Charltons - Hong Kong Law Newsletter - 16 January 2004

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# The Companies (Amendment) Ordinance 2003 To Take Effect On February 13, 2004

## A. Introduction

The Companies (Amendment) Ordinance 2003 (the **CAO**) is the first of a series of ordinances amending the Companies Ordinance (the **CO**) and will come into effect on February 13, 2004. The CAO implements certain corporate governance reforms recommended by the Standing Committee on Company Law Reform and makes a number of technical amendments. It also simplifies filing requirements and allows electronic processing of information at the Companies Registry in advance of the operation of its Integrated Companies Information System, Phase 1 of which, providing on-line search facilities, is expected to commence in early 2004.

The purpose of this memorandum is to summarise the principal changes introduced by the CAO. Section references are to sections of the CO as amended by the CAO unless otherwise stated.

## B. One Member/One Director Companies

### 1. One Member Companies

The CAO removes the requirement for a minimum of 2 shareholders and permits a company to have just one shareholder (Section 4(1)). This dispenses with the need for nominee shareholdings and should make incorporation by a sole trader easier.

#### Liability of a single member

The CAO repeals Section 31 of the CO which imposes personal liability for a company's debts on a sole member.

#### Entries in register of members (Section 95A)

If the number of shareholders of a company falls to one, a statement that the company has only one member and the date that occurred must be entered in the register of members. Likewise, if the number of shareholders increases from one to 2 or more, an entry that the company has ceased to have only one member and the date that occurred is required.

#### Shareholder meetings

Where a company has only one shareholder, that shareholder can constitute a quorum at general meetings even where the articles contain a provision to the contrary (Section 114AA). A sole shareholder who makes any decision that may be made by a company in general meeting must provide the company with a written record of that decision within 7 days. The written record must then be entered in a book kept for the purpose in the same way as minutes of general meetings (Section 116BC).

#### Contracts with a sole member/director

Where a company enters into an oral contract (otherwise than in the ordinary course of its business) with its sole member who is also its sole director, the company must record the terms of the contract in a written memorandum within 7 days after the contract is made. The written memorandum must be kept in the same place as the minutes of meetings of the directors (Section 162B).

### 2. One Director Companies

The CAO permits a private company to have a sole director who may also be the sole shareholder (Section 153A). A company that is not private must still have at least 2 directors (Section 153).

#### Reserve directors

Where a private company has a sole shareholder who is also the sole director, a reserve director (being a person over 18) can be appointed to act in place of the sole director in the event of his death. Particulars of the reserve director must be sent to the Registrar of Companies.

#### Secretary

A private company cannot have as its secretary (i) its sole director or (ii) a company whose sole director is also the sole director of the company (Section 154).

#### Written record of a sole director's decision

A sole director of a private company who makes any decision that could be made by a meeting of directors must provide the company with a written record of that decision within 7 days. That record must be kept in a book kept for the purpose in the same way as minutes of board meetings.

## C. Further Amendments Relating To Directors

### 1. Removal Of Directors (Section 157B)

Directors will be able to be removed by an ordinary resolution (i.e. a simple majority) instead of by special resolution (i.e. a 75% majority), making it easier for shareholders to remove directors. In addition, special notice must be given of a resolution to remove a director or to appoint a director in place of a director removed at the same meeting.

### 2. Loans To Directors (Sections 157H and 157HA)

The prohibition on a company making a loan to any of its directors, a director of its holding company or to another company controlled by one or more of its directors, or providing a guarantee or security for such a loan, is extended to cover more modern forms of credit, namely:

1. 'quasi-loans': essentially, these are transactions where the company pays a sum owed by a director and the director is then obliged to reimburse the company. An example would be a company's payment of amounts due on a credit card which include items of personal expenditure which the director is then obliged to reimburse to the company; and
2. 'credit transactions': being, in summary, transactions where goods or land are supplied to a director in return for periodical or deferred payments (eg. hire purchase).

The new prohibitions relating to quasi-loans and credit transactions do not apply to private companies unless the private company is part of a group of which another group member is listed.

'Director' is defined to include shadow directors (see paragraph C5 below). In the case of a listed company or company whose fellow group member is listed, the definition of 'director' also includes the spouse, children and step-children of a director and a trustee of any trust of which such persons are beneficiaries.

Transactions excepted from the prohibition are detailed in Section 157HA.

Consequential amendments have been made to require quasi-loans and credit transactions to be reported in the company's accounts (Section 161B). Many existing arrangements may be within the scope of the widened prohibition and should be reviewed to ensure compliance with the CO.

### 3. Indemnity And Insurance Of Officers And Auditors

Amendments to Section 165 CO clarify that the prohibition on a company exempting or indemnifying its officers or auditors from liability for negligence, default, breach of duty or trust applies only to exemptions from and indemnities against liabilities to the company or 'related companies' (ie. a subsidiary, holding company or fellow subsidiary of the company). There is no restriction on a company indemnifying its officers or auditors against liabilities to third parties incurred in performance of their duties.

In addition, new provisions (Section 165(3)) allow a company to provide insurance for its officers and auditors against:

1. any liability to the company, a related company or third party for negligence, default, breach of duty or trust (save for fraud) of which they may be guilty; and
2. any liability incurred in defending any proceedings for negligence, default, breach of duty or trust (including fraud).

As previously, companies are entitled to indemnify their officers or auditors against liabilities incurred in defending proceedings in which judgment is given in their favour or they are acquitted or in connection with a successful application for relief under Section 358 CO.

The effect of the amendments is that companies will be able to offer substantial protection to their directors (including independent non-executive directors) in the form of third party indemnities and insurance.

### 4. Directors Vicariously Liable For Acts Of Alternates

Amendments to Section 153B make a director vicariously liable for any tort committed by an alternate director appointed by him unless the company's articles contain a provision to the contrary. The alternate also remains personally liable for his own acts (Section 153B(2)). Claims will therefore be possible both against the alternate director and the director appointing him.

### 5. Definition Of Shadow Director

Section 2(1) is amended to include a definition of 'shadow director' as 'in relation to a company, a person in accordance with whose directions or instructions the directors or a majority of directors are accustomed to act'. There is a carve out from the definition for a person who gives advice to directors in a professional capacity.

The new definition applies throughout the CO making a shadow director subject to the same liabilities and obligations as an officially appointed director.

## D. Further Amendments Relating To Shareholders

### 1. Personal Right To Enforce Memorandum And Articles

The amended Section 23(1) makes clear that each member of a company has a personal right to enforce the terms of the memorandum and articles of association of the company. Previously the position was unclear due to inconsistent case law.

### 2. Circulation Of Members' Resolutions

The required threshold for circulation of shareholders' proposals is reduced to holders of 2.5% (from 5%) of the total voting rights or not less than 50 (instead of 100) shareholders holding shares on which there has been paid up an average of at least HK$2,000.

### 3. Repeal Of Right To Appeal Amendment Of The Objects Of A Public Company

Section 8 is amended so that the right of holders of not less than 5% of the nominal value of a company's share capital or any class thereof to apply to court to annul an amendment to the objects clause of a company's memorandum applies only to private companies. The right is repealed in respect of public companies.

### 4. Register Of Members

The requirement for the occupations or descriptions of shareholders to be included in the Register of Members is removed (Section 95(1)).

## E. Technical Amendments

### 1. Filing Requirements

#### Written statements to replace statutory declarations and affidavits

Companies will be allowed to file written statements or certificates in specified forms instead of statutory declarations or affidavits. Examples of provisions to which the new provisions apply include Section 47E (financial assistance: relaxation for unlisted companies) and Section 228 (voluntary winding up).

#### Promotion of specified forms

The CAO promotes the use of standard forms prescribed by the Registrar of Companies (the **Registrar**) to simplify the filing process. Approximately 24 new specified forms and 25 revised existing forms will be introduced to cater for the amendments to the CO introduced by the CAO. A new provision also entitles the Registrar to refuse to register forms deviating from the standard forms (Section 348).

Occasions which will require the filing of a specified form include the following:

1. Incorporation of a company (Section 18);
2. Notification of the situation or change in the situation of a company's registered office (Section 92(2));.
3. Notification of a company's change of name (the filing of the specified form replaces the need to file the special resolution); and
4. Notification of consolidation of share capital, conversion of shares into stock etc. (Section 54).

Amendments to Sections 346 to 348 provide for the delivery and storage of information at the Companies Registry in electronic form.

### 2. Reduction Of Share Capital (Section 58)

Amendments to Section 58 streamline the process of reducing a company's share capital. Court approval of a reduction in share capital will no longer be required where the sole purpose of the reduction is to re-designate the nominal value of the shares to a lower amount subject to satisfaction of the following safeguards:

1. the company has only one class of shares;
2. all issued shares are fully paid-up and the amount of the company's net assets is not less than its paid-up share capital;
3. the reduction affects all shares equally;
4. the amount arising from the reduction is not less than the difference between the company's fully paid-up share capital before and after the reduction; and
5. the amount arising from the reduction is credited to the company's share premium account.

### 3. Increase In Share Capital (Section 55)

Where an increase in share capital is effective on a date after the date of the relevant resolution, notice of the increase must be given to the Registrar within 15 days after the increase takes effect. The requirement for a printed copy of the resolution authorising the increase to be filed is removed.

### 4. Return Of Allotments (Section 45)

The period for filing a return of allotments (Form SC1) is reduced from 8 weeks to 1 month. The requirement to include the occupations or descriptions of the allottees is also removed.

### 5. Public Companies: Time Limit For Share Transfers (Section 70)

The period for completion of the transfer of shares, debentures or debenture stock and the issue of certificates in respect thereof is reduced from 2 months to 10 days for public companies unless the conditions of issue of the shares, debentures or debenture stock provide otherwise.

For private companies, the time limit is still 2 months.

### 6. Company Limited By A Guarantee

The incorporation of a company limited by a guarantee with a share capital is prohibited (Section 4(2)).

### 7. Winding-Up Provisions

#### Minimum Debt (Sections 178 and 327)

The minimum debt for which a winding-up petition can be presented is increased from HK$5,000 to HK$10,000 (or such other amount as is prescribed by the Financial Secretary).

#### Notice to Registrar of Appointment of a Receiver, Manager or Liquidator, or of a Mortgagee taking Possession (Sections 87 and 253)

Amendments require the specification of particulars including name, address, ID card or passport number in notices given to the Registrar of the appointment of a receiver, manager or liquidator or of a mortgagee taking possession. Any change in the particulars must also be notified to the Registrar.

### 8. Dormant Companies (Section 344A)

Amendments simplify the procedure for a company to become dormant and remove the requirement for a statutory declaration.

### 9. Register Of Charges (Section 85)

Amendments clarify the procedure for application to the Registrar for entry in the register of (i) a memorandum of satisfaction in respect of a debt wholly or partly paid and (ii) a memorandum that the whole or any part of the property or undertaking the subject of a registered charge has been released from the charge or ceased to be part of the company's property or undertaking. Applications must be in the specified form.

This note is intended as a summary only of the principal amendments to the Companies Ordinance made by the Companies (Amendment) Ordinance 2003. Specific legal advice should be sought in relation to any particular situation.

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**Charltons - Hong Kong Law Newsletter - Issue 10 - 16 January 2004**