LC Paper No. CB(1)644/99-00

Ref: CB1/ BC/11/98/2

Bills Committee on
Companies (Amendment) Bill 1999

Minutes of meeting held on
Tuesday, 20 April 1999, at 2:30 pm
in Conference Room B of the Legislative Council Building

Members present	**:**	Hon Albert HO Chun-yan (Chairman) Hon Kenneth TING Woo-shou, JP Hon James TIEN Pei-chun, JP Hon Eric LI Ka-cheung, JP Hon HUI Cheung-ching Hon CHAN Yuen-han Hon SIN Chung-kai Hon Mrs Miriam LAU Kin-yee, JP Hon FUNG Chi-kin
Members absent	**:**	Hon HO Sai-chu, JP Hon CHAN Kam-lam
Public officers attending	:	**Agenda item II** Miss Julina CHAN Principal Assistant Secretary for Financial Services Mr G W E Jones Registrar of Companies Mr E T O' Connell Registry Solicitor Ms Shandy LIU Senior Government Counsel Mr G A FOX

Senior Assistant Law Draftsman
Department of Justice

Miss TSE Woon-ping
Chief Assessor
Inland Revenue Department

Mrs TANG LI Suk-yee
Senior Assessor
Inland Revenue Department

Attendance by invitation : **Agenda item I**

The Hong Kong Institute of Company Secretaries

Mr Peter C TASHJIAN
Chief Executive

Mr John WONG
Treasurer

Agenda item II

Miss Winnie CHEUNG
Director of Professional Practices
Hong Kong Society of Accountants

Clerk in attendance : Ms Estella CHAN
Chief Assistant Secretary (1)4

Staff in attendance : Miss Anita HO
Assistant Legal Advisor 2

Ms Connie SZETO
Senior Assistant Secretary (1)1

I Discussion with deputation
(LC Paper Nos. CB(1)1133/98-99(01), (03) and 1143/98-99(01))

Members noted that amongst the organisations which had made submissions on the Bill, the Hong Kong Institute of Company Secretaries (HKICS) would be represented at this meeting to discuss the Institute's views. The Administration's response to Hong Kong Managers and Secretaries Limited's submission was tabled at the meeting (and subsequently issued vide LC Paper No. CB(1)1259/98-99). While Hong Kong Bar Association did not have any comment on the Bill, the Law Society of Hong Kong had suggested a drafting amendment on the Bill which was accepted by the Administration.

Meeting with the Hong Kong Institute of Company Secretaries

2. Upon the Chairman's invitation, Mr Peter TASHJIAN of HKICS presented HKICS' views on the Bill. He said that HKICS supported the Bill in general. However, HKICS was of the view that the requirement to obtain a 'no-objection' notice from the Commissioner of Inland Revenue (CIR) prior to seeking application under the proposed new procedure for deregistering solvent, defunct private companies was neither necessary nor cost effective despite the Inland Revenue Department (IRD)'s pledge to complete the process within one month or even a shorter time frame. He explained that the existing and proposed safeguards as detailed in the Institute's submission would be sufficient to protect the interest of creditors and other affected parties. These safeguards included, inter alia, criminal and civil liability of directors, corporate officers and members of companies under the Common Law, restricted scope of the new procedure to defunct private companies, special power vested with Registrar of Companies (R of C) under the Ordinance, continuation of liability upon company dissolution, and court intervention. Moreover, IRD could raise objection to the proposed striking-off of companies during the three-month gazette notice period. Although it had been regarded as the best practice to obtain tax clearance from IRD before companies proceeded with the deregistration process, HKICS considered it inappropriate to legislate for such a requirement as best practices should not be codified in law, which would have the disadvantage of reduced flexibility. In order to strengthen the proposed safeguards, consideration could be given to extending the gazette notice period of proposed striking off of companies, the period of cessation of business requirements, and the period required for keeping relevant books and records of companies.

3. Mr John WONG of HKICS supplemented that practitioners in the field had been following the best practice. If additional safeguards were considered necessary, it would be more advisable to stipulate the requirement in the form of guidelines and circulars to be issued by the R of C for relevant professionals and practitioners.

II Discussion with the Administration

'No-objection' notice from the Commissioner of Inland Revenue

4. The Principal Assistant Secretary for Financial Services (PAS/FS) explained that the tax clearance procedure was an integral part of the proposed new deregistration procedure which aimed to provide a fast, simple and inexpensive option to voluntary winding-up of companies and helped to stop further abuses of the striking-off provisions under sections 290A and 291 of the Companies Ordinance (the Ordinance). However, the provision of this simplified procedure had to be balanced by the Government's need to protect public revenue. In respect of existing statutory provisions to safeguard the interests of creditors etc., such remedial actions as making recourse to the court to redress the position, the lengthy process of reviving a company and taking action against its officers were both time-and resource-consuming, and would be at the expense of public money. Moreover, notwithstanding that professionals and practitioners had been following the best practice to obtain tax clearance before applying for striking-off on behalf of their client companies, it was envisaged that under the new simplified procedure, most of the companies that subscribed to the service would submit their deregistration applications without seeking service from practitioners. Hence, the specific statutory provision was considered the most effective and efficient means of revenue protection. She added that in the financial year 1998-1999, the Companies Registry (CR) received a total of 1,305 objections from IRD to section 291 strike-offs which represented 8.3% of all companies struck off during the period and this was a significant proportion by any standard.

5. R of C supplemented that although there was no specific requirement of IRD tax clearance under the liquidation procedure, section 265 of the Ordinance stipulated that all statutory debts due to the Hong Kong Special Administrative Region Government by a company was a preferential debt in winding up. Hence, the proposed 'no-objection' notice from IRD did reflect the same principle of revenue protection under the existing provisions relating to liquidation of companies.

6. Some members shared the concern of HKICS and questioned the need of the 'no-objection' notice. Mr Eric LI Ka-cheung said that apart form increasing the cost of the new deregistration procedure as a fee would be charged by CIR for issuance of the notice, the requirement might protract the process of deregistration. He doubted whether the 1,305 objections raised by IRD were all related to outstanding tax liabilities. Mr James TIEN Pei-chun enquired about the types of tax owing and the amount involved in the 1,305 objection cases. Mrs Miriam LAU Kin-yee asked about the basis of the proposed fee of $350 for issuance of the notice.

7. In response, R of C explained that in accordance with the existing deregistration procedure under sections 291 and 290A, the Registrar was required to publish a three-month notice of the names of companies intended to

be struck off in the Gazette and affected parties could raise objections during the period. The 1,305 objections from IRD were raised in response to the Gazette notice. As regards the types of outstanding tax and amount involved in these cases, the Chief Assessor, Inland Revenue Department (CA/IRD) said that according to information available at hand, the average amount of 'tax at risk' for ten of these cases was estimated to be $1.8 million. She added that the types and amounts of outstanding tax involved varied with the nature of the business of the company. Past experience revealed that substantial amounts of profits tax was owed by single transaction companies dealing with properties. Upon members' request, she undertook to provide an analysis of the 1,305 objection cases and

Admin information regarding the types of tax owing and the amount involved.

8. On the concern about the cost burden of the proposed 'no-objection' notice on small companies, R of C said that the total fee of $770 comprising $350 for the issuance of the notice and $420 for the deregistration service was much lower than the current fee payable to professionals for voluntary winding-up service and should be affordable by companies. PAS/FS reiterated that the new deregistration procedure would help to stop further abuses of the striking-off provisions under sections 290A and 291 where the service had been provided by the Administration at the expense of public money. The proposed fee of $350 was set at a level adequate to recover IRD's full cost of providing the new service. IRD had assured that if an application was initially rejected because of outstanding tax liabilities, the applicant could, once those liabilities were cleared, asked that the application be reconsidered. No further fee would

Admin be charged for this re-consideration. At members' request, CA/IRD agreed to provide a cost analysis of the $350 application fee for the 'no-objection' notice.

9. As regards the concern that the requirement of the 'no objection' notice would protract the process of deregistration, Mr James TIEN noted IRD's performance pledge of providing a response to such application within one month. He further asked whether a 'no- objection' response could be assumed if no reply was received from IRD within a month after submission of the application so that applicants could proceed with the deregistration process as early as possible.

10. In response, CA/IRD re-iterated that due to increased application of information technology in searching outstanding tax liabilities of companies, IRD would be able to make a response to applications in about a month. For non-complicated cases, an 'no-objection' notice could be issued within the one-month period. If further information was required for processing of applications, the applicants would be informed as soon as possible. Moreover, reasons for objections would be provided in the replies so that applicants could seek reconsideration of the applications as early as possible once they had cleared the outstanding liabilities. However, the suggested assumed 'no-objection' response after submitting the application for one month would create operational problems

and inflexibility for IRD and hence was considered inappropriate. She stressed that IRD would strive to observe its performance pledge and issue the 'objection' or 'no-objection' notice to applicants as early as possible.

11. On the Chairman's enquiry about the possibility of Government taking legal actions against companies seeking deregistration under the new procedure for failure to comply with requirements stipulated in the Ordinance on companies incorporated with limited liability, R of C said that while prosecution against breaches of the Ordinance would be considered in the light of individual circumstances, this would not delay the process of application for deregistration. The Registry Solicitor added that currently the majority of prosecutions were targeted at corporate directors who failed to file annual returns. These returns gave details about the directors, registered office of a company etc. which the Company Registry considered important information useful to the public. Moreover, the Registry would investigate into complaints and consider taking legal actions against companies which failed to keep audited accounts if it was considered in the public interest to do so.

Merger Relief

12. At the invitation of the Chairman, Miss Winnie CHEUNG of the Hong Kong Society of Accountants (HKSA) said that HKSA was in full support of the Bill in respect of provisions relating to merger relief. She explained that Hong Kong's legal framework when compared with many other jurisdictions was very restrictive in this area and as a result, businesses had been pushed to using overseas companies as vehicle for undertaking merging and acquisition activities and business reconstruction. As regards practices in other jurisdictions, Miss CHEUNG said that Singapore in 1987 and Malaysia adopted the same merger relief provisions in the UK Companies Act. For the United States and Canadian regimes, the "par value" and "legal capital" concepts had long been abandoned as it was recognised that capital maintenance requirements offered little protection to creditors and shareholders. Instead, reliance was placed on the use of a solvency test to assess the ability of a company to distribute assets and profit and for reduction of capital. The issue of merger relief, therefore, had become irrelevant. Such similar provisions were incorporated in the Australian Corporation Law in 1998.

13. Responding to the Chairman's enquiry, Miss CHEUNG explained that if Hong Kong was to follow the US or Canadian model, it would need to introduce a major reform in its corporation laws in order to strengthen the corporate governance regime and to give the necessary discretionary powers to corporate directors. The matter had been under discussion by the Standing Committee on Company Law Reform (SCCLR) as a longer term issue. PAS/FS supplemented that the comprehensive review by the consultant of the Ordinance had been completed and the Consultancy Report was released in March 1997. The Report

recommended that the legal framework for companies be amended to move away from the existing UK-based model towards the US and Canadian regimes. SCCLR was examining the Report and would submit its recommendations by end of 1999-2000.

Drafting aspects of the Bill

14. Members noted that the Legal Services Division had sought clarifications from the Administration on some legal and drafting aspects of the Bill. The relevant correspondence was circulated vide LC paper No. CB(1)1143/98-99(02). Noting the Assistant Legal Adviser 2 (ALA2)'s advice, members were concerned about clause 5 of the Bill where it was stated in the proposed section 48F (3) that "Where there is any conflict between any of the provisions of sections 48B to 48E and any of the provisions of regulations made under this section, the second-mentioned provision shall prevail over the first-mentioned provisions." As advised by ALA2, members noted that this section meant that the provision of regulation would prevail over the Ordinance and might contravene section 28(1)(b) of the Interpretation and General Clauses Ordinance (Cap. 1), where it was stated that "no subsidiary legislation shall be inconsistent with the provisions of any Ordinance". ALA2 pointed out that this proposed section 48F(3) was not found in the UK Companies Act and in UK, the draft regulation so made had to be passed by the Parliament. She drew members' attention that there was also inconsistency between the proposed section 48F(3) and section 49Q(4) of the Ordinance where it was stated that "No regulation shall be made under this section unless a draft of them has been laid before and approved by resolution of the Legislative Council...".

15. In view of the concern expressed, PAS/FS undertook to propose a Committee Stage amendment to provide that regulations to be made under section 48F had to be approved by way of positive vetting by the Legislative Council.

II Any other business

16. Members agreed to hold the next meeting on 7 May 1999, at 8:30 am.

17. The meeting ended at 4:20 pm.

Legislative Council Secretariat
20 December 1999