The British
Chamber of Commerce
in Hong Kong

香港英商會

02 October 2008

(E Mail: co_rewrite@fstb.gov.hk)

Companies Bill Team (Attn: Ms Jasmine So)
The Financial Services & The Treasury Bureau
15/F, Queensway Government Offices,
66 Queensway,
Hong Kong

Dear Ms So

Third Companies Ordinance Consultation

We are pleased to attach our submission on the captioned consultation which represents the views of our membership. We would underline the comment that there should be no legislative control over the setting of the issue price - there is no such control at the moment when shares are issued at a premium over par. We hope that these comments will be of use and we stand ready to respond to further questions as they arise.

Yours sincerely

James Riley
Chairman

Third Companies Ordinance Consultation Responses - to Companies Bill team.

1. Do you agree that Hong Kong should adopt to a mandatory system of no-par for all companies with a share capital?

This is a difficult question. Hong Kong has over 650,000 companies on the register, who will need to operate under the proposed no-par regime, were it to become mandatory. The countries who have adopted no-par so have far fewer incorporations (i.e. Singapore, New Zealand , Australia) and all require an individual director to be resident in the jurisdiction (this is not something we suggest for HK , as raised in our previous submission relating to the second companies ordinance consultation). As long as existing companies, some of who have share premium accounts are properly catered for , it may be possible to move to a mandatory no -par share system. However, a mandatory no-par system is less flexible, in terms of there being less choice, than in a system which has both a par value and a no-par value regime open to individual choice. To move 650,000 companies to the proposed new no-par share regime when perhaps only 10,000 really need it is the big question. Is that the right thing to do? Furthermore certain compaines may find that they have some use for share premium account and / or capital redemption reserve.
We think it will take a long time to move to a no-par share regime in the UK, as they are waiting for an amendment to the EU capital rules.

2. Do you agree that a period of about 12 months would be reasonable for companies to review their arrangements before migration to no-par? If you think another period more appropriate, please specify what that is and your reasons.

See our comments in 1 above – we would strongly prefer no-par to be optional rather than mandatory. 12 months is too short. 24 months allows time for companies with a long accounting period to be accommodated. This is anyway a very significant change to the regime affecting share capital in HK; we would also like time to consider in detail the drafting of the statutory deeming provision mentioned in the Consultation Document ("CD"). I.e. the concept that share capital and share premium (or, capital redemption reserve) will be merged into and treated as one, after the change to no-par.

3. Do you agree that there should not be any legislative control over the setting of the issue price of the no-par shares?

If we move to no-par, there should be no legislative control. The share issue price would be a matter for the director(s). In practice the extensive number of HK shelf companies incorporated will probably continue to have 1 share issued at say HK$1. Shelf companies do not exist in the same way in Singapore, New Zealand or Australia, as in Hong Kong. Any problem regarding this area may mean that offshore shelf companies (ie British Virgin Island companies) will become more user friendly than Hong Kong companies. We would always prefer measures which encouraged the use of Hong Kong companies over companies from other jurisdictions

4. Assuming the abolition of par value while the existing capital maintenance rules are largely maintained, do you favour:
(a) The abolition of the merger relief; or
(b) Its application to the amount in excess of the subscribed capital of the acquired company attributable to the shares acquired or cancelled; or
(c) Some other alternatives (please specify)?
Please provide reasons.

We prefer (b). - Merger relief applied to the excess attributable to the shares acquired or cancelled, so excessive relief is not given.

5. Assuming the abolition of par value while the existing capital maintenance rules are largely maintained, do you favour:
(a) The abolition of the group reconstruction relief; or
(b) Its application to the excess of the consideration for the shares over the base value of the assets transferred; or
(c) Some other alternatives (please specify)?
Please provide reasons.

We prefer (b), analogous to the position at 4.

6. Do you agree with, or have any comments on, the proposals outlines above on:
(a) Capilisation of profits with or without an issue of shares;
(b) Issuance of bonus shares without the need to transfer amounts to share capital;
(c) Consolidation and subdivision of shares; and
(d) Redeemable shares.

(a) We agree that profits should be able to be capitalised with or without an issue of shares. The capital reserve would not be distributable. Arguably the capital reserve arising from such capitalization of profits should be distributable subject to a solvency test (as for example is the contributed surplus for Bermuda companies).
(b) We agree that bonus no-par value shares should be able to be issued without increasing share capital (this question does not really make sense in relation to par value shares).
(c) We agree shares should be able to be consolidated or subdivided.
(d) We agree that shares which are redeemable should be possible.

7. Do you agree that the requirement for authorised capital should be removed?

We think companies should retain the option for the provision for authorised capital (in terms of number, not value, in the case of no-par value shares) in their Memorandum and Articles of Association, for the reason of flexibility.

8. Do you see value in companies having a choice whether to retain or delete the authorised capital from their Articles of Association?

Existing companies should be able to retain or delete the authorised share capital provision.

9. Do you see value in retaining the option of having partly paid shares? Please provide reasons.

It should still be possible to have partly paid shares.

10. Do you agree that the amount unpaid on partly paid shares should be defined by reference to the issue price, without a need to distinguish between shares issued before and after migration to no-par?

The unpaid part would be by reference to the issue price for no-par value shares and by reference to the par value otherwise. There would be no need to distinguish partly paid shares issued prior to the change to no-par.

11. Where partly paid shares without a par value are subdivided, do you agree that there should be reallocation (by legislation) of the outstanding liability on existing shares to the new shares to maintain the pre-existing ratios?

Where partly paid shares are subdivided it should be made clear by legislation that the unpaid part/liability is reallocated accordingly, to maintain pre- existing ratios.

12. Do you agree that Hong Kong should NOT adopt the solvency test approach to creditor protection which applies to all forms of distribution? Please provide reasons.

We still like the Capital Maintenance Approach. At the end of the day investors like to know what they would get back, for their shareholding. We would note that the solvency test approach is also common in popular competitor jurisdictions to Hong Kong such as Bermuda, which allows both no-par and par value shares and which is not mentioned in the C.A.

13. Should the solvency test currently used in Hong Kong (which is basically a cash flow test) be modified by including a balance sheet test?

Where a solvency test applies we think it should comprise both a cash flow test and a balance sheet test i.e. so that the company has a positive cash flow and a positive net worth before certain actions are taken .

14. Do you agree that reduction of capital should continue to be subject to judicial control and there is <u>no</u> need to introduce a court-free procedure as an alternative process in addition to the current rules?

We would like to see a Court free procedure for reduction of capital introduced, in addition to the Court based procedure which the directors could always choose in complex or uncertain cases, or where some of the directors cannot agree.

15. If your answer to Question 14 is negative (i.e. you think that an alternative court-free process for reduction of capital should be introduced):
(a) Should it be available to all companies (whether listed or unlisted) or just private companies or private and unlisted public companies; and
(b) Should all directors make the solvency declaration, or is it sufficient for the majority to do so?

(a) The Court free procedure should be available to private and unlisted public companies only .
(b) All directors should make the solvency declaration. If all directors do not, the Court procedure could then be adopted... This can be the subject of abuse where there is only one (unreliable) director so some safeguards are needed for this scenario.

16. Should the current provisions on buy-backs in relation to protection of creditors be:
(a) retained;
(b) amended to allow public companies (whether listed or unlisted) to fund buy-backs from capital subject to the solvency and other procedural requirements currently applicable to a buy-back out of capital by private companies;
Or
(c) amended to allow all companies (whether listed or unlisted) to fund buy-backs (regardless of the source of funds) subject to a solvency requirement (in a manner similar to that of the SCA)?

We would prefer the current position to apply i.e. (a).

17. Is there a case for legislating for treasury shares for all companies (as in Singapore)?

Companies should have the option to have Treasury shares, i.e. buy back shares and not cancel them. Treasury shares are useful in a number of cases. (e.g. for employee share schemes). Choice would be the key here. But it should not be for all companies , as most companies would not need this in Hong Kong.

18. Should the current financial assistance provisions be streamlined in a manner similar to the NZCA?

No. We do not see a need to follow the New Zealand approach on financial assistance provisions, here.

19. If your answer to Question 18 is in the negative, would you prefer instead:
(a) the current provisions be retained;
(b) the prohibition of financial assistance be abolished in respect of private companies (as the UK has done); or
(c) making solvency an additional exception to the prohibition for all companies (whether listed and unlisted) in a manner similar to the SCA?

We prefer (b) - that the prohibition on financial assistance be abolished in the case of all private companies., as is now the case in the UK.

20. Do you consider that there is a need for Hong Kong to have a court-free statutory amalgamation procedure, in addition to the existing court-sanctioned procedure?

Yes we prefer flexibility - there should be a Court free statutory amalgamation procedure available, in addition to the possibility of instead choosing the court -sanctioned procedure. We would note that there is no concept of "amalgamation" or "merger" per say under Hong Kong law or common law and hence we assume that the question is referring to a statutory scheme of arrangement procedure.

21. If your answer to Question 20 is positive, should the court-free statutory amalgamation procedure be based on the elements outlined in Table A above? If you think that there should be alternative or additional elements, please explain.

The court -free procedure can be based on the approach set out in Table A in the CD.