PART 1

PRELIMINARY

Introduction

1. Part 1 is an introductory part that sets out the title of the new Ordinance, its commencement date, and the interpretation and definitions of various terms and expressions that are used throughout the Ordinance, including the types of companies that can be formed under the Ordinance and the meaning of terms such as subsidiaries, parent companies, parent undertaking and subsidiary undertaking, etc. Part 1 will be further reviewed in the course of preparing the draft provisions of the CB for the second phase consultation in early 2010.

- The significant changes to be introduced under this Part are highlighted below:

  (a) Reducing the types of companies that can be formed to five, namely, (i) private companies limited by shares; (ii) public companies limited by shares; (iii) private unlimited companies with a share capital; (iv) public unlimited companies with a share capital; and (v) guarantee companies that do not have share capital; and

  (b) Replacing the phrase "officer who is in default" with "responsible person" and refining the definition to strengthen the enforcement regime (such as lowering of the threshold for a breach or contravention by removing wilfulness as an element of the offence, inclusion of negligent acts or omissions and expansion of the categories of persons to be caught).

Significant Changes

(a) Types of companies formed under the CO

Background

2. At present, under the combined effect of sections 4(2) and (4) and section 29 of the CO, 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 are determined. They are:

   (a) private companies limited by shares;

   (b) non-private companies limited by shares;

   (c) private companies limited by guarantee without share capital;

   (d) non-private companies limited by guarantee without share capital;

   (e) private unlimited companies with a share capital;

   (f) non-private unlimited companies with a share capital;

   (g) private unlimited companies without share capital; and

   (h) non-private unlimited companies without share capital.

3. Based on the SCCLR's recommendations[1], we propose to streamline the types of companies along the following lines:

   (a) the category of unlimited companies without share capital (i.e. (g) and (h) in paragraph 2 above) should be 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 register;

[1] See SCCLR, *Report of the Standing Committee on Company Law Reform on the Recommendations of a Consultancy Report of the Review of the Hong Kong Companies Ordinance* (February 2000), paragraph 5.78 (available at http://www.cr.gov.hk/en/standing/docs/Rpt_SCCLR(E).pdf) and SCCLR, "Chapter 4: Types of Company and Definitions of Private and Public Companies", *2006-07 Annual Report*, (available at http://www.cr.gov.hk/en/standing/docs/23anrep_e.pdf).

(b) companies limited by guarantee should become a separate category of companies (i.e. (c) and (d) in paragraph 2 above will be merged into one category of companies limited by guarantee without share capital). They should be treated in a manner similar to public companies with appropriate modifications. For example, like public companies, all guarantee companies should be required to file annual reports and audited accounts;

(c) non-private companies should be renamed "public companies" which are defined to mean companies other than private companies or guarantee companies. No change should be made to the definition of private companies in section 29 of the CO;

4. As a result, the types of companies permissible under the new CO will be reduced to five, 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 share capital.

Proposal

5. **Clause 1.9** defines an unlimited company and **Clause 1.7** defines a company limited by shares. Under the definitions, both types of companies must be companies having a share capital. **Clause 1.10** sets out the required characteristics of a private company which are the same as those currently provided under section 29 of the CO (i.e. a company is a private company if its articles restricts members' rights to transfer shares, limits the number of members to 50, and prohibits any invitation to the public to subscribe for any shares or debentures), but clarifies that a private company must have share capital. **Clause 1.11** provides that a company is a public company if it has a share capital and is neither a private company nor a guarantee company.

6. **Clause 1.8(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 constitution to the amount that the members undertake to contribute to the assets of the company in the event of its being wound up. **Clause 1.8(2)** makes it clear that a company limited by guarantee and having a share capital formed on or before 14 February 2004 under the CO, will be regarded as a guarantee company under the CB although it has a share capital.

(b) Replacing the phrase "officer who is in default" with "responsible person" and refining the definition to strengthen the enforcement regime

Background

7. Many offence provisions under the CO punish not only a company but also every officer of the company who is in default. The phrase "officer who is in default" is currently defined by section 351(2) as meaning any officer of the company, or any shadow director of the company, who knowingly and wilfully authorises or permits the default, refusal or contravention mentioned in relevant provisions of the CO.

8. There are a few problems with this definition. They are:

(a) the present formulation of "officer who is in default" does not cover negligence of officers; and

(b) where a company having a corporate officer commits an offence, the present provision does not punish, in addition to such corporate officer who has caused the default, any officer or shadow director of such a corporate officer who has caused the corporate officer to be in default.

9. In view of the above deficiencies, we consider it necessary that the enforcement regime under the new CO should be strengthened. In this respect, we propose to follow section 1121(3) of the UKCA 2006 by replacing the reference to "knowingly and wilfully authorises or permits the default, refusal or contravention" with "authorises or permits, participates in, or fails to take all reasonable steps to prevent, the contravention", thus lowering the threshold for a breach or contravention and extending it to negligent acts or omission. We propose also to extend the punishment to

an officer of a corporate officer of a company who has caused the default where such corporate officer commits an offence as an "officer in default", similar to section 1122(2) of the UKCA 2006. In view of these proposed changes, the term "responsible person" is, in our view, a better name than "officer who is in default".

Proposal

10. For the reasons stated in paragraph 9, a new term "responsible person" will be used in the new CO to replace the phrase "officer who is in default". **Clause 1.3(2)** defines a person as a "responsible person" of a company or non-Hong Kong company if he is an officer or shadow director of the company or non-Hong Kong company who authorises or permits, participates in, or fails to take all reasonable steps to prevent the contravention or failure in question.

11. **Clause 1.3(3)** extends the scope of responsible person of a company or non-Hong Kong company to cover an officer or shadow director of a body corporate that is an officer or shadow director of the company or non-Hong Kong company. Where the body corporate is liable as a responsible person, an officer or shadow director of the body corporate who caused the default will also be liable as a responsible person of the company or non-Hong Kong company.

12. The proposals will strengthen the enforcement regime in relation to breaches of obligations, or contraventions of requirements, under the CO by an officer (including shadow director) of a company or a non-Hong Kong company.