdings do not exist. It is desirable to retain the headcount test to protect small creditors. As it is unlikely for small creditors who oppose a proposed scheme to manipulate the outcome of voting by assigning part of their debts to other persons, there is therefore no need to extend the court's discretion to dispense with the headcount test to cover creditors' schemes.

#### Key provisions in the new CO

12. **Sections 673 and 674(1)** basically restate section 166 of Cap. 32. **Section 674(1)(c)(ii) and (d)(ii)** gives the court a discretion to dispense with the headcount test for members' schemes that retain the headcount test.

13. **Section 674(2)(a)(ii) and (b)(ii)** sets out the new requirement that replaces the headcount test. It provides that the number of votes cast against the resolution to approve a scheme of arrangement is not more than 10% of the votes attached to all disinterested shares. The new requirement would apply to the following two types of schemes of arrangement –

- (a) takeover offer within the meaning of section 674(5); and
- (b) general offer for share buy-back within the meaning of section 707.

"Disinterested shares" is defined in **section 674(3)** and basically means shares held by non-interested parties. Parties that may be included as "interested parties" are: (a) the company which makes the buy-back offer and the non-tendering member, plus their associates and nominees; and (b) the offeror and his associates and nominees. The term "associate" is defined in section 667.

14. To address the concern that minority shareholders are reluctant to challenge a scheme in Court because of the potentially huge legal costs, **section 676(5)** provides that a dissenting member may be ordered to pay legal costs only if his opposition to the scheme is frivolous or vexatious.

#### **Revising the definitions of "property" and "liabilities" in the provisions for facilitating reconstructions and amalgamations (Section 675)**

##### Position under Cap. 32

15. Section 167(4) of Cap. 32 defines "property" as including "property, rights and powers of every description" and "liabilities" as including "duties". Based on decided cases, a transfer order made under section 167 to facilitate reconstructions and amalgamations is unable to operate to transfer a contract of personal service. As a result, contracts of employment are not transferable under the section.

##### Position under the new CO

16. Personal rights and duties, which could not have been transferred and assigned unless with the consent of the parties concerned, may be transferred or assigned once a transfer order is made.

##### Key provisions in the new CO

17. **Sections 668 to 677** basically restate with modifications the provisions on schemes of arrangements in sections 166, 166A and 167 of Cap. 32, except the headcount test (see paragraphs 12 to 14 above). **Section 675** sets out additional powers which the court may exercise

to facilitate reconstructions or amalgamations of companies. In particular, **section 675(8)** defines “property” as including rights and powers of a personal character and incapable of being assigned or performed vicariously under the law; and rights and powers of any other description. “Liabilities” is defined as including duties of a personal character and incapable of being assigned or performed vicariously under the law; and duties of any other description.

### Introducing a new court-free statutory amalgamation procedure (Sections 678 to 686)

#### Position under Cap. 32

18. Under Cap. 32, companies intending to amalgamate have to resort to the procedures under sections 166 to 167 which require court sanction. In practice, sections 166 to 167 are rarely used given the high cost involved.

#### Position under the new CO

19. A court-free regime for amalgamations is provided in Division 3. To minimise the risk of abuse, the court-free regime is confined to amalgamations of wholly-owned intra-group companies where minority shareholders’ interest would normally not be an issue.

#### Key provisions in the new CO

20. **Sections 680 and 681** provide that an amalgamation may either be vertical (i.e. between the holding company and one or more of its wholly-owned subsidiaries) or horizontal (i.e. between two or more subsidiaries of the same holding company). The board of each amalgamating company must make a statement

(i) to confirm that the assets of the amalgamating company is not subject to any floating charge, or if there exists a floating charge, the chargee has consented to the amalgamation proposal, and (ii) to verify the solvency of the amalgamating company as well as the amalgamated company. Details of the solvency statement are set out in **section 679**. The amalgamation proposal must be approved by the members of each amalgamating company by special resolution.

21. As the effect of amalgamation is that the amalgamated company takes the benefits and is subject to the liabilities of the amalgamating companies (**section 685(3)**), this poses a problem when two or more of the amalgamating companies have floating charges subsisting over their respective assets in favour of different security holders. There will be a question of priorities between the competing security holders over the assets of the amalgamated company, which may result in unfairness between the security holders. The written consents of the holders of the floating charges are therefore required (**sections 680(2)(d)(ii) and 681(2)(d)(ii)**).

22. **Section 686** provides that before the effective date of the amalgamation proposal, the court may disallow or modify the amalgamation proposal or give directions, if it is satisfied that giving effect to the amalgamation proposal would unfairly prejudice a member or creditor of an amalgamating company or a person to whom an amalgamating company is under an obligation, on application by a member or creditor of an amalgamating company or such a person. This is to protect the interests of the minority shareholders and creditors in the course of the amalgamating process.

## Clarifying the meaning of “takeover offer”, “shares already held by the offeror” and “shares to which the offer relates” in a takeover (Sections 689, 691, 707 and 709)

### Position under Cap. 32

23. Section 168 of Cap. 32, together with the Ninth Schedule to Cap. 32, deal with the compulsory acquisition of shares following a takeover. Section 168 applies, inter alia, where a company makes an offer to acquire all the shares not already held by it in another company on terms which are the same in relation to all the shares to which the offer relates. There are no clear definitions of what would constitute “shares already held by an offeror” and “shares to which the offer relates”.

### Key provisions in the new CO

24. The meaning of the above terms is clarified in the new CO. **Section 689(1)** defines a takeover offer. First, it must be an offer to acquire all the shares (or shares of any class) in the company except those that, at the date of the offer, are held by the offeror. Secondly, in relation to all the shares to which the offer relates (or all the shares of the class to which the offer relates), the terms of the offer must be the same.

25. **Section 689(3)** provides that “shares that are held by an offeror” include shares that the offeror has contracted, unconditionally or conditionally to acquire, but exclude shares that are subject to a contract which is intended to secure that the holder of the shares will accept the offer when it is made and entered into for no consideration and by deed, for consideration of negligible value, or for consideration consisting of a promise by the offeror to make the offer.

26. **Sections 689 and 691** clarify that shares to which a takeover offer relates may include:

- (a) shares that are allotted after the date of the offer but before a date specified in the offer (**section 689(6)**);
- (b) shares which the offeror acquires or contracted to acquire other than by virtue of acceptances of the offer during the offer period unless the acquisition consideration exceeds the consideration specified in the terms of the offer (**section 691(2)**); and
- (c) shares which a nominee or an associate of the offeror has contracted to acquire after a takeover offer is made but before the end of the offer period, unless the acquisition consideration exceeds the consideration specified in the offer (**section 691(4)**).

27. **Sections 707(1), 707(3) and 709** contain similar provisions in relation to compulsory acquisition powers following a share buy-back offer.

## Introducing new provisions to allow a revised offer to be treated as the original offer so long as certain specified conditions are met (Sections 692 and 710)

### Position under Cap. 32

28. Cap. 32 does not have any provision on revised offers to provide for unexpected changes of circumstances after the making of an offer. As a result, an offeror who wishes to revise his offer will have to make a new takeover or share buy-back offer and address the acceptances received under the old offer.

### Key provisions in the new CO

29. **Section 692** provides that a revision of the terms of a takeover offer is not regarded as the making of a fresh offer if the terms of the offer provide for the revision and the acceptances on the previous terms to be regarded as acceptances on the revised terms; and the revision is made in accordance with that provision. **Section 710** contains a similar provision in the case of a share buy-back offer.

### Introducing new provisions to allow an offeror in a takeover offer or share buy-back offer to apply to court for an authorisation to give squeeze out notices (Sections 693 and 712)

#### Position under Cap. 32

30. Under Cap. 32, there is no mechanism for an offeror to apply for a court order authorising the giving of squeeze out notices for those takeover or buy-back offers which failed to achieve the applicable threshold for giving of such notices because of untraceable shareholders related to the offer.

#### Position under the new CO

31. A mechanism for an offeror to apply to the court for authorisation to give squeeze out notices in the above situation is provided in the new CO. Such a mechanism has been adopted in the United Kingdom since 1987 and is considered to be practical and useful.

### Key provisions in the new CO

32. **Section 693(3) to (7)** provides for the mechanism which will apply if the offeror has been unable to trace the relevant shareholders after reasonable enquiry. The consideration offered must be fair and reasonable and the court may not make an order unless it considers that it is just and equitable to do so having regard, in particular, to the number of shareholders who have been traced but have not accepted the offer. **Section 712(4) to (8)** provide for a similar mechanism in the case of a share buy-back offer.

## TRANSITIONAL AND SAVING ARRANGEMENTS

33. Transitional and saving arrangements are set out in **sections 122 and 123 of Schedule 11** to the new CO and are basically as follows –

- Sections 166, 166A and 167 of Cap. 32 and rule 117 of the Companies (Winding-up) Rules continue to apply to an arrangement or compromise if an application was made to the Court for a meeting to be summoned before the commencement of Division 2 of Part 13.
- Section 168(1), (2) and (3) and the Ninth Schedule to Cap. 32 continue to apply to an acquisition offer made before the commencement of Division 4 of Part 13.

# Part 14

## Remedies for Protection of Companies' or Members' Interests

### INTRODUCTION

Part 14 (Remedies for Protection of Companies' or Members' Interests) of the new Companies Ordinance (Cap. 622) ("new CO") contains provisions relating to the remedies available for protection of companies' or members' interests. These include the unfair prejudice remedy, the statutory injunction order restraining conduct that constitutes contravention of the new CO, the statutory derivative action, and the right to seek a court order for inspection of company records.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. The provisions on shareholder remedies were substantially revised by the Companies (Amendment) Ordinance 2004 with a view to enhancing legal remedies available to members of a company. The amendments included –

- (a) providing for a statutory derivative action that may be taken on behalf of a company by a member of the company (subsequently extended to cover multiple derivative action through Companies (Amendment) Ordinance 2010);
- (b) facilitating members to exercise their rights to obtain access to company records;

- (c) empowering the court, on application by an affected person or the Financial Secretary, to grant an injunction restraining any person from engaging in conduct which constitutes contravention of the Companies Ordinance (Cap. 32) ("Cap. 32") or a breach of his fiduciary or other duties owed to a company; and
- (d) improving the unfair prejudice remedy in section 168A of Cap. 32 to provide the court with a power to award damages to the members of a company where it was found that their interests had been unfairly prejudiced and to award such interest on the damages as the court thinks fit. The scope of the remedy has also been extended to allow past members (and their personal representatives) of local companies and members and past members (and their personal representatives) of non-Hong Kong companies to commence legal action under that section.

3. Part 14 of the new CO mainly restates the existing provisions with improved drafting, while at the same time introduces the following initiatives that aim at fostering shareholder protection, namely –

- (a) extending the scope of the unfair prejudice remedy to cover proposed acts and omissions (paragraphs 5 to 6); and
- (b) enhancing the court's discretion in granting relief in cases of unfair prejudice (paragraphs 7 to 8).

There is also a new provision for an express power for the Chief Justice to make rules relating to unfair prejudice proceedings (paragraphs 9 to 10).

4. The details of the major changes in Part 14 are set out in paragraphs 5 to 10 below. The multiple derivative action provisions are restated in Part 14 (paragraphs 11 to 12).

### Extending the scope of the unfair prejudice remedy to cover proposed acts and omissions (Section 724)

#### Position under Cap. 32

5. Section 168A(1) of Cap. 32 provides that a member of a company may petition to the court if the affairs of the company are being or have been conducted in a manner unfairly prejudicial to the interests of the members generally or of some part of the members. There is some uncertainty whether, under the provisions of Cap. 32, a member can bring an action for unfair prejudice where a course of action is only at the proposal stage, or where there is only a threat to do or not to do something.

#### Position and key provisions under the new CO

6. The scope of the unfair prejudice remedy is extended to cover proposed acts and omissions. **Sections 723 to 726** restate the unfair prejudice remedy provisions under section 168A of Cap. 32. **Section 724(1)(b)** provides that the court may exercise the power to grant remedies under these provisions if there is any actual or proposed act or omission of the company

(including one done or made on behalf of the company) which is or would be prejudicial to the interests of the members. The remedies that may be granted by the court under **section 725** are therefore extended to cover an order restraining the proposed act or requiring the doing of an act that the company has proposed to omit to do.

### Enhancing the court's discretion in granting relief in cases of unfair prejudice (Section 725)

#### Position under Cap. 32

7. Section 168A(2) of Cap. 32 provides that orders made by the court (other than for payment of damages and interest) must be "with a view to bringing to an end the matters complained of". This prevents the court from granting a remedy which is unable to meet that requirement.

#### Position and key provision under the new CO

8. To enhance the court's discretion in granting relief in cases of unfair prejudice, **section 725** provides that the court may make any order that it thinks fit for giving relief in respect of the matter complained of.

### Providing for an express power for the Chief Justice to make rules (Section 727)

#### Position under Cap. 32

9. Under Cap. 32, the rules in the Companies (Winding-up) Rules made under section 296 apply to proceedings under section 168A in so far as they are applicable.

### Position and key provision under the new CO

10. **Section 727** of the new CO provides for an express power for the Chief Justice, subject to the approval of the Legislative Council, to make rules in relation to unfair prejudice proceedings. The Chief Justice has made the Companies (Unfair Prejudice Petitions) Proceedings Rules (Cap. 622L).

### **Allowing a member of an associated company to bring a statutory derivative action (section 732)**

#### Position under Cap. 32

11. Prior to the amendment brought about by Part 4 of the Companies (Amendment) Ordinance 2010, the statutory derivative action (“SDA”) provisions in Part IVAA of Cap. 32 only allow a member of a specified corporation to bring an action or intervene in proceedings on behalf of the corporation in respect of misfeasance committed against the corporation. The amendment allows a member of a related company to bring or to intervene in an action on behalf of the corporation, thus expanding the scope of the SDA provisions to cover multiple derivative actions. Sections 731 to 738 of the new CO basically restate the amended provisions.

#### Position and key provisions under the new CO

12. **Section 732** gives standing to members of associated companies to bring or intervene in proceedings on behalf of the corporation in respect of “misconduct” committed against the company. “Associated company” is defined in section 2(1) to mean a subsidiary or a holding company of a body corporate or a subsidiary of such a holding company. “Misconduct” is defined in **section 731** to mean fraud, negligence, breach of duty, or default in compliance with any Ordinance or rule of law.

## **TRANSITIONAL AND SAVING ARRANGEMENTS**

13. Transitional and saving arrangements are set out in **sections 124 to 127 of Schedule 11** to the new CO and are basically as follows –

- Section 168A of Cap. 32 and the Companies (Winding-up) Rules continue to apply to an unfair prejudice petition presented before the commencement of Division 2 of Part 14.
- Section 350B(1)(g) and (h) of Cap. 32 continue to apply to an application for injunction made before the commencement of Division 3 of Part 14.
- Part IVAA of Cap. 32 continues to apply to an application for statutory derivative action made and proceedings brought or intervened in before the commencement of Division 4 of Part 14.
- Sections 152FA to 152FE of Cap. 32 continue to apply to an application for an order for inspection of a company’s records and an inspection made before the commencement of Division 5 of Part 14.

# Part 15

## Dissolution by Striking Off or Deregistration

### INTRODUCTION

Part 15 (Dissolution by Striking Off or Deregistration) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions on striking off and deregistration of defunct companies, restoration of companies that have been struck off the Companies Register or deregistered by the Registrar of Companies (“the Registrar”), and related matters, including treatment of the properties of dissolved companies.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 15 contains initiatives that aim at facilitating business and improving regulation, namely –

- (a) extending the voluntary deregistration procedure to guarantee companies (paragraphs 4 to 6);
- (b) imposing additional conditions for deregistration of defunct companies (paragraphs 7 to 10);
- (c) introducing a new procedure of “administrative restoration” of a dissolved company by the Registrar (paragraphs 11 to 14); and

- (d) streamlining the procedures for restoration of dissolved companies by court order (paragraphs 15 to 16).

3. The details of the major changes in Part 15 are set out in paragraphs 4 to 16 below.

#### Extending the voluntary deregistration procedure to guarantee companies (Section 750)

Position under the Companies Ordinance (Cap. 32) (“Cap. 32”)

4. Under Cap. 32, only a private company may make application to the Registrar for deregistration under section 291AA, provided that certain conditions are met, namely –

- (a) the company has not commenced operation or business or has not been in operation or carried on business for three months;
- (b) it has no outstanding liabilities; and
- (c) all the members agree to the deregistration.

Under this voluntary deregistration procedure, a company can be dissolved without going through the winding-up process.

5. Non-private companies and certain categories of business<sup>1</sup> are not allowed to apply for voluntary deregistration to avoid prejudicing the public interest. There has been a suggestion that non-private companies, particularly guarantee companies which are social or community organisations, should be allowed to deregister voluntarily if they satisfy the above conditions. It would be costly for them to commence a members' voluntary winding-up instead.

#### Position under the new CO and key provisions

6. The deregistration procedure is extended to guarantee companies. Public companies and certain categories of businesses<sup>2</sup> will continue to be excluded (**section 749**). The conditions for applying for voluntary deregistration (**section 750(2)**), particularly the requirement of agreement by all members would prevent any possible abuse of the procedure (see also paragraphs 8 and 9 below).

#### **Imposing additional conditions for voluntary deregistration of defunct companies (Sections 750 to 751)**

#### Position under Cap. 32

7. Under Cap. 32, a company only needs to satisfy the three conditions as set out in paragraph 4 above in applying for voluntary deregistration. However, there have been cases

where some companies applying for deregistration were parties to legal proceedings or were in possession of immovable property in Hong Kong or being holding companies owning subsidiaries' assets which consist of immovable property in Hong Kong with high maintenance costs or encumbrances attached. As a consequence, deregistration proved to have adverse impact on third parties or the Government (as the immovable property would be vested in the Government as bona vacantia following dissolution of the company under section 292 of Cap. 32).

#### Position under the new CO and key provisions

8. Additional conditions have been imposed on companies applying for deregistration so as to prevent any potential abuse of the deregistration procedure, such as where a company applying for deregistration is a party to legal proceedings or is in possession of immovable property in Hong Kong.

9. **Sections 750 to 751** mainly restate the existing deregistration provisions under Cap. 32 with three additional conditions for deregistration: firstly, the applicant must confirm that the company is not a party to any legal proceedings; secondly, it has no immovable property in Hong Kong and thirdly, if the company is a holding company, none of its subsidiaries' assets consist of any immovable property in Hong Kong (**section 750(2)(d), (e) and (f)**).

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<sup>1</sup> These include –

- (a) an authorized institution as defined in the Banking Ordinance (Cap. 155);
- (b) an insurer as defined in the Insurance Companies Ordinance (Cap. 41);
- (c) a corporation licensed under Part V of the Securities and Futures Ordinance (Cap. 571) to carry on a business in any regulated activity within the meaning of Schedule 5 to that Ordinance and an associated entity of the corporation within the meaning of Part VI of that Ordinance;
- (d) an approved trustee as defined in the Mandatory Provident Fund Schemes Ordinance (Cap. 485);
- (e) a company having a subsidiary that falls within any of the categories specified above;
- (f) a company that has fallen within any of the categories specified above at any time during the preceding 5 years.

<sup>2</sup> The categories of businesses are the same as in Cap. 32 (see footnote 1), with the addition of trust companies under Part VIII of the Trustee Ordinance (Cap. 29) and their holding companies.

10. Any person who knowingly or recklessly gives false or misleading information in a material particular to the Registrar in an application commits an offence. The person is liable on conviction on indictment to a fine of \$300,000 and to imprisonment for 2 years or on summary conviction to a fine at level 6 and to imprisonment for 6 months (**section 750(6)**).

### Introducing a new procedure of “administrative restoration” of a dissolved company by the Registrar (Sections 760 to 762)

#### Position under Cap. 32

11. Pursuant to Cap. 32, where the Registrar has reasonable cause to believe that a company is not carrying on business or in operation, she may adopt the procedure set out in section 291 and strike the name of the company off from the register. Under section 291(4), the procedure may also be used where a company is being wound up and the Registrar has reasonable cause to believe either that no liquidator is acting or that the affairs of the company are fully wound up, and the returns required to be made by the liquidator (under sections 239 and 248 of Cap. 32) have not been made for a period of six consecutive months. Under section 291(7), the company, a member or creditor may apply to the court before the expiration of 20 years from dissolution for the company to be restored.

12. There have been some cases where a company which has been struck off seeks to be restored on the ground that, contrary to the Registrar’s belief, it was actually in operation or carrying on business at the time of striking off.

This may occur because a company fails to file its annual returns, moves without notifying the Companies Registry of a change of registered office address and is unaware of the proposed strike-off despite that relevant notice has been published in the Gazette prior to the striking off action. Whilst restoration is often straightforward in such circumstances as it is unlikely to be contested, it still requires an application to the court.

#### Position under the new CO and key provisions

13. The new CO introduces a simplified restoration procedure to allow companies to be restored to the register in straightforward cases without the need for recourse to the Court. **Sections 760 to 762** enable the Registrar to restore a company which has been struck off under **section 746 or 747** (where it appears that the company is not in operation or carrying on business or, in the case of a company being wound up but with outstanding matters unattended to). The Registrar may, on an application by a director or member of a company, restore such a company. Three conditions must be met –

- (a) the company must be in operation or carrying on business at the time its name was struck off;
- (b) if the company has any immovable property situated in Hong Kong which has become vested in the Government as bona vacantia, the Government has no objection to the restoration; and
- (c) the applicant must bring up to date the company’s records kept by the Registrar.

14. The above administrative restoration procedure does not apply to companies which were deregistered upon applications to the Registrar under **section 751** (or section 291AA of Cap. 32). For those cases, application for restoration should be made to the court under **sections 765 to 766**.

### **Streamlining the procedures for restoration of dissolved companies by court order (Sections 765 to 767)**

#### Position under Cap. 32

15. There are two routes available for companies which have been struck off or deregistered pursuant to Cap. 32 to be restored or reinstated to the register by application to the court. They are respectively under sections 291(7) and 291AB(2) and are very similar in nature.

#### Position under the new CO and key provisions

16. The two existing procedures are merged into one for simplicity. **Sections 765 to 767** provide for a restoration procedure by court order. Where a company has been struck off the register by the Registrar or deregistered upon its own application, and thereby dissolved, any director or member or creditor of the company or any interested person, including the Government, may make an application to the court for restoration of the company.

## **TRANSITIONAL AND SAVING ARRANGEMENTS**

17. Transitional and saving arrangements are set out in **sections 128 to 131 of Schedule 11** to the new CO. The following provisions of Cap. 32, as in force immediately before their repeal, continue to apply in respect of a matter provided for in the provisions –

- Sections 290C and 290D – Disclaimer of property vested in Government;
- Sections 291(2), (3) and (6), 291A and 291AA – Striking off and deregistration of a company;
- Sections 291(7), 291A(2) and 291AB – Application for restoration of a dissolved company; and
- Section 292(2) – Effect of court order for restoration or reinstatement on bona vacantia.

# Part 16

## Non-Hong Kong Companies

### INTRODUCTION

Part 16 (Non-Hong Kong Companies) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to non-Hong Kong companies, i.e. companies incorporated outside Hong Kong that have established a place of business in Hong Kong.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 16 essentially restates Part XI of the Companies Ordinance (Cap. 32) (“Cap. 32”) which had been substantially amended by the Companies (Amendment) Ordinance 2004 mainly with a view to simplifying the filing requirements. In Part 16, there are no substantive changes to the registration regime of non-Hong Kong companies under Cap. 32. However, some clarification and modification of the regime are made, which aim at improving regulation and modernising the law, namely –

- (a) Clarifying provisions on changes of corporate names of non-Hong Kong companies (paragraphs 5 to 6);
- (b) Clarifying provisions for striking the name of a non-Hong Kong company off the Companies Register and restoration of the company to the Companies Register (paragraphs 7 to 9);
- (c) Moving certain procedural details to subsidiary legislation (paragraphs 10 to 11); and

- (d) Modifying the penalty provisions to align with those of Hong Kong incorporated companies (paragraphs 12 to 13).

3. Apart from the above changes, Part 16 also provides for a company to appeal to the Administrative Appeals Board, instead of to the court, against a notice issued by the Registrar of Companies (“the Registrar”) concerning the company’s name (paragraphs 14 to 15 below). This change was suggested by Members of the Bills Committee on the Companies (Amendment) Bill 2010.

4. The details of the above major changes are set out in paragraphs 5 to 15 below.

#### Clarifying provisions on changes of corporate names of non-Hong Kong companies (Sections 778 to 779)

##### Position under Cap. 32

5. Section 335(2) of Cap. 32 requires a non-Hong Kong company to notify the Registrar of any change of its corporate name. The provision is fairly general. There may be uncertainty as to whether notification is required in certain scenarios, such as where there is a change to the registered name of the company in its place of incorporation without a change in the translation appearing on the register which is being used as the company’s corporate name in Hong Kong.

### Position and key provisions in the new CO

6. **Section 778** clarifies the notification requirements in various scenarios relating to the changes of corporate names of non-Hong Kong companies. **Section 779** clarifies the registration procedures for change of corporate name.

### **Clarifying provisions for striking the name of a non-Hong Kong company off the Companies Register and restoration of the company to the Companies Register (Sections 796 to 801)**

#### Position under Cap. 32

7. Section 339A of Cap. 32 empowers the Registrar to remove the name of a non-Hong Kong company from the register if there is reasonable cause to believe that the company has ceased to have a place of business in Hong Kong, by applying the provisions relating to the striking off of local defunct companies in Cap. 32, with such adaptations as are necessary. Such a legislative provision by way of reference is considered unsatisfactory and may give rise to uncertainty as to which provisions would apply.

#### Position and key provisions in the new CO

8. To avoid the uncertainty in the application of a legislative provision by way of reference, express provisions are introduced in Part 16 to clarify the matters.

9. Division 8 of Part 16 comprising **sections 796 to 801** expressly sets out the steps that the Registrar should take before striking the name of a non-Hong Kong company off the Companies Register, the procedures for a director or member of a non-Hong Kong company that has been struck off to apply to the Registrar for its restoration to the Companies Register, and the conditions for granting such an application.

### **Moving certain procedural details to subsidiary legislation (Section 805)**

#### Position under Cap. 32

10. The procedural and technical details concerning the registration of and returns to be made by non-Hong Kong companies are set out in sections 333, 334 and 335 of Cap. 32. These include the particulars to be contained in the applications or returns and the accompanying documents. Such procedural and technical details are likely to require updating over time.

#### Position and key provisions in the new CO

11. To facilitate future updating, the requirements for procedural and technical details have been moved from primary into subsidiary legislation. **Section 805** empowers the Financial Secretary to make regulations to prescribe certain procedural and technical details. The details are set out in the Companies (Non-Hong Kong Companies) Regulation (Cap. 622J). These details include, among others –

- (a) the particulars to be contained in applications for registration of non-Hong Kong companies and the documents to accompany such applications;
- (b) the particulars to be contained in annual returns or returns of change of certain particulars by registered non-Hong Kong companies and the documents to accompany such returns; and
- (c) the documents to accompany a notice of the termination of the authorization of an authorized representative by a registered non-Hong Kong company to the Registrar.

## Modifying the penalty provisions to align with those of Hong Kong incorporated companies

### Position under Cap. 32

12. Section 340 of Cap. 32 imposes liability with a uniform level of penalty on a non-Hong Kong company that is in default of any provisions under Part XI as well as every officer or agent of that company who authorizes or permits the default. Under the Twelfth Schedule to Cap. 32, a fine of up to \$50,000 (level 5) may be imposed summarily upon any of these persons for any offence under Part XI and a daily default fine of \$700 may also be imposed for any continuing default. The imposition of a uniform level of penalty for different types of offences is considered unsatisfactory. It would also result in an offence of similar nature being subject to different penalty levels, depending on whether the company is a locally incorporated or a non-Hong Kong company.

### Position and key provisions in the new CO

13. In the new CO, the offence provisions are set out in individual sections of Part 16. The penalty levels are generally aligned with comparable offence provisions for Hong Kong incorporated companies. Following the offence provisions for Hong Kong incorporated companies, “every officer of the company who authorizes or permits the default” is replaced by “responsible person” which is defined in **section 3** of the new CO to mean an officer of the non-Hong Kong company who authorizes or permits, or participates in the contravention.

## Allowing a company to appeal to the Administrative Appeals Board instead of to the court (Section 784)

### Position under Cap. 32

14. Under Cap. 32, where the Registrar is satisfied that the name of a non-Hong Kong company gives so misleading an indication of

the nature of its activities in Hong Kong as to be likely to do harm to the public, the Registrar may issue a notice to the company pursuant to section 337B(1). The company cannot carry on business under that name two months after the notice is served, unless the company applies to the court to set aside the notice.

### Position and key provisions in the new CO

15. At the meeting of the Bills Committee on the Companies (Amendment) Bill 2010, Members suggested that a company should be allowed to appeal to the Administrative Appeals Board, instead of to the court, against a change-of-name direction / notice issued by the Registrar in view of the cost and time involved in court proceedings. The suggestion was agreed and, for non-Hong Kong companies, the relevant changes have been incorporated in **section 784**.

## TRANSITIONAL AND SAVING ARRANGEMENTS

16. The transitional provisions are set out in detail in **sections 132 to 140 of Schedule 11** to the new CO. The position relating to pending applications for registration and registration of returns is that they are regarded as applications made under the new CO but fees will be paid by reference to the Eighth Schedule to Cap. 32. In most other cases, the general position is that where the action was commenced under Cap. 32, the provisions of Cap. 32 will continue to apply, for example, service of notice regarding cessation of a place of business, notice of dissolution, striking the name of a non-Hong Kong company off the register and restoration of company to the register.

# Part 17

## Companies not Formed, but Registrable, under this Ordinance

### INTRODUCTION

Part 17 (Companies not Formed, but Registrable, under this Ordinance) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions relating to companies not formed under the new Ordinance or a former Companies Ordinance but eligible to be registered under the new CO.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. There is no significant change to the Companies Ordinance (Cap. 32) (“Cap. 32”) introduced under Part 17. Part 17 mainly restates, with some modifications, Part IX of Cap. 32<sup>1</sup>, which provides for the registration of companies which are/have been formed in pursuance of any Ordinance other than Cap. 32 or a former Companies Ordinance. The sequence of the provisions in Part IX of Cap. 32 is re-arranged in a more logical and user-friendly order. The archaic provisions on “joint stock company” under sections 310 to 312 of Cap. 32 have been removed. Further details are set out in paragraphs 3 to 5.

### Removing archaic provisions on “joint stock company”

#### Position under Cap. 32

3. Under section 310 of Cap. 32, a joint stock company with limited liability, formed pursuant to any Ordinance (other than Cap. 32 or any of its predecessors), or letters patent, or being otherwise duly constituted according to law, and consisting of one or more members, may register under Cap. 32 as a company limited by shares. Section 311 sets out the definition of a joint stock company while section 312 sets out the requirements for registration by such a company.

4. Sections 310 to 312 of Cap. 32 originated from the United Kingdom (“UK”) Companies (Consolidation) Act 1908, which allowed joint stock companies formed under the earlier UK Joint Stock Companies Acts of 1844 and 1856 to register as a company under the subsequent UK Companies Acts. The UK Joint Stock Companies Acts did not apply in Hong Kong, and there was no equivalent legislation in Hong Kong. As far as we can ascertain, currently there is no incorporated joint stock company in Hong Kong. The chance of unincorporated joint stock companies being in existence is very remote. If there had been any such companies in existence which wished to register under Cap. 32, they would have done so by now.

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<sup>1</sup> Except sections 324 and 325 which will remain in the Companies (Winding Up and Miscellaneous Provisions) Ordinance as they are closely related to the winding-up provisions.

### Position under the new CO

5. On the basis of the above, and for the sake of simplicity, the detailed provisions on registration of joint stock companies are repealed. If, despite the remote possibility, there were still in existence any unincorporated joint stock companies, they could simply dissolve the companies and incorporate new ones if they wish to become companies under the new CO.

### Key Provisions in the new CO

6. **Section 807** provides that an eligible company may be registered as an unlimited company or a company limited by guarantee. The expression “eligible company” is defined in section 806 as a company formed after 1 May 1865 in pursuance of an Ordinance other than the new CO or a former CO, or otherwise constituted after that date according to law.

7. **Sections 808 to 810** set out the requirements and restrictions regarding registration. **Section 808** makes it clear that a company whose members’ liability is limited by an Ordinance or otherwise according to law will not be registered under this Part.

8. An eligible company is regarded as having been incorporated under the new CO as an unlimited company or a company limited by guarantee (as the case may be) upon registration. Registration does not operate to create a new legal entity for the eligible company nor does it affect its property or its rights and liabilities in respect of any debt or obligation incurred by or on behalf of the company before registration (**section 814**). Any action or other legal proceedings by or against the eligible company or any of its officers or members that are pending at the time of registration may be continued in the same manner as if the registration had not taken place (**section 815**).

## TRANSITIONAL AND SAVING ARRANGEMENTS

9. A pending application for registration under section 310 of Cap. 32 is regarded as an application for registration under the new CO. If the applicant is not registered as a limited company or is registered as a limited company, but the liability of the shareholders was limited by some other Ordinance before registration, no registration fee is payable (**section 141 of Schedule 11**).

# Part 18

## Communications to and by Companies

### INTRODUCTION

Part 18 (Communications to and by Companies) of the new Companies Ordinance (Cap. 622) (“new CO”) relates to communications in electronic or hard copy form between a company and its members, debenture holders, and other persons. It also deals with communications sent by a company to its members and debenture holders by means of a website.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 18 aims at facilitating business by setting out the rules governing communications to and from companies in electronic form and hard copy form. New rules have been introduced governing communications to companies in electronic form and in hard copy form (paragraphs 4 to 5 below). Regarding the communications by a company to another person other than the Registrar of Companies (“the Registrar”), this Part restates Part IVAAA of the Companies Ordinance (Cap. 32) (“Cap. 32”) which was introduced through the Companies (Amendment) Ordinance 2010, covering communications in hard copy form, electronic form and by means of website (paragraphs 6 to 8 below).

3. Apart from the above, **section 826** provides that for documents or information to be sent or supplied to the Registrar, Part 18 has effect subject to Part 2. **Section 827** preserves the Cap. 32 provisions that, for a document that is issued for the purpose of any legal proceedings, it may be served on a company by sending it by post to or leaving it at the company’s registered office.

### KEY PROVISIONS IN THE NEW CO

#### Communications to a company in electronic form (Section 828)

4. **Sections 828 to 830** contain provisions dealing with communication from a natural person to a company which are modeled on the provisions in United Kingdom Companies Act 2006. **Section 828** provides that a document may be sent to a company in electronic form if the company has so agreed, generally or specially, or is regarded as having so agreed under a provision of the new CO. A company may revoke its agreement by giving a notice of revocation. The minimum period of the notice must be no less than 7 days or such longer period as specified in the company’s articles of association (for members), the instrument creating the debenture (for debenture holders) or any other agreement (for other persons), as appropriate. A document is deemed to have been received by the company 48 hours after it has been sent by electronic means, or otherwise any period as specified in the company’s articles (for members), the instrument creating the debenture (for debenture holders) or any other agreement (for other persons), as appropriate and unless the contrary is proved. A document sent in electronic form may also be sent by hand or by post.

#### Communications to a company in hard copy form (Section 829)

5. **Section 829** provides that if the document or information is sent or supplied by post to a company by a natural person, it is deemed to have been received by the company on the second business day after posting or otherwise as specified in the company’s articles of association (for

members) or instrument creating the debenture (for debenture holders), or any other agreement (for other persons), whichever is the later and unless the contrary is proved. If the document is sent by hand, it is deemed to have been received by the company when the document is delivered.

### Communications by a company to another person (Sections 831 to 837)

6. Division 4 of Part 18 restates the existing Part IVAAA of Cap. 32. In particular, **section 833** restates that a company may communicate with its members, debenture holders and other persons by means of a website, if so permitted by its articles or a members' resolution and if the recipient consents to the use of website communications. If the persons are members or debenture holders, they will be taken to have agreed to receive information from the company via a website if they have been asked individually for their acceptance and have not responded within 28 days of the company's request, unless it is proved that the person has not received the request. Companies are required to notify intended recipients each time any material is published on a website. The document or information should be available on the website throughout the period specified by the applicable provisions of the new CO or the Companies (Winding Up and Miscellaneous Provisions) Ordinance, or where no such period is specified, a period of 28 days.

7. **Section 833(10)** provides an exemption to relieve a company from notifying or seeking agreement from the other person for communication by means of website if communication in hard copy form has been returned by the post office as undeliverable at

that other person's last known address and sending information by other electronic means is not possible.

8. **Section 833(12)(b)** provides that a document is deemed to have been received by the intended recipient 48 hours after the document is first made available on the website or after receipt of the notice of the available date (whichever is the later). The 48 hours is subject to any period specified in the company's articles (for members), the instrument creating the debenture (for debenture holders) or any other agreement (for other persons), as appropriate.

## ACTIONS TO BE TAKEN BY STAKEHOLDERS

9. Existing companies may wish to amend their articles, instruments creating debentures or any other agreements, as appropriate, to make provisions for the following matters –

- Period specified deeming receipt of document or information in electronic form or by means of website. If the articles, instrument or agreement do/does not specify the period, the period is 48 hours (**section 823(5)** of the new CO).
- Manner of sending documents or information to joint holders of shares or debentures (**section 835** of the new CO).
- Manner of sending document or information where a holder of shares is dead or bankrupt (**section 836** of the new CO).

# Part 19

## Investigations and Enquiries

### INTRODUCTION

Part 19 (Investigations and Enquiries) of the new Companies Ordinance (Cap. 622) (“new CO”) contains provisions that deal with investigations and enquiries into a company’s affairs.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. Part 19 mainly reorganises the provisions<sup>1</sup> in the Companies Ordinance (Cap. 32) (“Cap. 32”) relating to the appointment of an inspector by the Financial Secretary (“FS”) to investigate the affairs of a company; and the power of the FS (or someone authorised by him) to inspect books and papers of a company, which will be rephrased in the new CO as a power to “enquire into a company’s affairs” to better describe the nature of the power (“the enquiry power”).

3. It is noteworthy that many of the previous investigations undertaken by inspectors involved listed companies or their related companies. The last appointment of an inspector was made in 1999, while the power to inspect books and papers (i.e. the “enquiry power” in the new CO) has never been invoked. The absence of investigation by inspectors since 1999 is mainly due to developments in the regulatory framework

for listed companies, namely, (a) the coming into operation of the Securities and Futures Ordinance (Cap. 571) (“SFO”) in April 2003 which empowered the Securities and Futures Commission with greater authority to investigate into market misconduct involving listed companies; and (b) the establishment of the Financial Reporting Council in 2006 which conducts independent investigations of possible auditing and reporting irregularities in relation to listed companies.

4. Notwithstanding the above, the possibility of the FS using the investigatory and enquiry powers in future cases where there are sufficient grounds to do so cannot not be ruled out. Therefore, the provisions are retained in the new CO as “reserve” or “last resort” powers as a supplement to the powers contained in other Ordinances, including the SFO and the Financial Reporting Council Ordinance (Cap. 588) (“FRCO”).

5. Part 19 also introduces modifications to the provisions in Cap. 32 concerning these “reserve” or “last resort” powers by making reference to similar provisions on investigations under the SFO and FRCO, which are more up-to-date. These modifications aim at ensuring better regulation by –

- (a) Enhancing the investigatory powers of an inspector (paragraphs 7 to 8);

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<sup>1</sup> Sections 142 to 152F of Cap. 32.

- (b) Providing better safeguards for confidentiality of information and protection of informers (paragraphs 9 to 11); and
  - (c) Providing a new power for the Registrar of Companies (“the Registrar”) to obtain documents or information for ascertaining whether any conduct that would constitute certain offences under the new CO has taken place (paragraphs 12 to 13).
6. Details of the above proposals in Part 19 are set out in paragraphs 7 to 13.

### Enhancing the investigatory powers of an inspector (Sections 846 to 850)

#### Position under Cap. 32

7. Sections 142 to 151 of Cap. 32 deal with investigations of a company’s affairs by independent inspectors appointed by the FS. The FS may appoint an inspector on application by the members (100 members or members holding not less than 10% of the shares issued) or a company by special resolution or on his own initiative where there is fraud or mismanagement involved. The FS must appoint an inspector upon an order

made by the court. The inspector is vested with a range of investigatory powers. At the end of the investigation the inspector is required to make a report to the FS.

#### Position and key provisions in the new CO

8. **Sections 846 to 850** of the new CO set out the inspector’s powers. New powers are given to the inspector, for example to require a person to preserve records or documents before production to the inspector (**section 846(1)(b)**), and to require a person to verify by statutory declaration any answer or explanation given to the inspector (**section 848(2)**). Criminal sanctions are introduced for non-compliance with a request made by an inspector (**section 863**). **Section 864** introduces an express provision to allow the court to order compliance with a request made by an inspector, not just to punish for the non-compliance. These powers are necessary and incidental to the proper conduct of an investigation by the inspector and will not change the nature of the investigations. The powers under **sections 848<sup>2</sup>, 863<sup>3</sup> and 864<sup>4</sup>** are based on similar powers found in the SFO and FRCO.

<sup>2</sup> Sections 183(2) and (3) of the SFO; Sections 28(3) and (4) of the FRCO.

<sup>3</sup> Sections 184(1) to (4) of the SFO; Section 31 of the FRCO.

<sup>4</sup> Section 185(1)(a) of the SFO; Section 32(2)(a) of the FRCO.

## Providing better safeguards for confidentiality of information and protection of informers (Sections 880 to 885)

### Position under Cap. 32

9. Cap. 32<sup>5</sup> provides for secrecy of information in respect of documents relating to a company obtained under the provisions relating to inspection of companies' books and papers in an enquiry, or seized by search warrant, but there are no confidentiality or "statutory gateway" provisions concerning information obtained by an inspector in an investigation, nor is there any provision dealing with the protection of an informer's identity.

### Position and key provisions in the new CO

10. **Sections 880 to 882** contain confidentiality provisions relating to information obtained in both investigations of a company's affairs by an inspector under the provisions set out in Division 2 of Part 19, and enquiry into a company's affairs by the FS under the provisions set out in Division 3. **Section 880** imposes a statutory

obligation to preserve secrecy and **section 881** defines expressly how such information may be disclosed to other regulatory authorities through the introduction of a statutory regime similar to the provisions in the SFO<sup>6</sup>, FRCO<sup>7</sup> and the Banking Ordinance (Cap. 155)<sup>8</sup>. **Section 882** creates an offence for breach of the secrecy provisions.

11. Provisions to encourage persons to volunteer information to facilitate investigations and enquiries are included in the new CO. **Section 884**<sup>9</sup> introduces provisions to provide protection (by granting immunity from liability for disclosure) to persons who volunteered information to facilitate an investigation of a company's affairs or enquiry into a company's affairs. **Section 885**<sup>10</sup> gives additional protection by expressly stating that the identity of an informer should be kept anonymous in civil, criminal or tribunal proceedings. These sections are also applicable to the new power for the Registrar to obtain documents, records and information (see paragraph 12 below).

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<sup>5</sup> Section 152C of Cap. 32.

<sup>6</sup> Section 378 of the SFO.

<sup>7</sup> Section 51 of the FRCO.

<sup>8</sup> Section 120 of the Banking Ordinance.

<sup>9</sup> Section 884 of the new CO is based on section 448A of the UKCA 2006.

<sup>10</sup> Section 885 of the new CO is based on section 52 of the FRCO.

Providing a new power for the Registrar to obtain documents or information for ascertaining whether any conduct that would constitute certain offences under the new CO has taken place (Sections 873 to 876)

#### Position and key provisions in the new CO

12. **Section 873** gives the Registrar a new power to require production of records or documents, to make copies of the records or documents and to require information or explanations in respect of the records or documents, for the purposes of ascertaining whether any conduct that would constitute an offence under **section 750(6)** or **section 895(1)** relating to the giving of false or misleading information in documents delivered to the Registrar has taken place. **Section 875** provides criminal sanctions for non-compliance with the Registrar's request.

13. This new power will help safeguard the integrity of the companies register and the quality of information disclosed to the public and will strengthen enforcement, thus ensuring better regulation.

## TRANSITIONAL AND SAVING ARRANGEMENTS

14. The major changes described in these Highlights apply to activities carried out after the commencement date of the new CO. For activities started pursuant to the provisions under Cap. 32 and in progress when the new CO commences, Cap. 32 provisions will continue to apply (**sections 142 to 148 of Schedule 11** to the new CO).

# Part 20

## Miscellaneous

### INTRODUCTION

Part 20 (Miscellaneous) of the new Companies Ordinance (Cap. 622) (“new CO”) contains miscellaneous provisions that mainly re-enact provisions in the Companies Ordinance (Cap. 32) (“Cap. 32”) that may be classified into the following categories –

- (a) miscellaneous offences, namely the offences for false statements and for improper use of “Limited” or “有限公司” etc., based on sections 349<sup>1</sup> and 350<sup>2</sup> of Cap. 32 respectively;
- (b) miscellaneous provisions relating to investigation or enforcement measures, including provisions mirroring sections 306<sup>3</sup>, 351A<sup>4</sup>, 351B<sup>5</sup> and 352<sup>6</sup> of Cap. 32, and a new power for the Registrar of Companies (“the Registrar”) to compound specified offences under the new CO;
- (c) miscellaneous provisions relating to misconduct by an officer or auditor of a company derived from section 358<sup>7</sup> of Cap. 32; and
- (d) other miscellaneous provisions, such as those modelled on sections 49Q(3)(b) and (c)<sup>8</sup>, 354<sup>9</sup>, 355<sup>10</sup>, 357<sup>11</sup>, 359A<sup>12</sup> and 360<sup>13</sup> of Cap. 32, and provisions that deal with paperless holding and transfer of shares and debentures<sup>14</sup>.

### POLICY OBJECTIVES AND MAJOR CHANGES

2. The new initiatives under this Part aim at improving the regulatory regime and removing the anomaly relating to security for costs under Cap. 32, namely –

- (a) Redefining the scope of the offence for making false statements (paragraphs 4 to 5);

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<sup>1</sup> Section 349 of Cap. 32: “Penalty for false statements”.

<sup>2</sup> Section 350 of Cap. 32: “Penalty for improper use of “Limited”, “Corporation” or “Incorporated””.

<sup>3</sup> Section 306 of Cap. 32: “Enforcement of duties under Ordinance by court order”.

<sup>4</sup> Section 351A of Cap. 32: “Limitation on commencement of proceedings”.

<sup>5</sup> Section 351B of Cap. 32: “Production and inspection of books where offence suspected”.

<sup>6</sup> Section 352 of Cap. 32: “Application of fines”.

<sup>7</sup> Section 358 of Cap. 32: “Power of court to grant relief in certain cases”.

<sup>8</sup> Section 49Q of Cap. 32: “Power for Chief Executive in Council to modify certain sections”.

<sup>9</sup> Section 354 of Cap. 32: “Saving as to private prosecutors”.

<sup>10</sup> Section 355 of Cap. 32: “Saving for privileged communications”.

<sup>11</sup> Section 357 of Cap. 32: “Costs in actions by certain limited companies”.

<sup>12</sup> Section 359A of Cap. 32: “Power to make regulations”.

<sup>13</sup> Section 360 of Cap. 32: “Power to amend requirements as to accounts, Schedules, tables, forms and fees”.

<sup>14</sup> Section 908 of the new CO and Schedule 8. The provisions in Schedule 8 have been incorporated into Cap. 32 after enactment of the Companies (Amendment) Ordinance 2010. Implementation of the provisions would be subject to the enactment of an ordinance for a scripless securities market, the legislative exercise for which is under preparation.

- (b) Empowering the Registrar to compound specified offences (paragraphs 6 to 16); and
  - (c) Widening the categories of companies in respect of which the court may require security for costs in civil actions (paragraphs 17 to 21).
3. The details of the above changes in Part 20 are set out in paragraphs 4 to 21 below.

### Redefining the scope of the offence for making false statements (Section 895)

#### Position under Cap. 32

4. Section 349 of Cap. 32 provides for a criminal offence where any person wilfully makes a statement to the Registrar which is false in any material particular, knowing it to be false. The requisite mental element of the offence requires proof of knowledge and wilful intent and does not cover the making of a misleading statement or making of false statements recklessly.

#### Position and key provisions in the new CO

5. **Section 895** provides for the matters covered by section 349 of Cap. 32 subject to the modifications that the offence is extended to cover “a statement that is misleading, false or deceptive in any material particular” and that the mental element covers acts committed “knowingly or recklessly”.

### Empowering the Registrar to compound specified offences (Section 899)

#### Position under Cap. 32

6. The Registrar has implemented a range of administrative measures to encourage due compliance with the filing obligations under Cap. 32 in addition to prosecution for non-compliance<sup>15</sup>. There is no power to compound offences under Cap. 32.

#### Position under the new CO

7. To further expand the repertoire of measures to encourage due compliance with filing obligations and to optimise the use of judicial resources, the new CO introduces a new power for the Registrar to compound, at her discretion, specified offences as set out in Schedule 7 to the new CO.

8. In compounding an offence, the Registrar will give a notice to a company in breach to offer it an opportunity to rectify the default by paying an amount of HK\$600 to the Registrar as a compounding fee and remedying the breach constituting the offence within a specified period. If the company accepts and complies with the terms of the notice, no prosecution will be initiated against it for that offence.

<sup>15</sup> These include publication of various information pamphlets, posters and external circulars to provide general guidelines on compliance. While information pamphlets are distributed to company promoters on incorporation or registration of companies, posters on compliance are placed in the public areas of the Companies Registry. In addition, companies may also subscribe to an Annual Return e-Reminder / e-Alert Service to receive electronic notifications on the filing of annual returns.

9. The general principles for determining which offences should be compoundable offences were developed by an expert working group and agreed by the Standing Committee on Company Law Reform.

10. In accordance with these principles, the compound offer regime will apply to straightforward, minor regulatory offences committed by companies that are easily detectable by the Registrar from objective reliable evidence. Schedule 7 to the new CO sets out the offences identified as appropriate for compounding. These are failure to deliver directors' written consents to act to the Registrar<sup>16</sup>, failure to engrave name on a company's common seal<sup>17</sup>, improper use of the common seal<sup>18</sup>, failure to file annual returns<sup>19</sup> and failure to deliver accounts<sup>20</sup>.

11. Some other minor regulatory offences included in subsidiary legislation have also been included in Schedule 7<sup>21</sup>. These are offences

for failure to display continuously the company's registered name<sup>22</sup> at the registered office and business venue, failure to disclose the company's registered name, etc. in its communication documents, transaction instruments and on any of its websites<sup>23</sup>. Additionally, similar offences for registered non-Hong Kong companies which are set out in the new CO have also been included<sup>24</sup>.

#### Key provisions in the new CO

12. **Section 899** gives the Registrar a new power to compound specified offences under the new CO.

13. **Section 899(1)** provides that the Registrar may, if she has reason to believe that a person has committed an offence specified in **Schedule 7**, give the person a notice in writing which –

- (a) states that the Registrar has reason to believe that the person has committed the offence and setting out the particulars of the offence;

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<sup>16</sup> Section 74(2) of the new CO.

<sup>17</sup> Section 124(3) of the new CO: offence by a Hong Kong company for failure to produce its common seal in metallic form and to engrave name on the seal.

<sup>18</sup> Section 124(4) of the new CO: offence by officers of Hong Kong companies for improper use of the common seal.

<sup>19</sup> Section 662(6) of the new CO: failure to file annual returns by Hong Kong companies within the prescribed time; and section 788(3) of the new CO: failure to file annual returns by registered non-Hong Kong companies within the prescribed time.

<sup>20</sup> Section 789(3) of the new CO: failure to deliver accounts by registered non-Hong Kong companies.

<sup>21</sup> Section 911 of the new CO provides that the Financial Secretary may by notice published in the Gazette amend Schedule 7. A notice amending the Schedule was published in the Gazette on 25 October 2013.

<sup>22</sup> Section 7(1) of the Companies (Disclosure of Company Name and Liability Status) Regulation (Cap. 622B) in respect of section 3(1) of the Regulation.

<sup>23</sup> Section 7(1) of the Companies (Disclosure of Company Name and Liability Status) Regulation (Cap. 622B) in respect of section 4 of the Regulation.

<sup>24</sup> Section 792(6) of the new CO re section 792(1) and (2). This was added to Schedule 7 at the same time as the offences applicable to local companies were added.

- (b) sets out the conditions upon which no proceedings will be instituted against the person in respect of the offence, including the amount of compounding fee to be paid and the period within which the conditions have to be complied with; and
- (c) requests any other information that the Registrar thinks fit.

14. **Section 899(2)** states that the notice may be given only before the proceedings on the offence commence. **Section 899(3)** empowers the Registrar, by a further written notice, to extend the period within which the conditions as specified in the notice issued have to be complied with<sup>25</sup>. **Section 899(4)** provides that the notice under **section 899(1)** may not be withdrawn during the period specified in the notice or the extended period.

15. **Section 899(7)** clarifies that the payment of the compounding fee specified in the notice is not to be taken as an admission by the person of any liability for the offence alleged in the notice to have been committed by that person.

16. The specified offences that are compoundable are set out in **Schedule 7** (see paragraphs 10 and 11 above). **Section 911(1)** provides that the Financial Secretary may amend the Schedule by notice published in the Gazette.

## Widening the categories of companies in respect of which the court may require security for costs in civil actions (Section 905)

### Position under Cap. 32

17. Section 357 of Cap. 32 provides that where a limited company is a plaintiff, if there is reason to believe that the company will be unable to pay the costs of the defendant if the defendant is successful in its defence, the court may require sufficient security to be given for those costs, and may stay all proceedings until the security is given. However, section 357 only applies to a limited company which is formed and registered under Cap. 32 or an existing limited company, i.e. one formed and registered under an earlier Companies Ordinance. Therefore, a plaintiff which is an unlimited company or a company incorporated outside Hong Kong would not be caught by the section.

18. In a number of Hong Kong cases involving applications for security for costs against companies incorporated outside Hong Kong, the court recommended the amendment of section 357 of Cap. 32 to remove the anomaly that a company incorporated outside Hong Kong but having its central management and control in Hong Kong is immune from any security for costs as it is neither ordinarily resident out of the jurisdiction under Order 23 rule 1(1)(a) of the Rules of the High Court (Cap. 4A) nor a company caught by section 357 of Cap. 32.

<sup>25</sup> It also specifies that such power of extension may be exercisable during, or after the end of, that period.

## Position and key provisions in the new CO

19. The new CO widens the categories of companies in respect of which the court may require security for costs in actions. It is considered reasonable and just to order a foreign plaintiff to give security for costs in view of the difficulties that a defendant may encounter in enforcing a judgment against a foreign party. This also covers the loophole under Order 23 rule 1(1)(a) of the Rules of the High Court (Cap. 4A) in the situation where the plaintiff is a company incorporated outside Hong Kong but having its central management and control in Hong Kong.

20. **Section 905** re-enacts the matters in section 357 of Cap. 32 and extends the provisions to all types of companies incorporated outside Hong Kong, irrespective of whether the company is a limited or an unlimited company.

21. **Section 905** is not extended to unlimited companies incorporated in Hong Kong. It is an established common law principle that the insolvency or poverty of a plaintiff is no ground for requiring him to give security for costs. The only exception is in the case of a limited company under section 357 of Cap. 32. This is considered a price for the privilege of limited liability and therefore the provision is not extended to unlimited companies.

## TRANSITIONAL AND SAVING ARRANGEMENTS

22. The only transitional provision relates to **section 897** of the new CO where an application for inspection and production of documents made before the commencement of the new CO will continue to be dealt with under the provisions of Cap. 32 (**section 149 of Schedule 11** to the new CO).

# Part 21

## Consequential Amendments, and Transitional and Saving Provisions

### INTRODUCTION

Part 21 (Consequential Amendments, and Transitional and Saving Provisions) of the new Companies Ordinance (Cap. 622) (“new CO”) contains technical provisions that deal with consequential and related amendments to the Companies Ordinance (Cap. 32) (“Cap. 32”) and its subsidiary legislation and to other ordinances and subsidiary legislation in the Laws of Hong Kong, as well as transitional and saving arrangements, that are necessary on the commencement of the new CO.

### POLICY OBJECTIVES AND MAJOR PROVISIONS

2. Part 21 contains technical provisions of the following categories –

- (a) provisions for consequential and related amendments to Cap. 32, other ordinances, and their subsidiary legislation that are necessary on the commencement of the new CO (paragraphs 3 to 5);
- (b) transitional and saving provisions for smooth transition from the Cap. 32 regime to the new CO regime (paragraphs 6 to 8); and
- (c) provisions supplemental to the consequential and related amendments, and transitional and saving provisions mentioned above (paragraphs 9 to 11).

Provisions for consequential and related amendments to Cap. 32, other ordinances, and their subsidiary legislation that are necessary on the commencement of the new CO (Section 912 and Schedules 9 and 10)

3. The new CO restates with modifications most of the provisions in Cap. 32 concerning the formation and operation of live companies in Hong Kong. With the commencement of the new CO, such provisions in Cap. 32 will be repealed. Cap. 32 will be retitled as “Companies (Winding up and Miscellaneous Provisions) Ordinance”, housing the remaining provisions the predominance of which deal with company winding up and insolvency as well as prospectuses.

4. **Section 912(1)** provides for the inclusion in **Schedules 9 and 10** of the consequential and related amendments as follows –

- (a) Schedule 9 sets out the amendments to Cap. 32 and its subsidiary legislation including the amendments to retitle Cap. 32 as “Companies (Winding Up and Miscellaneous Provisions) Ordinance”; and
- (b) Schedule 10 sets out the amendments to other ordinances and subsidiary legislation.

The Financial Secretary is given a power under **section 912(2)** to amend Schedules 9 or 10 by notice published in the Gazette.

5. The consequential and related amendments include, for example, changes in references from “Companies Ordinance (Cap. 32)” to “Companies Ordinance (Cap. 622)”, and amendments arising from the repeal of the existing provisions in Cap. 32 in whole or in part.

### Transitional and saving provisions for smooth transition from Cap. 32 to the new CO regime (Sections 913 to 919 and Schedule 11)

6. **Section 913(1)** relates to the enactment of the transitional and saving provisions as required in respect of each Part of the new CO to enable a smooth transition from Cap. 32 to the new CO regime. Such transitional and saving provisions are set out in **Schedule 11**. The Financial Secretary is given a power under **section 913(2)** to amend Schedule 11 by notice published in the Gazette.

7. Other transitional and saving provisions of general application are contained in **sections 914 to 919**. For example, **section 914(4)** provides that the Eighth Schedule to Cap. 32 continues to apply to fees payable in respect of matters under the Cap. 32 provisions which have a continuing effect after the new CO commences.

8. Another example is **section 914(6) to (9)** which allows the Registrar of Companies (“the Registrar”) to specify appropriate forms for use for compliance with filing obligations under Cap. 32 which have a continuing effect after the new CO commences. The purpose is to simplify the process involved in the delivery and registration of documents after the new CO is in implementation. The operation of the provisions is as follows –

- (a) The effect of **section 914(6) and (7)** is that, before the date determined by the Registrar under **section 914(6)(b)**, a specified form used for the purpose under a provision of Cap. 32 may continue to be used alongside a new form, if so specified by the Registrar pursuant to **section 914(6)(a)**, and after that date, only the new specified form should be used for the purpose of the provision of Cap. 32.
- (b) **Section 914(8) and (9)** is in respect of particulars and information which are required to be provided other than by way of specified form for the purpose under a provision of Cap. 32. On or after the date determined by the Registrar under **section 914(8)(b)**, the particulars or information required by Cap. 32 should be stated or furnished in the form specified by the Registrar under **section 914(8)(a)**. Before that date, the requisite particulars or information may continue to be provided pursuant to the provisions of Cap. 32.

**Provisions supplemental to the consequential and related amendments, and transitional and saving provisions mentioned above (Sections 920 and 921)**

9. **Sections 920 and 921** contain supplemental provisions to the consequential and related amendments, and transitional and saving provisions mentioned in the preceding paragraphs.

10. **Section 920** clarifies that the provisions containing the consequential and related amendments, and the transitional and saving provisions are in addition to and not in derogation of section 23 of the Interpretation and General Clauses Ordinance (Cap. 1), except as otherwise provided in the provisions.

11. **Section 921** contains a general fallback transitional and saving provision. It provides that things done under the provisions of another ordinance (including Cap. 32) that are repealed and re-enacted by the new CO will continue to be legally effective. It also states that references to the repealed provisions in enactments, instruments or documents are to be construed as including references to the corresponding new provisions under the new CO, and vice versa. This general fallback provision has effect subject to any specific transitional or saving provisions set out in the new CO.

# Annex 1

## Lists of Members of the Standing Committee on Company Law Reform and the five Advisory Groups

### I. Standing Committee on Company Law Reform

#### (A) List of Members of the Standing Committee on Company Law Reform 2013-14

Chairman	Ex-Officio Members
Mr Anderson CHOW Ka-ming, SC	Ms Ada CHUNG, JP Registrar of Companies
Members	Mr Stefan GANNON, JP representing the Hong Kong Monetary Authority
Mr Stephen BIRKETT	Mr David GRAHAM representing the Hong Kong Exchanges and Clearing Limited
Mr Rock CHEN Chung-nin, BBS, JP	Mr HO Chung-kei, Patrick, JP representing the Secretary for Financial Services and the Treasury
Mr CHEW Fook-aun	Professor Edward L G TYLER representing the Department of Justice
Professor David Donald	Ms Teresa WONG Siu-wan, Official Receiver
Mr Vincent FAN Chor-wah	Mr Andrew YOUNG representing the Securities and Futures Commission
Professor GOO Say-hak	
Mr Peter W GREENWOOD	
Ms Roxanne ISMAIL	
Mr Johnson KONG Chi-how	
Mr Rainier LAM Hok-chung	
Mrs Catherine MORLEY	
Mr Kenneth NG Sing-yip	
Dr Kelvin WONG Tin-yau	
Ms Benita YU Ka-po	
Ms Wendy YUNG Wen-yee	
	Secretary
	Mrs Karen HO

## (B) List of past Chairmen and Members for the period of the Rewrite Exercise

Past Chairmen	Past Ex-officio Members
Mr Benjamin YU, SBS, SC, JP	Mr Charles BARR
Mr Godfrey LAM Wan-ho, SC, JP	Mr Darryl CHAN Wai-man
	Mr Y K CHOI, JP
Past Members	Mr Paul CHOW, SBS, JP
Mrs Anne CARVER	Mr Mark DICKENS, JP
Mr Felix CHAN Kwok-wai, MH	Mr Gordon W E JONES, JP
Mr Stephen HUI Chiu-chung, JP	Mr John LEUNG Chi-yan, JP
Ms Teresa KO Yuk-yin, JP	Mr E T O'CONNELL, JP
Ms Paddy LUI Wai-yu, JP	Mr William RYBACK
Mr John POON Cho-ming	
Mr Michael W SCALES	Past Secretaries
Ms Edith SHIH	Mr Edward LAU
Mr David P R STANNARD	Ms Phyllis MCKENNA
Ms Vanessa STOTT	
Mr William TAM Sai-ming	
Mr Carlson TONG, JP	
Mr Paul Franz WINKELMANN	
Mr Patrick WONG Chi-kwong	

## II. Joint Working Group formed by the Government and the Hong Kong Institute of Certified Public Accountants

### List of Members

Chairman	Ex-Officio Members
Mr Roger Thomas BEST, JP	Ms Ada CHUNG Lai-ling, JP
	Mr Charles Ramsay GRIEVE
Members	Mr HO Tin Ching
Mr Wilson FUNG Ying-wai	Miss Grace KWOK Wing-see
Mr Peter GRIFFITHS	
Ms Elizabeth LAW Kwan-mei, MH	Secretary
Mr Steve ONG	Mrs Christine Frances SIT
Mr John Bernard WILKINSON	
Mr Paul Franz WINKELMANN	

### III. Advisory Group on Provisions Relating to Share Capital, Distribution of Profits and Assets and Charges ("AG1")

#### List of Members

Name (Nominating Organisation)	
<b>Chairman</b>	<b>Members</b>
Mr David STANNARD (Standing Committee on Company Law Reform)	Mr Lincoln SOO Hung-leung, JP (The Chinese General Chamber of Commerce)
<b>Members</b>	Mr William TAM Sai-ming (The Hong Kong Association of Banks)
Mr Stephen BIRKETT	Dr Davy K C WU (Hong Kong Baptist University)
Mr CHAO Tien-yo (The Law Society of Hong Kong)	Ms Wendy W Y YUNG (The Hong Kong Institute of Chartered Secretaries)
Mr Colin CHAU Yu-nien (Hong Kong Exchanges and Clearing Limited)	<b>Representatives of Government Departments</b>
Prof Stephen CHEUNG Yan-leung, JP (The City University of Hong Kong)	Ms Feliciana CHEUNG Siu-wai (Hong Kong Monetary Authority)
Ms Ada CHUNG Lai-ling, JP (Companies Registry)	Mr William SHIU Wai-chuen (Land Registry)
Ms Julianne DOE (The Hong Kong Institute of Directors)	Mr Edward Lawson Griffin TYLER (Department of Justice)
Mr Dennis HIE Hok-fung (The Chinese University of Hong Kong)	<b>Alternate Members</b>
Mr Stephen HOPKINS (The Hong Kong General Chamber of Commerce)	Ms Tina W P LEE (The Hong Kong Association of Banks)
Ms Roxanne ISMAIL (Hong Kong Bar Association)	Mr Richard LEUNG Wai-keung (The Hong Kong Institute of Chartered Secretaries)
Mr John LEUNG Chi-yan, JP (Financial Services and the Treasury Bureau)	Mr Steve ONG (The Hong Kong Institute of Certified Public Accountants)
Ms Sonia LEUNG (The Securities and Future Commission)	Mr Emil YU Chen-on (The Hong Kong General Chamber of Commerce)
Mr Stefan Huoy-cheng LO (The City University of Hong Kong)	Mr Rimsky YUEN Kwok-keung, SC (Hong Kong Bar Association)
Ms Catherine MORLEY (The Hong Kong Institute of Certified Public Accountants)	

## IV. Advisory Group on Provisions Relating to Company Formation, Registration, Re-registration and Company Meeting and Administration ("AG2")

### List of Members

Name (Nominating Organisation)	
<b>Chairman</b>	<b>Members</b>
Mr Michael William SCALES (Standing Committee on Company Law Reform)	Mr William TSANG Yu-hei (The Hong Kong Institute of Certified Public Accountants)
<b>Members</b>	Mr Christopher TO (The Hong Kong Institute of Directors)
Dr Douglas ARNER (The University of Hong Kong)	<b>Representatives of Government Departments</b>
Ms Anne CHAPMAN (Hong Kong Exchanges and Clearing Limited)	Ms Pancy FUNG Shuk-hing (Intellectual Property Department)
Ms Ada CHUNG Lai-ling, JP (Companies Registry)	Ms D I HARDWICK (Lands Department)
Mr Russell Adam COLEMAN, SC (Hong Kong Bar Association)	Mr Charles NG Siong-kwong (Invest Hong Kong)
Mr Angus FORSYTH (The Hong Kong General Chamber of Commerce)	Mr Edward Lawson Griffin TYLER (Department of Justice)
Ms Gail HUMPHRYES (The Securities and Futures Commission)	<b>Alternate Members</b>
Mr IP Shing-hing, JP (The Chinese General Chamber of Commerce)	Mr Francis CHAN Chok-fai (The Hong Kong General Chamber of Commerce)
Mr Vincent KWAN Po-chuen (The Law Society of Hong Kong)	Mr Brian HO (The Securities and Futures Commission)
Dr Alex LAU Kun-luen (Hong Kong Baptist University)	Mr Charles MANZONI (Hong Kong Bar Association)
Mr John LEUNG Chi-yan, JP (Financial Services and the Treasury Bureau)	Mr Paul MOYES (The Hong Kong Institute of Chartered Secretaries)
Mrs Natalia SENG SZE Ka-mee (The Hong Kong Institute of Chartered Secretaries)	Ms Melissa Kaye PANG (The Law Society of Hong Kong)
Ms Vanessa STOTT (The Polytechnic University of Hong Kong)	Mr Peter Michael TISMAN (The Hong Kong Institute of Certified Public Accountants)

## V. Advisory Group on Provisions Relating to Directors and Officers ("AG3")

### List of Members

Name (Nominating Organisation)	
<b>Chairman</b>	<b>Members</b>
Mr Patrick WONG Chi-kwong (Standing Committee on Company Law Reform)	Mr Paul Franz WINKELMANN (The Hong Kong Institute of Certified Public Accountants)
<b>Members</b>	Mr Peter S H WONG (The Hong Kong Institute of Directors)
Mrs Anne CARVER (The Chinese University of Hong Kong)	Ms Eirene YEUNG (The Hong Kong Institute of Chartered Secretaries)
Mr Charles CHAU Chi-chung (The Law Society of Hong Kong)	Mr Rimsky YUEN Kwok-keung, SC (Hong Kong Bar Association)
Prof Stephen CHEUNG Yan-leung, JP (The City University of Hong Kong)	
Ms Ada CHUNG Lai-ling, JP (Companies Registry)	<b>Representatives of Government Departments</b>
Mr Vincent FAN Chor-wah (The Chinese General Chamber of Commerce)	Mr Edward Lawson Griffin TYLER (Department of Justice)
Mr GOO Say-hak (The University of Hong Kong)	
Ms Molly HO Kam-lan (The Hong Kong Association of Banks)	<b>Alternate Members</b>
Prof Simon S M HO (Hong Kong Baptist University)	Mr Brian HO (The Securities and Futures Commission)
Mr Stephen HUI Chiu-chung, JP (Standing Committee on Company Law Reform)	Mr Bernard HUI Man-bock, JP (The Hong Kong General Chamber of Commerce)
Ms Gail HUMPHRYES (The Securities and Futures Commission)	Ms Mary LAM Shuk-man (The Hong Kong Institute of Certified Public Accountants)
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Mr Gareth Huw THOMAS (The Hong Kong General Chamber of Commerce)	Mr Melvin SNG (The Law Society of Hong Kong)
Mr Carlson TONG, JP (Standing Committee on Company Law Reform)	Mr Tony TAM Chung-kit (The Hong Kong Association of Banks)
Mr Richard George WILLIAMS (Hong Kong Exchanges and Clearing Limited)	Ms Kelly WICK (Hong Kong Exchanges and Clearing Limited)

## VI. Advisory Group on Provisions Relating to Inspections, Investigation, Offences and Punishment ("AG4")

### List of Members

Name (Nominating Organisation)	
<b>Chairman</b>	<b>Representatives of Government Departments</b>
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Mr Richard LEUNG Wai-keung (The Hong Kong Institute of Chartered Secretaries)	Ms Samantha SUEN (The Hong Kong Institute of Chartered Secretaries)
Ms Alexandra LO Dak-wai (The Chinese University of Hong Kong)	Miss Christabel YOUNG Tsz-lan (The Hong Kong Exchanges and Clearing Limited)
Ms Karen NGAI (The Securities and Futures Commission)	
Mr Thomas SO Shiu-tsung (The Law Society of Hong Kong)	
Ms Vanessa STOTT (The Polytechnic University of Hong Kong)	
Ms Cynthia Y S TANG (The Hong Kong Institute of Directors)	
Mr Emil YU Chen-on (The Hong Kong General Chamber of Commerce)	

## Annex 2

# The New Companies Ordinance (Cap. 622) Major Initiatives

### MEASURES FOR ENHANCING CORPORATE GOVERNANCE

#### Strengthening the Accountability of Directors

- Restricting the appointment of corporate directors by requiring every private company to have at least one natural person to act as director, to enhance transparency and accountability.
- Clarifying in the statute the directors' duty of care, skill and diligence with a view to providing clear guidance to directors.

#### Enhancing Shareholder Engagement in the Decision-Making Process

- Introducing a comprehensive set of rules for proposing and passing a written resolution.
- Requiring a company to bear the expenses of circulating members' statements relating to the business of, and proposed resolutions for, Annual General Meetings, if they are received in time to be sent with the notice of the meeting.
- Reducing the threshold requirement for members to demand a poll from 10% to 5% of the total voting rights.

### Improving the Disclosure of Company Information

- Requiring public companies and the larger (i.e., companies that do not qualify for simplified reporting) private companies<sup>1</sup> and guarantee companies<sup>2</sup> to prepare a more comprehensive directors' report which includes an analytical and forward-looking "business review", whilst allowing private companies to opt out by special resolution. The business review will provide useful information for shareholders. In particular, the requirement to include information relating to environmental and employee matters that have a significant effect on the company is in line with international trends to promote corporate social responsibility.

#### Fostering Shareholder Protection

- Introducing more effective rules to deal with directors' conflicts of interests, including expanding the requirement for seeking shareholders' approval to cover directors' employment contracts which exceed three years.
- Requiring disinterested shareholders' approval in cases where shareholders' approval is required for transactions of public companies and their subsidiaries.

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<sup>1</sup> Under the new Ordinance, a private company is regarded as small if it satisfies any two of the following conditions: (a) total annual revenue of no more than HK\$100 million; (b) total assets of no more than HK\$100 million; and (c) no more than 100 employees.

<sup>2</sup> Under the new Ordinance, a guarantee company is regarded as small if its total annual revenue does not exceed HK\$25 million.

- Requiring the conduct of directors to be ratified by disinterested shareholders' approval to prevent conflicts of interest and possible abuse of power by interested majority shareholders in ratifying the unauthorised conduct of directors.
- Replacing the "headcount test" with a not more than 10% disinterested voting requirement for privatisations and specified schemes of arrangement, while giving the court a new discretion to dispense with the test (in cases where it is retained) for members' schemes.
- Extending the scope of the unfair prejudice remedy to cover "proposed acts and omissions", so that a member may bring an action for unfair prejudice even if the act or omission that would be prejudicial to the interests of members is not yet effected.

### Strengthening Auditors' Rights

- Empowering an auditor to require a wider range of persons, including the officers of a company's Hong Kong subsidiary undertakings and any person holding or accountable for the company or its subsidiary undertakings' accounting records, to provide information or explanation reasonably required for the performance of the auditor's duties. The offence for failure to provide the information or explanation is extended to cover officers of the company and the wider range of persons.

## MEASURES FOR ENSURING BETTER REGULATION

### Ensuring the Accuracy of Information on the Public Register

- Clarifying the powers of the Registrar of Companies (the Registrar) in relation to the registration of documents, such as specifying the requirements for the authentication of documents to be delivered to the Companies Registry (the Registry) and the manner of delivery, and withholding the registration of unsatisfactory documents pending further particulars.
- Clarifying the Registrar's powers in relation to the keeping of the register, such as rectifying typographical or clerical errors, making annotations and requiring a company to resolve any inconsistency or provide updated information.
- Providing a statutory basis for applications to court for removing information from the register that is inaccurate, forged or derived from anything invalid, ineffective or done without the authority of the company.
- Requiring a company to deliver to the Registry a return, including a statement of capital, whenever there is a change to its capital structure, to ensure that the public register contains up-to-date information on a company's share capital structure.

- Requiring all guarantee companies to file annual returns with financial statements and introducing an escalating scale of annual registration fees for annual returns of guarantee companies to encourage timely compliance of statutory filing requirement.

### Improving the Registration of Charges

- Revising the list of registrable charges, such as expressly providing that a charge on an aircraft or any share in an aircraft is registrable, and removing the requirement to register a charge for the purpose of securing an issue of debentures.
- Replacing the automatic acceleration of the repayment obligation with a choice given to the lender as to whether the secured amount is to become immediately payable when a charge is void due to non-compliance with the registration requirements.
- Requiring a certified copy of the charge instrument (in addition to the prescribed particulars of the charge) to be registered and available for public inspection, to provide more detailed information to those who search the register.
- Shortening the period for delivery to the Registrar of the charge instrument and the prescribed particulars from five weeks to one month, to reduce the period during which the charge is not visible on the register.
- Requiring written evidence of satisfaction / release of a charge to accompany a notification to the Registrar for registration of the satisfaction / release, thus making such documents available for public inspection.

### Refining the Scheme for Deregistration of Companies

- Imposing three additional conditions for the deregistration of defunct companies, namely that the applicant must confirm that the company is not a party to any legal proceedings and that neither the company nor its subsidiary has any immovable property in Hong Kong, to minimise any potential abuse of the deregistration procedure.

### Improving the Enforcement Regime

- Enhancing the investigatory powers of an inspector, for example, by requiring a person under investigation to preserve records or documents and to verify statements made by statutory declaration.
- Providing better safeguards to ensure the confidentiality of information obtained in investigations and enquiries and for the better protection of informers.
- Providing new powers for the Registrar to obtain documents or information to ascertain whether any conduct that would constitute an offence in relation to the provision of false or misleading statement to the Registrar has taken place.
- Strengthening the enforcement regime in relation to the liabilities of officers of companies for the companies' contravention of provisions in the new Ordinance, including lowering the threshold for prosecuting a breach or contravention and extending it to cover reckless acts through a new definition of "responsible person".

- Introducing a new offence in relation to inaccurate auditor's reports. The offence would be committed if the auditors in question knowingly or recklessly caused two important statements to be omitted from the auditor's report.
- Empowering the Registrar to compound specified offences to optimise the use of judicial resources. Compoundable offences are generally confined to straightforward, minor regulatory offences committed by companies that are punishable by a fine.
- Introducing a new court-free statutory amalgamation procedure for wholly owned intra-group companies.
- Streamlining the procedures for the restoration of dissolved companies by court order.
- Introducing a new administrative restoration procedure for a company dissolved by the Registrar in straightforward cases, without the need for recourse to the court.

## MEASURES FOR FACILITATING BUSINESS

### Streamlining Procedures

- Allowing companies to dispense with Annual General Meetings by unanimous shareholders' consent.
- Introducing an alternative court-free procedure for reducing capital based on a solvency test.
- Allowing all types of companies (rather than just private companies, as in the existing Companies Ordinance (Cap. 32)) to purchase their own shares out of capital, subject to a solvency test.
- Allowing all types of companies (whether listed or unlisted) to provide financial assistance to another party for the purpose of acquiring the company's own shares or the shares of its holding company, subject to a solvency test. Under the existing Companies Ordinance (Cap. 32), subject to certain specified exceptions, there is a broad prohibition on the giving of financial assistance to purchase the company's own shares.
- Facilitating SMEs to prepare simplified financial and directors' reports along the following lines:
  - a private company (with the exception of a bank/deposit-taking company, an insurance company or a stockbroker) will automatically qualify for simplified reporting if it qualifies as a "small private company".
  - the holding company of a group of companies that qualifies as a "group of small private companies" will also qualify for simplified reporting.
  - a private company that is not a member of a corporate group may adopt simplified reporting with the agreement of all the members.
- Allowing small guarantee companies and groups of small guarantee companies, which have a total annual revenue of not more than \$25 million, to qualify for simplified reporting.

### Facilitating Simplified Reporting

- A private company or a group of private companies which is not qualified as a “small private company” or a “group of small private companies” respectively may prepare simplified reports if it meets a higher size criteria and if the members holding 75% of the voting rights so resolve and no member objects.
- Making the summary financial reporting provisions more user-friendly and extending their application to companies in general (rather than confining them to listed companies, as in the existing Companies Ordinance) (Cap. 32).

### Facilitating Business Operations

- Making the use of a common seal optional and relaxing the requirements for a company to have an official seal for use abroad.
- Permitting a general meeting to be held at more than one location using electronic technology.
- Setting out the rules governing communications to and by companies in electronic form.

## MEASURES FOR MODERNISING THE LAW

### Rewriting the Law in Simple and Plain Language

- Modernising the language and re-arranging the sequence of some of the provisions in a more logical and user-friendly order so as to make the new Ordinance more readable and comprehensible.

### Abolishing Par Value for Shares

- Adopting a mandatory system of no-par for all local companies with a share capital as par value is an antiquated concept that may give rise to practical problems, such as inhibiting the raising of new capital and unnecessarily complicating the accounting regime.

### Abolishing Memorandum of Association

- Abolishing the requirement for companies to have a memorandum of association and only articles of association are required. Conditions contained in the memorandum of existing companies will be deemed to be provisions of their articles, except those relating to authorized share capital and par value, which are regarded as deleted under the new Ordinance.

### Removing the Power to Issue Share Warrants

- Removing the power of companies to issue share warrants to bearers. Share warrants are rarely issued by companies nowadays and are undesirable from the perspective of anti-money laundering because of the lack of transparency in the recording of their ownership and the manner by which they are transferred.

### Clarifying the Rules on Indemnification of Directors against Liabilities to Third Parties

- Clarifying the rules on the indemnification of directors against liabilities to third parties in order to remove the uncertainties at common law.

## Annex 3

# The New Companies Ordinance (Cap. 622) List of Subsidiary Legislation

1. Cap. 622A Companies (Words and Expressions in Company Names) Order
2. Cap. 622B Companies (Disclosure of Company Name and Liability Status) Regulation
3. Cap. 622C Companies (Accounting Standards (Prescribed Body)) Regulation
4. Cap. 622D Companies (Directors' Report) Regulation
5. Cap. 622E Companies (Summary Financial Reports) Regulation
6. Cap. 622F Companies (Revision of Financial Statements and Reports) Regulation
7. Cap. 622G Companies (Disclosure of Information about Benefits of Directors) Regulation
8. Cap. 622H Companies (Model Articles) Notice
9. Cap. 622I Company Records (Inspection and Provision of Copies) Regulation
10. Cap. 622J Companies (Non-Hong Kong Companies) Regulation
11. Cap. 622K Companies (Fees) Regulation
12. Cap. 622L Companies (Unfair Prejudice Petitions) Proceedings Rules

