Bills Committee on Companies (Amendment) Bill 2002

Follow-up actions arising from the discussion at the meeting on 3 April 2003

Introduction

This paper sets out the outcome of the follow-up actions arising from the discussion at the meeting on 3 April 2003.

(a) Speech for the resumption of Second Reading debate on the Bill

2. We agree to include in the speech to be delivered by the Secretary for Financial Services and the Treasury (SFST) at the resumption of Second Reading debate on the Bill an undertaking that the policy and drafting of section 157I would be looked at by the Administration and referred to the Standing Committee on Company Law Reform (SCCLR) taking into account Members' views and the UK equivalent of such provision.

3. As regards the issue of cost implications for requisitionists, it would be addressed in the consultation paper to be issued by the SCCLR on Phase II of its Corporate Governance Review in May/June 2003 and a decision is expected to be made in early 2004. This timetable will be included in SFST's speech.

(b) Returns on Allotments

4. The experience of the Companies Registry (CR) is that most companies deliver their returns of allotment of shares to CR for registration within 2 to 4 weeks after the allotment. Hence, we do not expect companies to have major difficulties in complying with the requirement of filing the returns within one month as proposed in the new section 45(1). It is worth noting that the same filing period is adopted in the UK, Australia and Singapore.

(c) Punishment

5. The punishment, where applicable[1], for failure to comply with the requirement of filing a statutory declaration or an affidavit under certain sections will not be amended by the Bill. For example, the punishment for failure to file a statutory declaration under section 47E, i.e. a maximum fine at level 5 (i.e. $50,000) and a maximum daily default fine of $1,300, will remain unchanged.

6. At present, the Companies Ordinance does not provide for punishment for the making of a false statutory declaration. We rely on section 36 of the Crimes Ordinance (Cap. 200), which provides that any person, who knowingly and wilfully makes (otherwise than on oath[2]) a statement made in a statutory declaration false in a material particular, may be prosecuted and, if convicted, subject to a fine[3] and a maximum imprisonment of two years.

7. With the filing requirements of a statutory declaration or an affidavit being replaced by a written statement as proposed in the Bill, we will rely on section 349 of the Companies Ordinance, which provides that any person in any return, report, certificate, balance sheet or other document required by or for the purposes of any of the provisions of the Ordinance wilfully makes a statement false in any material particular, knowing it to be false, may be prosecuted and, if convicted, subject to a maximum penalty of $100,000 and maximum imprisonment of 6 months.

8. The purpose of section 349 is to provide a deterrent against making a false statement, thereby encouraging a culture of compliance with the filing requirements under the Companies Ordinance. The offence in question is more in the nature of an offence of dishonesty rather than a regulatory offence. Where the circumstances justify, separate offences relating to making a statutory declaration (to be replaced by a written statement) are provided for in certain provisions of the Ordinance. For example, section 49K(6) provides

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[1] No punishment is imposed for failure to comply with the requirements of filing a statutory declaration or an affidavit under certain sections. For example, section 233(2)(a) provides that the statutory declaration shall have no effect for the purposes of the Companies Ordinance unless it is made within 5 weeks prior to the passing of the relevant special resolution and is filed with the CR within the required time limit.

[2] If any person being required or authorized by law to make any statement on oath for any purpose and being lawfully sworn (otherwise than in a judicial proceeding) wilfully makes a statement which is material for that purpose and which he knows to be false or does not believe to be true, he shall be guilty of an offence and shall be liable on conviction upon indictment to imprisonment for 7 years and to a fine under section 32 of the Crimes Ordinance (Cap. 200).

[3] Section 101F(b) of the Criminal Procedure Ordinance (Cap. 221) provides that if the amount of fine is unspecified, then it shall be implied that such offence shall, without prejudice to any law against excessive or unreasonable fines or assessments, be punishable by a fine of any amount.

that a director, who makes a statutory declaration relating to the redemption of shares under section 49K without having reasonable grounds for the opinion expressed in the declaration is subject to a maximum penalty of $125,000 and maximum imprisonment of 2 years (on indictment) or a maximum penalty of $50,000 and maximum imprisonment of 6 months (on summary prosecution). The punishment for the separate offences will remain intact in the Ordinance.

9. Having regard to the purpose of section 349 and the separate offences in relation to making a statutory declaration in the Ordinance where the relevant circumstances justify, we have taken the view that the existing level of punishment under section 349 (i.e. a maximum penalty of $100,000 and maximum imprisonment of 6 months) is adequate.

(d) Committee Stage Amendments to clause 26

10. In drafting the Committee Stage Amendments (CSAs) to clause 26, we have regard to the concern that this clause should not dispense with the court's confirmation of a reduction in share capital arising from a permanent loss in the share capital. The CSAs as presently drafted make it clear that the court's confirmation can be dispensed with if the sole purpose of the reduction is to re-designate the nominal value of the shares of the company to a lower amount, and the amount arising from the reduction to be credited to the share premium account is not less than the amount representing the difference between the amount of the company's fully paid-up share capital immediately before the reduction and the amount of its fully paid-up share capital immediately after the reduction ("the difference").

11. If there were a permanent loss in the share capital in the first place, the amount arising from the reduction to be credited to the share premium account would be less than the difference[4]. Since this requirement cannot be met, the court's confirmation of the reduction cannot be dispensed with by virtue of this clause. This notwithstanding, we are prepared to consider any suggestion on the wording of the CSAs to put matters beyond all doubt.

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[4] Assuming that a company has issued a total of ten shares, each of which has a par value of $10 and all these shares are fully paid up, the company's fully paid-up share capital is $100 (i.e. $10x10). If the company redsignates the par value of its shares to $2, the total fully paid-up share capital after the reduction will be $20 (i.e. $2x10) and the reduction in the share capital arising from the redesignation will be $80 (i.e. $100 - $20). However, if there were a loss of $50 in the capital in the first place, the reduction to be credited to the share premium account would be $30 (i.e. ($100 - $50)-$20). As such amount is less than the difference of $80, such reduction cannot satisfy paragraph (e) of new section 58(3).

(e) New section 114AA

12. It has been a well-established principle that one person does not make a meeting *(Sharp v Dawes[1876] 2 QBD26)*. However, where special circumstances exist[5], the court has ruled that a meeting with one member could be validly held. With the introduction of one-member companies in the Bill, we consider it necessary to include new section 114A to provide that in the case of such companies, one member present in person or by proxy shall be a quorum of a meeting of the company. The wording of this section is basically the same as that in section 370A[6] of the UK Companies Act 1985.

(f) New clause 44

13. This clause is drafted on the basis of section 382B of the UK Companies Act 1985. It aims to cover the types of decision the courts have held may be taken by the member(s) unanimously without the need for a formal meeting of the company or a written resolution. These are decisions made under circumstances where the principle in *Re Duomatic, Ltd [1969] 1 All ER 161*[7] (the Duomatic principle) applies. In the case of a one-member company, if no other person is entitled to receive a notice of a general meeting, by virtue of the Duomatic principle, the solitary decision of the sole member is tantamount to a decision of the company. In other words, there is no need for a formal meeting or the passing of a written resolution. However, where decisions of the company are required to comply with certain procedures that persons other than members of the company are entitled to attend general meetings[8], it appears that the company should hold a formal meeting unless it is clear that the Duomatic principle applies.

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5 For example, in *East v Bennett Brothers, Ltd. [1911] 1 ch 163*, the company's memorandum authorized changes in the capital structure with the sanction of an extraordinary resolution of the holders of the shares of any class affected, passed at a separate meeting of such holders. The court held that the single holder of all the preference shares was capable of constituting a meeting.

6 Section 370A of the UK Companies Act 1985 provides that notwithstanding any provision to the contrary in the articles of a private company limited by shares or by guarantee having only one member, one member present in person or by proxy shall be a quorum.

7 In *Re Duomatic, Ltd [1969] 1 All ER 161,* the directors, who were also the only ordinary shareholders having a right to attend and vote at general meeting, had drawn remuneration which was subsequently shown in accounts which they had, as directors, approved. That was challenged in the subsequent liquidation on the ground that it had never been sanctioned by a general meeting. The court held that although the directors did not take the formal step of constituting themselves a general meeting of the company and passing a formal resolution approving the payment of directors' salaries, at the time of approving the accounts, they did apply their minds to the question and accordingly, their consent should be regarded as tantamount to a resolution of a general meeting.

8 For example, the existing section 132 of the Ordinance with regard to the removal of auditors.

14. There has been concern that this clause would have the effect of requiring the sole member of a company to file with the company any decision that he has made even though such decision is of a minor nature e.g. the coffee brand to be used in the company. In practice, a company usually confers general management powers on its directors through its articles of association and it is therefore unlikely that its members would need to decide on issues of a minor nature.

15. In the event that the sole member wishes to do so[9], the decision so made is no different from a decision made at a general meeting. It follows that a written record of such decision should be filed with the company just as a decision made at a general meeting is recorded in the minutes of the meeting. This is not an absurdity but is simply a restatement of the basic principle of the company law i.e. a company is an entity established by process of law in order to be a nominal, artificial party to legal relationships. The company and its members are two separate entities and this should be so even if the company has only one member.

16. We are considering whether the company should be required to keep the records filed under this clause in a book as if they were the minutes of general meetings.

Financial Services Branch
Financial Services and the Treasury Bureau
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[9] The sole member can recoup the power from general management by amending the company's articles of association. Otherwise, by reason of the principle laid down in Automatic Self-Cleansing Filter Syndicate Company Limited v. Cuninghame [1906] 2 Ch 34, where powers have been vested in the board of directors, the company in general meeting cannot interfere with their exercise.