

**Bills Committee on
Companies (Amendment) Bill 2002**

**Summary of concerns
(as at 21 October 2002)**

<u>Subject/Clause</u>	<u>Organization/individual</u>	<u>Concern/View</u>
Reducing threshold for shareholders' proposals	Mr David WEBB (CB(1) 2604/01-02)	Support the 2.5% threshold but have reservation on the detail of the 50-holder threshold as it may not be fair to shareholders of companies with low par value relative to market value or net assets per share. Consideration should be given to requiring requisitionists to make a specific deposit to defray costs, at a fixed amount per registered shareholder. The deposit will be refunded if the proposed resolution receives the support of more than 5% by value of shares voted in general meeting.
Removing directors by ordinary resolution	Mr David WEBB Chinese General Chamber of Commerce (CGCC) (CB(1) 2610/01-02(01))	Support the proposal. Not agree to paragraph 7(c) of the Legal Service Division Report (LS 50/01-02) which states that the proposal may affect the readiness of directors to make hard decisions which are unpalatable to investors. Emphasize that decisions which are "unpalatable" to a majority of shareholders are generally decision which are not in their best interest. There may be circumstances where directors of a company have to appoint/remove directors by special resolution which conflicts with the proposed ordinary resolution. Which resolution should then prevail.

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Providing a statutory definition of “Shadow Director”	CGCC	Should specify the extent to and the details of which the threshold for “shadow director” is lowered.
Extending the statutory provisions to cover in generic terms provision of financial assistance to directors	CGCC	The proposal may affect the financial flexibility of some companies, particularly those small and medium enterprises (SMEs) which usually operate on a tight capital.
Permitting the formation of a company by one person	Hong Kong General Chamber of Commerce (HKGCC) (CB(1) 2592/01-02)	Need to address problems arising from the death of the sole shareholder and director.
Authorization of electronic forms of publicity	HKGCC	To consider amending the relevant provisions, including section 74A, to enable the Registrar to approve web-sites as an alternative to newspapers.
Specified forms	Society of Chinese Accountants & Auditors (SCAA) (CB(1) 2658/01-02)	Not able to comment on the impact of the proposed specified forms unless given the chance to review these forms.

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Statutory declaration	SCAA	The proposed replacement of statutory declaration by written statement may give the public a wrong impression that there is a relaxation on the accuracy of information lodged with the Company Registry. Given that accuracy of information is of prime importance to certain sections in the Companies Ordinance, it is necessary for the Administration to assess the social impact of such changes. Meanwhile, the public should be made aware of the consequences of making a false statement.
Clause 2 Definition of “manager” Definition of “shadow director”	Law Society of Hong Kong (LS) (CB(1) 2340/01-02(02)) Lingnan University (LU) (CB(1) 2610/01-02(02)) SCAA Securities and Future Commission (SFC) (CB(1) 2622/01-02(05))	Need to amend the wording to clarify whether “under the immediate authority of the board” includes for example someone who reports directly to the managing director. There may be circumstances that a person occupying a position under the immediate authority of the board of directors may not be called a “manager”. The definition is too general. Many employees of SMEs, particularly those with single director, may become officers as the director concerned normally oversees most of the day-to-day operation of these organizations. Consideration should be given to expressly excluding bank representatives, who make recommendations for improvement of the way the companies should run their business, from the definition.

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	W H Lam & Company (WHL) (CB(1) 42/02-03(01))	Need to have a clear definition for the term “professional capacity”.
Clause 4	WHL	The proposed section 4(1) may run the risk of creating more unnecessary work for the Registrar and other relevant authorities in the event that the only director and shareholder of a company cannot be contacted.
Clause 5	LU	No need to provide for dissenting shareholders to apply to the court to cancel the alteration when the resolution has been passed by the majority. In appropriate circumstances, the dissenting shareholders may invoke section 168A.
Clause 7	Hong Kong Society of Accountants (HKSA) (CB(1) 42/02-03(03))	Suggest to further amend section 22 to extend the period within which the Registrar may direct a company to change its name from 12 months to five years to prevent possible abuses.
Clause 9	LU Federation of Hong Kong Industries (FHKI) (CB(1) 2645/01-02)	The amendment has not added anything new to the existing law since there are many cases which have already clarified the meaning of section 23(1). It is inappropriate to apply new section 23 to cover the situation whereby shareholders, particularly those minority shareholders, in private companies who fail to spell out their rights in joint agreements as this may distort the neutrally applied terms between the shareholders.

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	Institute of Professional Development (IPD) (CB(1) 64/02-03(02))	While welcoming the introduction of the provision which will bring a degree of clarity in respect of the right of shareholders to take direct legal action to enforce the company memorandum and articles, proposed section 23 as drafted is too broad which may give rise to circumstances where enforcement by a minority shareholder is not in the interests of the company. To this end, there is a need to qualify shareholders' statutory right to enforce the provision. Consideration could be given to making the right of action subject to the reasonability of the behaviour of the shareholder in light of the alternative courses of action available. However, any statutory provision giving the court the right to deny the right of action on the basis of an alternative course of action must be carefully drafted so that it does not amount to a statutory injunction against proposed section 23. Perhaps the court should be bound to exercise its discretion in light of all the relevant circumstances.
Clause 10	LU	No need to provide for dissenting shareholders to apply to the court to cancel the alteration when the resolution has been passed by the majority. In appropriate circumstances, the dissenting shareholders may invoke section 168A.
Clauses 14 to 17 and 19 to 23	LS HKGCC	Need to specifically address the consequences of making a false statement. Disappointed that only minor amendments are proposed in relation to share repurchases. A more comprehensive review should be conducted with a view to simplifying the relevant provisions.

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	<p>Hong Kong Institute of Company Secretaries (HKICS) (CB(1) 2622/01-02(04))</p> <p>SFC</p>	<p>There is no provision dealing with the consequences of making a false statement.</p> <p>The consequences of making a false statement are not set out in the Bill.</p>
<p>Clause 25</p>	<p>LS</p>	<p>Suggest to amend sub-clauses (1) and (2) such that notification is still required within 15 days of passing the resolution and, where appropriate, again on the resolution lapsing or becoming unconditional since there may be circumstances where someone searching the public register will want to know the passing of a resolution to increase capital, even if the increase will or may take place at a later date.</p>
<p>Clause 26</p>	<p>Hong Kong Association of Banks (HKAB) (CB(1) 2547/01-02(01))</p> <p>Mr Winston POON,SC (CB(1) 94/02-03)</p>	<p>There should be an additional condition such that court confirmation of a reduction of share capital is not required if no cash is paid out of the company. Otherwise, a court confirmation is required to protect creditors.</p> <p>The clause as drafted seems to permit the reduction of the capital of a company for any purpose, including the elimination of losses, without the sanction of the Court provided that the four conditions set out in the provision are satisfied. This has failed to reflect the intention of the recommendation of the Standing Committee on Company Law Reform to ensure that the capital of a company is maintained for the protection of its creditors.</p>

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Clause 31	WHL	The time limit of 10 business days for the completion of a transfer of shares by a public company is too tight. Suggest to extend the time limit to 15 business days or one month.
Clause 32	LS HKICS	Need to clarify the rationale for removing the requirement for the certificate to state the amount secured, which is a useful information, particularly to creditors. Query why the requirement for the certificate of registration to state the amount secured should be removed.
Clause 33	LS HKAB	Need to clarify the position of a creditor if the company wrongfully files a memorandum of satisfaction. The amendment may give rise to the possibility of a release being entered based on a certificate of the company when in fact the property covered by the charge has not actually been released by the mortgagee or chargee. A certificate of the mortgagee or chargee should be required prior to release.
Clause 38	LS Mr David WEBB Stephenson Harwood & Lo (SH&L) (CB(1) 2622/01-02(01))	Question the need for new section 95A and the consequences in the event of non-compliance. Fail to see the relevance of recording the number of shareholders. The requirement under new section 95A may not be necessary as any transfer or repurchase should have been recorded in the register of members. One can check the number of members in a company by

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		looking at the register.
Clause 42	<p>HKAB</p> <p>Mr David WEBB</p>	<p>It is not possible to have a meeting of one person. Suggest to amend the clause to the effect that a written resolution or record of a decision be treated for all purposes of the Companies Ordinance and any Articles of Association as being equivalent to a resolution passed at a duly convened and quorate meeting.</p> <p>Fail to see the need to provide for a quorum for a meeting of a company having only one member since meetings, by definition, require at least two participants. In this connection, a written resolution of that member will have the same effect as a meeting of shareholders.</p>
Clause 44	<p>HKAB</p> <p>SH&L</p>	<p>Refer to comments in respect of Clause 42</p> <p>A delay of 30 days in filing the written resolution is too long and will be subject to abuse. Suggest to require filing to be done as soon as possible. In line with new section 153C relating to proofs of decisions of single director, consideration should be given to providing that such filing will be sufficient proof of the actions taken by the relevant member.</p>
Clause 53	SCAA	<p>It is expected that many SMEs will have only one director after the enactment of the Bill. As the single director will have total control of the company and the chance of the number of directors being reduced to zero is greatly increased, the remaining officers of the company viz the Secretary or the Manager will have practical difficulties, if not impossible, to put the board back from zero to one. Therefore, it is not fair nor appropriate to hold these officers liable</p>

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		under proposed section 153A(3).
Clause 54	LU SH&L SFC HKSA	<p>Need to clarify the definition of “alternate director”. If the articles of a company provide for the appointment of an alternate director and the board of directors approves the appointment, there is no reason why an alternate director so appointed shall be deemed to be the agent of the director who appoints him, rendering the director concerned liable for any tort committed by the alternate director.</p> <p>Whether the ambit of section 153B should be restricted such that a director will not be liable for the acts of his alternates if he has taken reasonable care to appoint a competent person to act as the alternate and the alternate’s actions which give rise to the liability have been taken independently of the director appointing him.</p> <p>The proposed provision seems to defeat the policy objective of improving the standard of corporate governance by holding directors responsible for the acts and omissions of their alternates.</p> <p>Query the all-embracing nature of the proposed provision since there may be situations in which a company director in practice has no control over the appointment and actions of the person who is his alternate. It is therefore inequitable to make the director vicariously liable for torts committed by his alternate. Besides, the term “alternate director” is not defined under the Ordinance.</p>
Clause 55	HKAB	Refer to comments in respect of Clause 42

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Clause 56	Mr David WEBB	Fail to see the sole director of a company should be prohibited from acting as Secretary of the company. The proposed provision imposes an unnecessary burden on the sole owner and director of a very small business who must find a third party to act as Secretary, which will inevitably incur expenses.
Clause 57	LU HKSA	<p>Instead of calling for a special notice, consideration should be given to specifying a longer notification period if the 14-day notice period is deemed insufficient.</p> <p>To enhance the effectiveness and flexibility of the proposed provision, consideration should be given to allowing the requirement regarding special notice to be waived with the unanimous consent of the members of the company.</p>
Clause 58	HKAB	<p>The phrase “take part” under new section 157H(4) is not clear and can catch a transaction which does not involve any giving of credit to the director concerned. Need to amend the proposed section such that a company is prohibited from taking part in an arrangement if it involves some form of the giving of credit to the director concerned.</p> <p>Need to review the definition of “credit transaction” under new section 157H(7). The way it is drafted can cover transactions which do not necessarily involve any credit, such as ordinary contracts for sale of land and tenancy agreements of property. The former are conditional while rent for the latter is usually payable monthly and in advance, thus do not involve the extension of any credit.</p>

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	<p>SFC</p> <p>FHKI</p> <p>HKSA</p>	<p>New section 157HA does not seem to adequately provide in all cases an exception to the provision of new section 157H(2) or (4).</p> <p>New section 157H(1)(d) does not extend to loans made to a company in which directors of the <u>holding</u> company (of the company making the loan etc) have a controlling interest.</p> <p>The requirement for private companies to first obtain the approval of shareholders before they can make loans to their directors is likely to impair the efficient functioning of companies, particularly those family-owned SMEs. It is therefore recommended that private companies with shareholders' fund below a threshold be exempted from the requirement.</p> <p>Need to clarify whether there is any empirical evidence as to what will constitute a reasonable threshold. If there is a need to specify a ceiling, consideration should be given to devising a formula that will have regard to the size of transactions which are usual for a particular company. Otherwise, the proposed provision may have the effect of preventing companies from entering into a normal arm's length transaction with its directors.</p>
<p>Clause 63</p>	<p>HKAB</p> <p>SFC</p>	<p>Refer to comments on "credit transaction" under section 157H of Clause 58.</p> <p>It is not clear as to who will be deemed to be a person "connected with a director of the company" under new sections 161(B)(1)(b), 3(a) and 12(a)</p>

<u>Subject/Clause</u>	<u>Organization/individual</u>	<u>Concern/View</u>
	HKSA WHL	<p>The proposed disclosure requirements can be unduly onerous and in practice overload financial statements with details that will not be useful to most users. Suggest to adopt the disclosure requirements similar to those in the Hong Kong Statement of Standard Accounting Practice on Related Party Disclosure (SSAP 2.120).</p> <p>Need to clearly define the phrase “a person connected with a director of the company” under section 161B(12)(a) to avoid possible confusion.</p>
Clause 65	HKAB HKSA	<p>Question why the requirement for a company which has only one shareholder and enters into a contract with that shareholder, who is also a director, to set out the contract concerned in a written memorandum which is kept with the company’s books does not apply to contracts entered into in the ordinary course of business.</p> <p>Need to clarify the purpose of introducing new section 162B for companies with one member.</p>
Clause 66	HKAB LU HKSA	<p>It is questionable whether it is correct that the company should be entitled to purchase directors’ and officers’ liability insurance for the benefit of auditors and covering costs of defending proceedings in respect of fraud.</p> <p>Need to clarify the position where a company purchases insurance against any liability to the company on behalf of its officers.</p> <p>Need to clarify the purpose of new section 165(3)(b).</p>

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	<p>Ms Amy YUNG Islands District Council member (CB(1) 42/02-03(02))</p>	<p>The protection under which a company should be allowed to obtain insurance for directors and officers to cover their liabilities to the company and other expenses incurred in defending any proceedings taken against them for negligence, default, breach of duty and trust (including fraud) is too wide for the directors who have fiduciary responsibility towards the company and the shareholders.</p>
<p>Clause 76</p>	<p>LS HKICS SFC</p>	<p>Need to set out the consequences of making a false statement.</p> <p>There is no provision dealing with the consequences of making a false statement.</p> <p>The consequences of making a false statement are not set out in the Bill.</p>
<p>Clauses 79(1) to (5)</p>	<p>LS HKICS SFC</p>	<p>Need to set out the consequences of making a false statement.</p> <p>There is no provision dealing with the consequences of making a false statement.</p> <p>The consequences of making a false statement are not set out in the Bill.</p>
<p>Clause 86</p>	<p>LS HKICS SFC</p>	<p>Need to set out the consequences of making a false statement.</p> <p>There is no provision dealing with the consequences of making a false statement.</p> <p>The consequences of making a false statement are not set out in the Bill.</p>

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Clause 108	HKSA	Need to clearly define the phrase “electronic means” by reference to examples of more common modes of communication.
Others	Baker & McKenzie (CB(1) 2622/01-02(02)) Consumer Council (CB(1) 2622/01-02(03)) FHKI	Comments mainly on drafting aspect which shall be considered during the clause-by-clause examination of the Bill. Consideration should be given to including in the Bill a provision to abolish private company corporate directors. This will assist in identifying the actual persons responsible for the actions of companies. Express concern that the proliferation of new regulations on business will not only incur additional compliance cost on companies, particularly those SMEs, but also erode their competitiveness in the world market. Caution that an overly regulated business environment will defeat the entrepreneurial spirit and deter overseas investors from setting up companies in Hong Kong.