



# The New Hong Kong Companies Ordinance

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## Companies Ordinance Rewrite

- **Background to the Hong Kong Companies Ordinance Rewrite**
  - Rewrite of the Companies Ordinance was endorsed by Legislative Council (“LegCo”) and launched mid-2006
  - Phased approach:
    - **1st phase** (the new Companies Ordinance (“new CO”) – deals with all provision relating to live companies
    - **2nd phase** – deals with winding-up and insolvency related provisions
    - provisions on prospectuses will be dealt with in a separate review by the Securities and Futures Commission



## Companies Ordinance Rewrite (2)

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- The Companies Bill was introduced into LegCo in January 2011
- The Bills Committee conducted 44 meetings totalling over 120 hours and examined over 200 papers and submissions from the Administration and various deputations along with over 800 amendments
- The resumed second reading debate commenced in LegCo on 3rd July 2012 and after 8 days of intense deliberation, the new CO was passed by LegCo on 12 July 2012



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## The new CO

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- 21 Parts, comprising 921 sections and 11 schedules
- 12 items of subsidiary legislation – [introduced into Legislative Council in batches from February 2013](#)
- Commencement expected in 2014 after enactment of subsidiary legislation



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## Structure of the new CO

- Divided into 21 Parts, comprising 921 sections and 11 Schedules

- Part 1 – Preliminary
- Part 2 – Registrar of Companies and Companies Register
- Part 3 – Company Formation and Related Matters, and Re-registration of Company
- Part 4 – Share Capital
- Part 5 – Transactions in relation to Share Capital
- Part 6 – Distribution of Profits and Assets
- Part 7 – Debentures
- Part 8 – Registration of Charges
- Part 9 – Accounts and Audit
- Part 10 – Directors and Company Secretaries



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## Structure of the new CO (2)

- Part 11 – Fair Dealing by Directors
- Part 12 – Company Administration and Procedure
- Part 13 – Arrangements, Amalgamation, and Compulsory Share Acquisition in Takeover and Share Buy-Back
- Part 14 – Remedies for Protection of Companies' or Members' Interests
- Part 15 – Dissolution by Striking Off or Deregistration
- Part 16 – Non-Hong Kong Companies
- Part 17 – Companies not Formed, but Registrable, under this Ordinance
- Part 18 – Communications to and by Companies
- Part 19 – Investigations and Enquiries
- Part 20 – Miscellaneous
- Part 21 – Consequential Amendments, and Transitional and Saving Provisions

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## Four major objectives of the new CO

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- Enhancing corporate governance
- Ensuring better regulation
- Facilitating business
- Modernising the law



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## Topics to be considered to-day

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- **Modernizing the Law**
  - Abolition of Memorandum of Association (“MA”) for **all** companies
  - Migration to mandatory no-par for **all** companies
- **Ensuring Better Regulation**
  - Lowering the threshold for contravention by officers through a new definition of “responsible person”
  - Improving the registration of charges regime
  - Empowering the Registrar to compound specified offences to encourage due compliance and optimize the use of judicial resources

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## Topics to be considered to-day (2)

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- ***Facilitating Business***

- Introducing a new alternative court free procedure for reducing capital based upon a solvency test
- Allowing all types of companies (other than just private companies) to purchase their own shares out of capital, subject to a solvency test
- Allowing all types of companies (whether listed / unlisted) to provide financial assistance to another party to acquire shares in the company or its holding company, subject to a solvency test

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## Abolition of the MA for all companies

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### ***Background***

- Abolition of ultra vires rule, means the objects clause has become less significant with most companies having the capacity and right powers and privileges of a natural person (section 5A of Cap 32 and **section 115** of new CO)
- Most information is now contained in the incorporation form and AA and most provisions of the MA can be amended
- The need for MA as a separate constitutional document has diminished
- Under new CO, the MA is abolished for all companies

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## Abolition of the MA for all companies (2)

- Pursuant to **section 67** of the new CO, any one or more persons may form a company by signing the articles of the company intended to be formed and delivering to the Registrar for registration: (i) an incorporation form; and (ii) a **copy** of the articles
- The agreement by the subscribers to take up shares in the company (previously set out in the MA) will now be in the articles, which will be signed by all of the subscribers
- The incorporation form must contain a statement confirming that the company's articles have been signed for the purposes of section 67(1)(a) by every person proposing to become a member of the company on formation and a statement that the articles delivered under section 67(1)(b)(ii) are the same as those signed by the founder members / subscribers (**section 68(1)(e)**)

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## Abolition of the MA for all companies (3)

### **Mandatory Articles**

- Every company is statutorily **required** to have articles on the following:
  - Company name (**section 81**)
  - If the company has a licence to dispense with the use of the word "limited" in its name – objects (**section 82(1)**)
  - Members liabilities (**section 83**)
  - Liabilities / Contributions of members (**section 84**)
  - Capital and initial shareholding on formation (**section 85**)
- These mandatory articles comprise information previously set out in the MA

### **Optional Articles**

- Any company other than one with a licence to dispense with the use of the word "limited" in its name **may** state objects (**section 82(2)**)
- A company **may** state the maximum number of shares that a company may issue

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## Abolition of the MA for all companies (4)

### Model Articles / Bespoke Articles

- For additional regulations, all companies may create bespoke articles or may adopt all or any of the Model Articles to be prescribed by the Financial Secretary for the type of company to which it belongs (**sections 78 and 79**)
- Companies (Model Articles) Notice will prescribe Model Articles for:
  - (1) public company
  - (2) private company limited by shares
  - (3) guarantee company
- These replace Table A and Table C in the First Schedule to Cap 32
- The Model Articles will apply by default if no additional articles are filed by the company or in so far as not excluded / modified by any articles so filed (**section 80**)

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## Abolition of the MA for all companies (5)

### Existing Companies

- **Section 98:**
  - A condition of the MA of an existing company immediately before commencement of the new CO is deemed to be regarded as a provision of that company's articles of association, except that any such condition setting out authorized share capital and the par value of shares are to be regarded as deleted for all purposes
  - All references in any other ordinances / documents etc to MA is a reference to Articles of Association

### What Needs to be Done

- The deeming provisions ensure that existing companies need not take any steps as a result of the changes – the deeming provisions are sufficient to ensure compliance
- However companies may wish to take this opportunity to review their constitutional documents to see if there are any changes that they wish to make as a result of the new CO

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## Retiring the concept of par

### Retiring the Concept of Par

- Abolition of Par Value of Shares for **all** companies
  - Par value does not serve its original purpose of protecting creditors and shareholders and gives no indication of real value of shares
  - Par value gives rise to practical problems, inhibiting raising of new capital and unnecessarily complicating the accounting regime
  - Upon commencement of **section 135** of the new CO, a company's shares will have no nominal value. This applies to all companies
  - Relevant concepts such as nominal value and share premium will be abolished

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## Retiring the concept of par (2)

- Deeming provisions to ensure that contractual rights defined by reference to par value and related concepts will not be affected by the abolition of par. The deeming provisions will save considerable work, expense and time for companies and reduce the possibility of disputes (**section 40 – Schedule 11**)
- Existing share capital will be amalgamated with any amount standing to the credit of the company's share premium account and capital redemption reserve (**section 37 – Schedule 11**)
- The currently permitted uses of the share premium account are preserved for credit balance of share premium account on date of migration to no-par (**section 38 – Schedule 11**)

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## Retiring the concept of par (3)

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- **Section 170** sets out permitted alterations of share capital. In addition to previous permitted alterations, in the no-par regime a company can now:
  - increase share capital without allotting and issuing new shares if funds / assets are provided by members
  - capitalize profits with / without allotting / issuing new shares
  - allot and issue bonus shares with / without increasing share capital
- The no-par environment provides increased flexibility
- Mandatory no-par regimes exist in Australia, New Zealand and Singapore

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## Retiring the concept of par (3)

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- *The Companies Registry has issued an External Circular on this topic which can be accessed at:*

[http://www.cr.gov.hk/en/publications/guidelines\\_01.htm](http://www.cr.gov.hk/en/publications/guidelines_01.htm)

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## Responsible Person

- Lowering the threshold for contravention by officers through a new definition of “responsible person”
  - The Companies Ordinance attributes criminal liability to an officer in default if he knowingly and wilfully authorizes or permits the default. The evidential burden is very high because of the requirement of “wilfulness”
  - The offences involved are mostly regulatory in nature and the majority (over 90%) are summary offences punishable by fine
  - “Responsible person” is defined in the new CO as an officer of a company who authorizes or permits, or participates in, the contravention or failure (section 3)
  - The effect of the new formulation is to lower the prosecution threshold to remove the “wilful” element

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## Responsible Person (2)

- The original proposal for the new formulation in the Companies Bill was modelled upon section 1121 of the UK Companies Act 2006 and had an additional limb of “fails to take all reasonable steps to prevent the contravention”
- This caused concern during the legislative process that negligence was being criminalized
- After much lively debate, the administration agreed to amend the formulation recognizing that the amended formulation would still achieve the policy objective of ensuring better regulation

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## Changes in the Registration of Charges

- **Improving the registration of charges regime**
  - Current regime is basically retained with some improvements
  - Updating the list of registrable charges (**section 334**)
    - It is expressly provided that a charge on an aircraft / share in an aircraft is registrable
    - A charge on instalments due but not paid on issue price of shares is registrable
    - Charge for the purposes of securing any issue debentures is removed (as usually registered as a floating charge)

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## Changes in the Registration of Charges (2)

- It is clarified that a shipowner's lien on subfreights is not regarded as a charge on book debts / floating charge and is not registrable
- A charge on cash deposits is not regarded as a charge on book debts
- Replacing the automatic acceleration of repayment obligation with a choice for the lender (**section 337(6)**)
- Requiring a certified copy of the charge instrument to be registrable and available for public inspection (**sections 335, 336 and 338 to 340**)
- 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**)

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## Changes in the Registration of Charges (3)

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- Requiring a certified copy of written evidence of debt satisfaction or release of a charge to be registered and made available for public inspection (**section 345**)
- 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(4)**)
- Empowering the Court to rectify the particulars in the registered charge instrument and evidence of discharge (**section 347**)
- More important than ever for lenders to make enquiries and search the register to ascertain what charges have already been registered by the company

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## Changes in the Registration of Charges (4)

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- Most significant change is registration of copy charge instrument
- Full details of charge available on public register e.g. negative pledge / automatic crystallisation
- Third parties will have deemed notice of all terms in the charge instrument
- Later chargees will be deemed to know terms of all previous charges; and this may affect priorities

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## Compounding

- **Section 899** empowers the Registrar, at her discretion, to compound specified offences so as to:
  - Encourage compliance with the provisions of the new CO, and
  - Optimize the use of judicial resources
- Specified offences are set out in **Schedule 7** of the new CO:
  - Failing to deliver director's written Consent to Act (**section 74(2)**)
  - Failing to engrave name etc. on common seal (**section 124(3)**)
  - Improper use of the common seal (**section 124(4)**)
  - Failure to file annual returns (**sections 662(6)** and **section 788(3)** re registered non-Hong Kong companies)
  - Failure by a registered non-Hong Kong company to deliver accounts (**section 789(3)**)

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## Compounding (2)

- Additional offences relating to the display of company names will be added upon enactment of the Companies (Display and Publication of Company Name and Liability Status) Regulation
- Corresponding offences for registered non-Hong Kong companies re the display of names will also be added (**section 792(6)** of the new CO re breach of **section 792(1) and (2)**)
- The Registrar may, if she has reason to believe a prescribed offence has been committed, give the company notice in writing which:
  - (i) States that the Registrar has reason to believe the company has committed the offence and setting out particulars of the offence; and
  - (ii) Conditions upon which no prosecution action will be taken including:
    - Amount of the compounding fee to be paid;
    - The period within which conditions must be complied with; and
    - Any other information that the Registrar considers necessary

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## Compounding (3)

- Where the offence is a failure to do a particular act, the Notice will require the act to be done within a specified period (which can be extended)
- The compounding fee will be set as HK\$600
- If the fee is paid and the act is done, no prosecution action will be taken
- If either the fee is not paid or the act is not done, the Registrar may proceed with prosecution action
- The payment of compounding fee is not an admission of liability
- The Notice may only be issued before proceedings for any contravention are commenced
- Offences will be confined to those offences that are straight forward minor regulatory offences committed by a company that are punishable by a fine only

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## Transactions in relation to Share Capital

- Except for re-designating the nominal value of shares to a lower amount, 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**). The new CO introduces, as an alternative procedure, a general court-free procedure which will be faster and cheaper and can be utilised by all companies
- **Sections 215 to 225** provide for the said court-free procedure, subject to compliance with a solvency test. The company needs to obtain members' approval by a special resolution. The company must publish notices with relevant information in the Gazette and newspapers and must register a solvency statement with the Registrar of Companies. 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

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## Transactions in relation to Share Capital (2)

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- 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**)
- Under the new CO, all companies are allowed to fund buy-backs out of capital, subject to a solvency requirement (**sections 258 to 266**). The procedures are similar to a court-free reduction of capital



## Transactions in relation to Share Capital (3)

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- **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. The main change under the new CO are to allow all types of companies (listed or unlisted) to provide financial assistance, subject to satisfaction of a solvency test and one of the three procedures set out in **sections 283 to 289**
- **Section 204** of the new CO provides that a uniform solvency test will be applicable to 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. The solvency test is based on cash flow alone. A 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



## Looking Forward

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- *The CR will arrange seminars and workshops on the new CO for stakeholders*
- *The new CO can be accessed at:*  
 [< http://hklaw.ccgo.hksarg/eng/index.htm >](http://hklaw.ccgo.hksarg/eng/index.htm)
- *The CR website has information on the new CO, please visit the website at: < http:// www.cr.gov.hk >*



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