



The New Companies Ordinance

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Accounts and Audit





Application of new CO provisions to first financial year [s 358]

- The requirements in the new CO in relation to accounting records [ss 373, 374, 376 & 377], simplified reporting [s 359], financial statements [ss 379 & 436], directors' report [s 388], laying reporting documents before AGM [s 429], summary financial report [s 439] and revision of financial statements [s 449] apply to a financial year that begins on or after commencement of the new CO.
- Corresponding requirements in Cap 32 continue to apply in relation to books of account, accounts, directors' report, laying of accounts before AGM, summary financial report and revision of accounts for a financial year beginning before commencement of the new CO [Schedule 11 ss 76, 77, 78, 83, 84 and 107(2)].

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Accounting reference period

- S 367 provides for the determination of a company's **first financial year** and subsequent financial years by reference to its **accounting reference period**.
- A company's first financial year after the commencement of the new CO begins on the first day of its first accounting reference period and ends on the last day of that period [s 367(1)].
- The financial year is the period by reference to which the company's financial statements are to be prepared [s 379(1)].
- For an existing company, the first accounting reference period begins on the day immediately following the end date of the company's accounts for the financial year immediately before the commencement of the new CO and ends on the first anniversary of that date [ss 368(1), 369(1) to (4)].

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Accounting reference period (cont'd)

- Examples

Commencement date of new CO : 3 March 2014

Company A

- ◆ Current financial year : 1 April 2013 to 31 March 2014
- ◆ End date of company's accounts prepared under Cap 32 : 31 March 2014
- ◆ Company's first accounting reference period under the new CO :
1 April 2014 to 31 March 2015

Company B

- ◆ Current financial year : 1 January 2014 to 31 December 2014
- ◆ End date of company's accounts prepared under Cap 32 : 31 December 2014
- ◆ Company's first accounting reference period under the new CO:
1 January 2015 to 31 December 2015

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Accounting reference period (cont'd)

- For a company formed and registered under the new CO, the first accounting reference period begins on the incorporation date and ends on –
 - ◆ a date specified by the directors falling within 18 months after the company's incorporation; or
 - ◆ if none specified, the last day of the month of the first anniversary of the company's incorporation [ss 368(2), 369(5) to (7)].
- 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 the company's accounting reference date [s 368(3)].

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Simplified reporting

- Currently a private company (other than a company which is a member of a corporate group) may with the written agreement of all the shareholders prepare simplified accounts and directors' report in respect of one financial year at a time.
- Under the new CO, private or guarantee companies falling within the "reporting exemption" are qualified for simplified reporting.

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Simplified reporting (cont'd)

- Companies qualified for reporting exemption
 - ◆ a small private company / holding company of a group of small private companies meeting two of the following conditions in a financial year –
 - total revenue / aggregate total revenue not exceeding \$100 million
 - total assets / aggregate total assets not exceeding \$100 million
 - employees / aggregate employees not exceeding 100

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Simplified reporting (cont'd)

- ◆ an eligible private company / holding company of a group of eligible private companies meeting a higher size criteria (i.e. two of the following conditions in a financial year: total revenue / aggregate total revenue not exceeding \$200 million, total assets / aggregate total assets not exceeding HK\$200 million, and employees / aggregate employees not more than 100) and with 75% approval from members and no member objects.
- ◆ other private companies (not being a member of a corporate group) with unanimous members' written agreement.
- ◆ a small guarantee company / holding company of a group of small guarantee companies with total revenue / aggregate total revenue not exceeding \$25 million in a financial year.

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Duty to prepare a more analytical business review

- The new CO requires a directors' report to include a business review which should cover the following information of a company
 - ◆ a fair review of its business
 - ◆ a description of its principal risks and uncertainties
 - ◆ particulars of any important events affecting it which have occurred since the end of the financial year
 - ◆ an indication of likely future development in its business

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Duty to prepare a more analytical business review (cont'd)

- ◆ a discussion on its environmental policies and performance, including compliance with the relevant laws and regulations that have a significant impact on the company
- ◆ an account of its key relationships with employees, customers, suppliers and others that have a significant impact on the company and on which its success depends
- The requirement for business review is in line with international trends to promote corporate social responsibility.

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Duty to prepare a more analytical business review (cont'd)

- The following companies are not required to prepare a business review -
 - ◆ companies falling with the reporting exemption
 - ◆ a private company that does not fall within the reporting exemption with 75% approval from members
 - ◆ a wholly owned subsidiary of a body corporate
- A director is not liable for untrue or misleading statement or omission unless he knew or was reckless as to whether it was untrue or misleading, or there was dishonest concealment of a material fact.

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Auditor's rights

- Auditor's rights to information
 - ◆ S 412 empowers auditors to require information and explanation for the performance of their duties from a wider range of persons –
 - (a) an officer of the company
 - (b) a HK incorporated subsidiary of the company
 - (c) an officer or auditor of such a subsidiary
 - (d) a person holding or accountable for the accounting records of the company or such a subsidiary
 - (e) any of the above persons or subsidiary at the time to which the information or explanation relates

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Auditor's rights (cont'd)

- ◆ The auditor of a holding company may require the company to obtain information or explanation from its subsidiary undertaking that is not a HK incorporated company, an officer or auditor of such a subsidiary undertaking and a person holding or accountable for the accounting records of such a subsidiary undertaking.
- Auditor's rights in relation to general meetings and written resolutions [ss 411, 555, 559, 575]
 - ◆ S 575 requires a company to give notice of or any other document relating to a general meeting to the auditor at the same time as the notice or document is given to its members.
 - ◆ S 559 requires the company to send to the auditor notice of the fact that a written resolution is passed.

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Auditor's rights (cont'd)

- Qualified privilege
 - ◆ S 410 provides that in the absence of malice, an auditor is not liable for defamation in respect of any statement made by the auditor in the course of performing duties as auditor of the company.
 - ◆ "Performing duties as auditor of a company" includes making a statement of circumstances or a cessation statement upon the resignation or removal of the auditor or when the auditor is not reappointed.

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Auditor's rights (cont'd)

- Outgoing auditor's statement of circumstances
 - ◆ Under s 425(1), the auditor's duty to make a statement of circumstances connected with the cessation of office is extended to situations where the auditor is removed from office and where a retiring auditor is not reappointed.
 - ◆ Currently, such a requirement only applies to a resigning auditor (s 140A Cap 32).
 - ◆ A company is not bound to circulate the statement if the Court is satisfied that the auditor has abused the use of the statement or is using the statement to secure needless publicity for defamatory matter [s 427].

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Auditor's rights (cont'd)

- ◆ The auditor must deliver a copy of the statement to the Registrar for registration within the prescribed time [ss 426(5) and 427(5)].
- Outgoing auditor may provide information to incoming auditor [s 414]
 - ◆ A person who is or has been an auditor of a company does not contravene any duty in law by reason only that the person gives information of which he became aware in the capacity of auditor to another person —
 - (a) who is an auditor of the company;
 - (b) who has been appointed as auditor of the company but whose term of office has not yet begun; or
 - (c) to whom the company has offered the position as auditor but who has not yet been appointed.

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New Offence relating to Inaccurate Auditor's Reports

- If the auditor is of the opinion that the financial statements of a company are not in agreement with its accounting records in any material respect or
- If the auditor has failed to obtain all the information or explanations that are necessary and material for the purpose of the audit
 - ◆ the auditor must state that opinion or fact in the auditor's report
- The offence would be committed if the auditor in question knowingly or recklessly caused any of the two statements to be omitted from the auditor's report [section 408]

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Summary financial reports

- Summary financial report provisions are extended to all companies except those that prepare simplified accounts [s 438]
 - ◆ Currently summary financial report provisions apply to listed companies only (ss 141CA to 141CG Cap 32)
 - ◆ Unless prohibited [s 446], companies have a choice of sending to its members a copy of the summary financial report instead of reporting documents [ss 439, 441, 442]
 - ◆ Companies (Summary Financial Reports) Regulation Cap 622E replaces Companies (Summary Financial Reports of Listed Companies) Regulation Cap 32M.

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Revision of financial statements

- Voluntary revision of financial statements and reports [ss 449 & 450](cf section 141E Cap 32)
 - ◆ Prescribed requirements set out in Companies (Revision of Financial Statements and Reports) Regulation Cap 622F which replaces Companies (Revision of Accounts and Reports) Regulation Cap 32N.
 - ◆ Basic principle – provisions relating to original documents apply to revised documents.

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Major Changes affecting Directors



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Corporate directorship

- Corporate directors are not permitted for public and guarantee companies.
- Private companies must have at least one director who is a natural person. Existing companies have 6 months to comply with the requirement.

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Indemnification of directors against liability to company

- A provision that exempts a director from liability for negligence, default, breach of duty or breach of trust in relation to the company is void.
- The avoidance of a provision that indemnifies a director against liability is extended to include indemnity for a director of an associated company. The scope of permitted liability insurance is also extended to a director of an associated company.
- The new CO provides for permitted indemnity against liability incurred by a director to a third party. The indemnity must not cover liability to pay a fine in criminal proceedings, in defending criminal proceedings in which the director is convicted etc.
- Permitted indemnities must be disclosed in directors' report and copies must be kept and made available for inspection by members.

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Directors' duty of care, skill and diligence

- There is no provision in Cap 32 on the directors' duty of care, skill and diligence. The common law position in HK is not entirely clear.
- Under the new CO, a director must exercise reasonable care, skill and diligence, i.e. the care, skill and diligence that would be exercised by a reasonably diligent person with –
 - ◆ 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"); and
 - ◆ the general knowledge, skill and experience that the director has ("subjective test")
- The duty also applies to a shadow director.

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Ratification of conduct by directors by disinterested members' approval

- No specific provision in Cap 32 on ratification by members' approval.
- Ratification of conduct involving negligence, default, breach of duty or breach of trust is by resolution, disregarding the votes of a member who is a director in respect of whose conduct the ratification is sought, or who is an entity connected with that director or holder of any shares in the company in trust for that director or entity.
- Does not affect the validity of a decision taken by unanimous consent of the members or power of the directors to agree not to sue, or to settle or release a claim made on behalf of the company.

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Transactions with directors or their connected entities

- For public companies the prohibitions on loans and similar transactions are extended to cover a wider category of persons connected with a director. For example, adult children, cohabittees, parents.
 - ◆ Connected entity includes family members, person in cohabitation relationship, associated body corporate, specified categories of trustees and partner.
- Disinterested members' approval of the transaction is required in the case of public companies.
 - ◆ Interested parties: the relevant directors, connected entities and any person who holds any shares in the company in trust for these persons/entities.
- Members' approval is required for directors' employment for a guaranteed term exceeding three years. For public companies, the votes of the director or the person holding shares in trust for him must be disregarded.

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Transactions with directors or their connected entities (cont'd)

- To facilitate business, new exemptions and exceptions are introduced
 - ◆ exemptions from prohibition on loans etc with prescribed approval of members
 - ◆ exception for small loans etc not exceeding 5% of net assets or called up capital
 - ◆ exception for expenditure on defending proceedings etc or in connection with investigation or regulatory action, subject to financial limit and requirements as to repayment
- The criminal sanction in Cap 32 is removed. Civil consequences only -
 - ◆ voidable at company's instance, with exceptions
 - ◆ directors and others liable to account to company
- The prohibitions on payments for loss of office are extended to cover payment to entity connected with director or former director and to payment to director of holding company.

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Transactions with directors or their connected entities (cont'd)

- The ambit of disclosure of material interest in contract of significance with the company is widened
 - ◆ covers "transaction" and "arrangement", instead of just "contract"
 - ◆ for a public company, the ambit of disclosure is widened to include disclosure of material interest of entities connected with director, except interest that the director is not aware of
 - ◆ disclose the "nature and extent" of interest, instead of just "nature"
 - ◆ also covers shadow directors
 - ◆ procedures for declaration of interest are set out

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Major Changes relating to Company Administration



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Introduction of a comprehensive set of rules for written resolution

- Cap 32 does not provide for the procedures for proposing and passing a written resolution.
- Anything that may be done by a resolution passed at a general meeting or class meeting, without any previous notice being required, may be done by a written resolution. Exception - a resolution removing auditor or director.
- A written resolution is passed when all members who are entitled to vote have signified their agreement.

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Introduction of a comprehensive set of rules for written resolution (cont'd)

- Procedure for proposing and passing a written resolution
 - ◆ The directors or members holding 5% of total voting rights may propose a written resolution.
 - ◆ A member who proposes a written resolution may request the company to circulate with the resolution a statement of not more than 1000 words on the resolution.
 - ◆ A company is not bound to circulate the statement if the Court is satisfied that the right is being abused or being used to secure needless publicity for defamatory matter.

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Introduction of a comprehensive set of rules for written resolution (cont'd)

- Written resolutions may be circulated by sending in hard copy or electronic form or by making them available on the website.
- The period for agreeing to the proposed written resolution is 28 days or such period as specified in the articles.
- The statutory provisions do not override any rule of law e.g. the common law principle of unanimous shareholders' consent.
- Articles may provide its own procedures for passing a written resolution provided unanimous members' approval is required.

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Dispensation with the holding of AGM

- Circumstances in which company not required to hold AGM
 - ◆ If everything done by written resolution
 - ◆ Single member company
 - ◆ A dormant company
 - ◆ Members' unanimous resolution to dispense with the holding of AGM in respect of a particular financial year or for subsequent financial years

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Dispensation with the holding of AGM (cont'd)

- Where no AGM is held –
 - ◆ Directors (failing which members) may appoint the company's first auditor for the company's first financial year.
 - ◆ Copy of financial statements and reports to be sent to the members.
 - ◆ Current auditor deemed to be re-appointed unless he declines.
 - ◆ If reappointment declined, members replace retiring auditor at a general meeting.

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Dispensation with the holding of AGM (cont'd)

- AGM is required to be held after dispensation if -
 - ◆ a member requests the company to convene an AGM by giving notice to the company not later than 3 months before the end of the statutory period for holding an AGM.
 - ◆ the unanimous resolution for dispensing with holding an AGM is revoked by an ordinary resolution.

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Engagement of shareholders in decision making

- Under Cap 32 members may request the company to circulate at their expense a proposed resolution for an AGM or a statement relating to any proposed resolution or business to be dealt with at general meeting.
- The new CO provides that the expenses of circulation of the statement and the resolution in relation to an AGM are to be paid by the company if the request is received in time to enable the company to send a copy of the statement or resolution with the notice of meeting.
- Company not required to circulate the statement if the right is abused or is used to secure needless publicity for defamatory matter.

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Lowering the threshold for demanding a poll

- The threshold for members to demand a poll is reduced from 10% (in Cap 32) to 5% of the total voting rights.
- The other threshold of at least 5 members in Cap 32 is retained.

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Clarification of the rights of proxy

- Subject to the articles, 2 members present in person or by proxy form a quorum of a general meeting. Currently Cap 32 requires 2 members personally present to be a quorum.
- A proxy may exercise all or any of the member's rights to attend, speak and vote at a general meeting. Currently Cap 32 allows a proxy to vote on a poll only.
- Subject to the articles, a proxy may be elected as the chairperson of a general meeting. There is no express provision to that effect in Cap. 32.
- Where a proxy put forward by a company is appointed by a member to be his proxy, the new CO requires the proxy to vote in the way specified in the appointment of the proxy.
- The appointment of a proxy is regarded as revoked if the appointor attends and votes at the meeting.
- Multiple proxies are allowed in the case of a company having a share capital.

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