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**LAW OF
COMPANIES
IN HONG KONG**

FOURTH EDITION

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This is not an easy time to launch a new book on Hong Kong Company Law with the new Companies Ordinance (Cap.622) to be brought into operation in the first quarter of 2014 (3 March 2014). The authors are to be congratulated on the skill with which they have weaved the new provisions of the new Companies Ordinance (Cap.622) into the text, in appropriate cases giving the legislative background to the changes.

Thus, this publication will remain current even when the new law (Cap.622) comes into operation in 2014.

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1. INTRODUCTION

This chapter provides an introduction to companies and the regulation of companies in Hong Kong. The chapter introduces the concept of a company, distinguishing a company from other business associations. The chapter also discusses the scope of company law and its historical development, and outlines the current structure or framework for the regulation of companies in Hong Kong. Finally, the chapter also provides an introduction to legal theories on company law.

1.001

2. COMPANIES AND THE SCOPE OF COMPANY LAW

2.1 Companies in society

Main uses of company vehicle. The traditional concept of a company is a particular type of association of persons, but today it is possible for both a group of persons and a sole individual to constitute a company. In Hong Kong, as elsewhere in the industrialised world, companies have become a common and important feature in commerce and society generally. Some of the main uses of companies are as follows:

1.002

- Vehicle for carrying on trade or business. Companies are commonly used for the purpose of business.¹ Large businesses are invariably carried on through a company, while companies are also the dominant business vehicle for small businesses.
- Holding of property. Purchasers of residential or commercial property in Hong Kong sometimes do so by way of using a company. When the persons who own the company later wish to have the property sold, then this can be done by way of a sale of all the shares in the company to the new purchaser instead of selling the land itself. Previously, there could be savings on stamp duty where a company is used to acquire land as the rates of stamp duty for sale of shares were lower than for sale of land. However, this is no longer the case for new acquisitions of land.²

¹ As at 2012, about 85% of businesses in Hong Kong are in the form of a company: S H Goo, *Study Report on History of Company Incorporation in Hong Kong – A Study Commissioned by the Companies Registry* (July 2013) 48. On the use of a company as a business vehicle, see further para.1.024 below.

² Where a foreign company is used, no stamp duty is payable in Hong Kong at all on the sale of the shares. However, with measures introduced with effect from 2012 for cooling the Hong Kong property market, there are disincentives for using companies (whether Hong Kong or foreign) to acquire residential property due to the additional 15% “buyer’s stamp duty” charged on top of the existing stamp duty (Stamp Duty Ordinance (Cap.117) s.29CB, introduced by the Stamp Duty (Amendment) Ordinance 2014), and the higher *ad valorem* stamp duty rates for acquisitions of residential property which apply where the purchaser is not a Hong Kong permanent resident (Stamp Duty Ordinance First Schedule, Head 1(1) Scale 1, introduced by the Stamp Duty (Amendment) (No.2) Ordinance 2014; and as amended by the Stamp Duty (Amendment) Ordinance 2018 and Stamp Duty (Amendment) (No.2) Ordinance 2018). The higher Scale 1 *ad valorem* stamp duty rates introduced by the 2014 Amendment (No.2) Ordinance previously also applied to non-residential property, but the higher rates were abolished for non-residential property by the Stamp Duty (Amendment) Ordinance 2021 in view of the recent downturn in the commercial property sector in Hong Kong.

- Acting as trustee. Professional trustees provide services to administer trusts for the benefit of their clients. The use of a company has the advantage of avoiding the inconvenience that arises, for example, where a natural person who acts as trustee dies.³
- Vehicle for collective investment. A company can be used to hold assets for the purpose of investment by public investors. Collective investment schemes could be in the form of unit trusts, where investors hold units in the scheme, with the trustee holding the investment assets (such as shares or other securities), and a manager appointed to manage the investments. An alternative is to use the company form, where the investors hold shares in the company, and the company holds and manages the investment assets. Such collective investment schemes can be open-ended (where investors can recoup their investment by having their units or shares redeemed by the trust or company before the expiry of the term of the investment) or closed-ended (where the units or shares cannot be redeemed before the expiry of the investment term, and where investors can only sell their units or shares to others if they wished for early recoupment of their investment). Open-ended fund companies (OFCs) (also referred to as open-ended investment companies) are common in various overseas countries.⁴ In Hong Kong, OFCs were not previously used due to restrictions in company law on redemptions of shares.⁵ However, legislation has now been enacted to enable OFCs to be established in Hong Kong.⁶
- Non-profit purposes. Companies are also used to engage in non-profit enterprises as an alternative to using a simple unincorporated association of persons. For example, companies can be established to operate charities, or to run clubs or sporting activities. Some political parties in Hong Kong are also constituted as a company.⁷
- Carrying on certain government enterprises. The Government sometimes chooses to incorporate a company to carry out activities which can involve a public function. For example, the Hong Kong Mortgage Corporation Ltd is a company wholly owned by the Government and which has functions related to enhancing stability of the banking sector and promoting wider home ownership in Hong Kong.⁸

³ This is because the company's existence continues notwithstanding changes in the members who constitute the company: see para.1.069 below.

⁴ E.g., for England, see the Open-Ended Investment Companies Regulation 2001 (UK).

⁵ For restrictions under company law in general, see Chapter 15.

⁶ Securities and Futures Ordinance (Cap.571) Pt.IVA, introduced by the Securities and Futures (Amendment) Ordinance 2016 (effective from 30 July 2018). See further Financial Services and the Treasury Bureau, *Open-Ended Fund Companies Consultation Paper* (March 2014) and *Consultation Conclusions* (January 2016).

⁷ Securities and Futures Commission, *Consultation Paper on the Securities and Futures (Open-ended Fund Companies) Rules and Code on Open-Ended Fund Companies* (June 2017).

⁸ See *Democratic Party v Secretary for Justice* [2007] 2 HKLRD 804.

⁹ See the website for the Hong Kong Mortgage Corporation Ltd at <<http://www.hkmc.com.hk>>.

2.2 Companies and corporations

Registered companies. The subject of this book is predominantly the registered company (namely companies formed and registered under the Companies Ordinance (Cap.622) or its predecessors⁹), but a little needs to be said on the concepts of "companies" and "corporations" generally. 1.003

2.2.1 Anglo-Hong Kong law

Meaning of "company". In ordinary everyday usage, the term "company" might be used to describe all types of businesses other than sole traders. However, the term "company" has a narrower meaning under modern Anglo-Hong Kong law. The term does not have a strict technical meaning under the common law,¹⁰ but the term is defined in s.2 of the Companies Ordinance to be a company formed and registered under that Ordinance (or a predecessor Companies Ordinance). Accordingly, under modern law in England and Hong Kong, the term "company" is ordinarily understood to refer to an *incorporated* association (or incorporated body). 1.004

Meaning of "corporation". As such, companies form a subset¹¹ of the wider concept of "corporation" (or "body corporate"), a concept recognised under the common law. In an English treatise on corporations from early last century, a corporation was described in the following terms: 1.005

"That body politic known as a Corporation possesses no physical being, but exists in the eye of the law. It is a group composed of many individuals named corporators, yet it has a personality separate and distinct from those individuals. It has a continuous identity. Although the legal existence of an individual ceases with his death, the legal existence of a corporation is not affected by the death or retirement of an individual corporator. It may have a corporate name and seal, and may enjoy rights, privileges and powers according to the scheme of its creation. It may, in certain respects, claim freedom of action as is allowed to an individual; in other respects it is hampered by incapacities which arise partly from its natural and 'internal' limitations, and partly from external restrictions imposed by the policy of the law."¹²

Legal personality. Corporations are said to be artificial legal persons, as opposed to the human individual or natural persons. The possession of legal personality means that the possessor is the subject of the legal system.¹³ The possessor is an entity recognised by the legal system as being the subject of rights and duties. This means that the duties and rights are vested in that entity and not in someone else. So for example, corporations, as a legal person, can own property and can enter into contracts. 1.006

⁹ Namely, Companies Ordinance (1 of 1865) (repealed); Companies Ordinance (58 of 1911) (repealed); Companies Ordinance (39 of 1932) (renamed as the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32) upon the commencement of Cap.622).

¹⁰ *Re Stanley* [1906] 1 Ch 131.

¹¹ In other words, companies are one type of corporation, but there are other types of corporations that are not "companies" as defined in Cap.622. For examples of other types of corporations, see para.1.009 below.

¹² Cecil T Carr, *The General Principles of the Law of Corporations* (Cambridge University Press 1905) 1.

¹³ *J H Rayner (Mincing Lane) Ltd v Department of Trade and Industry* [1989] Ch 72, 107.

1.007 Types of corporation. English common law recognised two categories of corporations: the corporation aggregate and corporation sole. Blackstone described these as follows:

“Corporations aggregate consist of many persons united together into one society, and are kept up by a perpetual succession of members, so as to continue forever; of which kind are the mayor and commonalty of a city, the head and fellows of a college, the dean and chapter of a cathedral church. Corporations sole consist of one person only and his successors, in some particular station, who are incorporated by law, in order to give them some legal capacities and advantages, particularly that of perpetuity, which in their natural persons they could not have had. In this sense the king is a sole corporation; so is a bishop; so are some deans, and prebendaries, distinct from their separate chapters; and so is every parson and vicar.”¹⁴

1.008 Registered company is corporation aggregate. A company registered under the Companies Ordinance (Cap.622) is an example of a corporation aggregate.¹⁵ Such a registered company with a single member is also a corporation aggregate rather than a corporation sole notwithstanding that there is only one member. The concept of corporation sole is a concept of a corporation that comprises a single person and his successors occupying some particular office or position. That is different from single member companies under the Companies Ordinance: such companies might have a sole member at any particular time, but it is legally possible for others to join the company as members so that the company has more than one member.

1.009 Creation of corporations. Under English law, corporations can be created by the Crown by way of letters patent or grant of a charter of incorporation, or by an Act of Parliament.¹⁶ In Hong Kong today, corporations can be created by an Ordinance passed by the Legislative Council. There are a number of statutory corporations created with public functions, such as the Hospital Authority,¹⁷ the Communications Authority,¹⁸ the Securities and Futures Commission¹⁹ and the Hong Kong Tourism Board.²⁰ The various universities in Hong Kong are also corporations.²¹ Some statutory corporations engage in business, such as the Ocean Park Corporation.²² There are also entities established under other Ordinances which are created as a body corporate (e.g. credit unions registered under the Credit Unions Ordinance (Cap.119), ss.3 and 6). These are examples of corporations aggregate. Examples of corporations sole created by statute in Hong Kong include various public bodies such as the Ombudsman²³ and the

¹⁴ William Blackstone, *Blackstone's Commentaries on the Laws of England* (London, 1820) 127. On corporations sole, see also *Hubbard Association of Scientologists International v Attorney-General (Vic)* [1976] VR 119; *Doe v Bennett* (2004) 236 DLR (4th) 577.

¹⁵ *Excelling Profit Investments Ltd v Sera Ltd* [1992] 2 HKC 262.

¹⁶ William Blackstone, *Blackstone's Commentaries on the Laws of England* (London, 1820) 129.

¹⁷ Hospital Authority Ordinance (Cap.113) s.3.

¹⁸ Communications Authority Ordinance (Cap.616) s.3.

¹⁹ Securities and Futures Ordinance (Cap.571) s.3.

²⁰ Hong Kong Tourism Board Ordinance (Cap.302) s.3.

²¹ E.g., City University of Hong Kong Ordinance (Cap.1132) s.3.

²² Ocean Park Corporation Ordinance (Cap.388).

²³ The Ombudsman Ordinance (Cap.397) s.3.

Privacy Commissioner,²⁴ and also religious bodies.²⁵ Corporations which are created pursuant to statute have their rights and powers defined by the statute under which the corporation is created.

2.2.2 Foreign jurisdictions

Companies outside Hong Kong. The terms “company” and “corporation” may mean different things in foreign jurisdictions. For example, the business equivalent of Hong Kong registered companies in the various states of the United States is the business corporation.²⁶ The term “company” is used in the looser sense, referring to both incorporated and unincorporated businesses. There also exists in the United States a hybrid business entity known as the “limited liability company” (LLC).²⁷ LLCs in the United States are in nature partnerships and are different from the type of limited liability company recognised under Hong Kong law (which is a body corporate).

2.3 What company law covers

Scope of company law. Broadly speaking, company law covers the body of laws dealing with the establishment of companies; powers and liabilities of companies; internal administration or operation of companies; rights and duties of corporate participants such as shareholders and directors; financing of companies; external administration (e.g., by liquidators in a winding-up); and dissolution of companies.

2.3.1 “Core” company law

Core and non-core elements of company law. A distinction is sometimes drawn between “core” company law and other areas of law which affect companies but which might be classified as separate subject areas in their own right. Core company law is thus said to cover matters such as establishment of companies and regulation of the internal administration of companies and corporate participants. Rules dealing with a company’s raising of funds from the public through an issue of shares are classed as falling within the area of securities laws (which cover not only company shares, but also other types of securities or financial instruments/investments, and which extend to regulation of the securities markets such as the stock market). The rules on winding-up of companies which become insolvent might be grouped under the rubric of insolvency law, to cover not only corporate insolvencies but also personal bankruptcy laws (which deal with bankruptcy of individuals). Also, laws dealing with company charges could be categorised together with laws dealing with other security interests which either a company or individual could create in favour of creditors (the law here involves rights between a debtor and secured creditor, who has certain rights over the debtor’s assets as security for a loan).

²⁴ Personal Data (Privacy) Ordinance (Cap.486) s.5.

²⁵ E.g., Abbot of the Order of Cistercians of the Strict Observance Incorporation Ordinance (Cap.1107).

²⁶ See the Model Business Corporation Act (MBCA), which has been adopted in a number of states in the US. On the MBCA, see, e.g., Elliot Goldstein, “Revision of the Model Business Corporation Act” (1985) 63 *Texas Law Review* 1471.

²⁷ See, e.g., Wayne M Gazur and Neil M Goff, “Assessing the Limited Liability Company” (1991) 41 *Case Western Reserve Law Review* 387.

- 1.013 Different approaches to whether or not to have the companies statute confined to just core company law.** Prior to the reforms made by the Companies Ordinance (Cap.622) ("Cap.622"), the main Ordinance dealing with company law in Hong Kong (the predecessor Companies Ordinance) has not been confined to core company law. This can be contrasted with overseas jurisdictions including the current UK regime. The Companies Act 2006 (UK) (as was the case of its predecessor, the Companies Act 1985) deals with core company law, while corporate insolvency, together with personal bankruptcies, is dealt with under the Insolvency Act 1986 (UK), and corporate fundraising is dealt with under the Financial Services and Markets Act 2000 (UK). New Zealand is another example of a common law jurisdiction where the companies legislation (Companies Act 1993 (NZ)) deals with core company law only. However, the Corporations Act 2001 (Cth) in Australia covers not only core company law, but also corporate securities and other financial services, as well as corporate insolvency.
- 1.014 Scope of Companies Ordinance (Cap.622).** In 1997 in Hong Kong, a recommendation had been made by consultants appointed by the Government for the Companies Ordinance to be reformed to be confined to core company law.²⁸ The Standing Committee on Company Law Reform (SCCLR) did not favour complete segregation of company law and securities law, although it did see merit in treating insolvency law as a separate topic and in looking at the possibilities of placing the law of company charges in a separate regime governing personal property security interests.²⁹ What has transpired from the more recent review of the Companies Ordinance (under the Companies Ordinance Rewrite project ("CO Rewrite"), which resulted in a new Companies Ordinance (Cap.622) being enacted in 2012,³⁰ is that Cap.622 is confined to core company law (but still including company charges, as is also the case in the United Kingdom). Under the amendments made when Cap.622 came into operation, the core company law provisions in the predecessor Companies Ordinance (Cap.32) were repealed. Cap.32 was not repealed in its entirety as there are provisions which are retained in that Ordinance. These provisions are mainly on winding-up, prospectuses (relating to public offerings of shares and debentures), and disqualification of directors. The predecessor CO was renamed the Companies (Winding-Up and Miscellaneous Provisions) Ordinance upon the commencement of Cap.622.
- 1.015 Only partial separation of core and non-core company law.** The separation of core company law from some of the other areas of company law under the reforms is only partial and does not entirely follow the segregation adopted in jurisdictions such as the United Kingdom. The Securities and Futures Commission (SFC) had earlier proposed that the provisions in Cap.32 on prospectuses will be moved to the Securities and Futures Ordinance (Cap.571),³¹ though this has not yet been implemented. In respect of insolvency law, although the winding-up provisions are contained in that Ordinance (Cap.32) separate from the Ordinance dealing with core company law (namely

²⁸ Ermanno Pascutto and Cally Jordan, *Review of the Hong Kong Companies Ordinance: Consultancy Report* (March 1997) ("Pascutto Report") 57–69.

²⁹ SCCLR, *Report of the Standing Committee on Company Law Reform on the Recommendations of a Consultancy Report of the Review of the Hong Kong Companies Ordinance* (February 2000) 28–33.

³⁰ Cap.622 commenced operation on 3 March 2014.

³¹ SFC, *Consultation Conclusions on Possible Reforms to the Prospectus Regime in the Companies Ordinance* (September 2006).

Cap.622), there is no merging of corporate insolvency and personal bankruptcy laws in a single Ordinance on insolvency.

2.4 Facilitative or mandatory rules?

Whether company law should be mandatory or facilitative. In corporate regulation, there has been a debate whether company law should be mandatory or merely enabling.³² 1.016

Mandatory rules. The idea of mandatory rules is that company law should be composed of a body of mandatory or directive legal rules, reinforced by state-backed sanctions.³³ Mandatory rules can take the form of certain procedural requirements, rules which allocate decision-making power in companies with respect to particular matters,³⁴ and rules which set standards of behaviour (such as fiduciary duties). Mandatory rules are argued to be necessary to protect the interests of shareholders, creditors and others from self-interested actions of corporate managers.³⁵ 1.017

Facilitative rules. The alternative view is that company law should be facilitative or enabling, in the sense that corporators should be free to opt-out and to adopt their own specific rules if they choose.³⁶ Enabling rules might be composed of default rules which apply unless modified by corporators, or rules which allow the court to give effect to the intention of the parties where that intention is otherwise frustrated by some irregularity. Those who argue that company law should be enabling emphasise the importance of individual rights and freedoms and private ordering of relationships. 1.018

Balance between rules required. Commentators such as Bottomley have argued that company law must involve both mandatory and facilitative rules.³⁷ Mandatory standards must be set by the state to uphold public values, for example to avoid oppressive or unfair conduct and to provide for financial and decision-making accountability. On the other hand, empowering and facilitative rules are also needed to enable corporators to add their own constitutional rules, in recognition of the private internal dimensions of companies. In Hong Kong, the SCCLR has also expressed the view that it is appropriate for company law to provide for a balanced mix of default and mandatory rules.³⁸ 1.019

³² See, e.g., Jeffrey N Gordon, "The Mandatory Structure of Corporate Law" (1989) 89 *Columbia Law Review* 154; Henry N Butler and Larry E Ribstein, "Opting out of Fiduciary Duties: A Response to the Anti-Contractarians" (1990) 65 *Washington Law Review* 1; John C Coffee Jr, "The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role" (1989) 89 *Columbia Law Review* 1618; William Bratton, "Public Values and Corporate Fiduciary Law" (1992) 44 *Rutgers Law Review* 675.

³³ Stephen Bottomley, "The Birds, The Beasts, and the Bat: Developing a Constitutionalist Theory of Corporate Regulation" (1999) 27(2) *Federal Law Review* 243, 251.

³⁴ For example, the decision for a lawful reduction must be made by the members in general meeting; see Companies Ordinance (Cap.622) s.211.

³⁵ Stephen Bottomley, "The Birds, The Beasts, and the Bat: Developing a Constitutionalist Theory of Corporate Regulation" (1999) 27(2) *Federal Law Review* 243, 251.

³⁶ *Ibid.*

³⁷ *Ibid.*

³⁸ SCCLR, *Report of the Standing Committee on Company Law Reform on the Recommendations of a Consultancy Report of the Review of the Hong Kong Companies Ordinance* (February 2000) [4.23].

2.5 Sources of law

- 1.020 **Statutory and common law.** Company law in Hong Kong is composed of both statutory and common law.
- 1.021 **Companies Ordinance (Cap.622)** In 2012, a new Companies Ordinance (Cap.622) was enacted, with effect from 3 March 2014 (see LN 163 of 2013).³⁹ Cap.622 replaced many of the provisions in the predecessor Companies Ordinance (Cap.32). Previously, the predecessor CO was the main source of law on companies in Hong Kong and contained provisions which regulate the creation, administration and winding-up of companies. Following the commencement of Cap.622, the provisions on creation and administration of companies (core company law) are now contained in Cap.622. The corresponding provisions in the predecessor CO were repealed, but the predecessor CO still contains the provisions on winding-up, public issues of shares or debentures and disqualification of directors, and the Ordinance was renamed as the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (Cap.32). Accordingly, there are presently two Ordinances in Hong Kong covering company law. Companies are often said to be a “creature of statute”, and this is correct in the sense that companies are today created pursuant to statute, and the rights and liabilities of companies are set out in statute.
- 1.022 **Common law.** The Companies Ordinance is not a code on company law, as major areas affecting the operation of companies are covered by common law principles. For example, a great number of equitable doctrines and principles come into play in regulating rights and duties of corporate participants. General principles of agency law are important in regulating dealings between a company and outsiders (or third parties). Apart from these other areas of law which find their way into company law principles, there are also various company law doctrines (e.g., on the corporate veil, or the capital maintenance doctrine) which, at their inception, might have been regarded by the courts as being derivative of, or implicit from, the early company law statutes, but which have largely been developed and fleshed out in case law by the courts.
- 1.023 **Influence of the UK and other common law jurisdictions.** The Hong Kong Companies Ordinance has traditionally and, to a large extent, still does follow UK company law. As such, much of the jurisprudence in English court decisions is relevant for Hong Kong. The company law of some other common law jurisdictions overseas is also derived from the UK model, and so court decisions in such jurisdictions (such as Australia) — on both the common law and comparable statutory provisions — might also have persuasive authority in Hong Kong even if they do not operate as binding precedents. Some of the provisions in the Companies Ordinance have also been enacted with reference to legislative developments in jurisdictions other than the United Kingdom (such as in Australia, New Zealand, Canada, and Singapore), and so reference to overseas decisions on the comparable statutory provisions will often be useful.

³⁹ The reforms are discussed further below at para.1.114.

3. COMPANIES AND OTHER FORMS OF BUSINESS ASSOCIATION

3.1 Introduction

Types of business vehicles. Businesses can be operated through different types of business vehicles or business organisations. The three broad types of business vehicles which are recognised under Hong Kong law are: 1.024

1. sole proprietorships;
2. partnerships; and
3. companies.

Legal rights dependent on type of business vehicle. The type of business vehicle adopted has implications on the legal relationships between the owners and operators of the business as well as between the owners/operators and third parties with whom the business deals. In other words, the types of legal rights that arise will depend on the type of business vehicle used. 1.025

3.2 Sole proprietorships

Persons running a business on their own. A person operating the business on their own account can do so as a sole trader or sole proprietor. 1.026

Few formalities for sole proprietorship. As a matter of formality, sole proprietorships are straightforward to establish. The main legal requirement for establishment is registration of the business under the Business Registration Ordinance (Cap.310). (This requirement also applies for other business vehicles.) 1.027

Benefits and responsibilities of sole trader. The sole trader receives all the profits of the business, and is personally liable for all its losses. Contracts are entered into for the business by the sole trader personally (or by employees or agents acting on behalf of the sole trader, who, as the principal, is the party to the contract). 1.028

Law applicable to sole traders. There are no specific legal rules applied to the category of sole proprietors or sole traders. Rights and liabilities simply accrue to the individual; and the general law (e.g. contract law or agency law) applies to the sole trader as it applies to any individual. 1.029

3.3 Partnerships

3.3.1 General

Partnership between two or more persons. A partnership can be formed between two or more persons (partners). Partners are regarded as joint owners of the business, and would share in both the profits and losses of the business. 1.030

1.031 Partnership law applies. A special body of law is applicable to partnerships — i.e., partnership law. This body of law is composed of principles under the Partnership Ordinance (Cap.38) and principles of the common law.

3.3.2 Formation and identification of partnerships

1.032 Partnership rights and liabilities. Whether certain persons are in a partnership relationship impacts on their rights and liabilities.

1.033 Contractual intention to form partnership required. The formation of a partnership depends on the contractual intentions of the parties.⁴⁰ Thus, there must be a valid agreement between the parties, as a matter of contract law, to establish a partnership. The relevant intention is not whether the parties subjectively intended to form a partnership, but whether, objectively speaking, the parties intended to form an association that the law regards as a partnership.⁴¹

1.034 Definition of “partnership”. Section 3(1) of the Partnership Ordinance defines a partnership as “the relation which subsists between persons carrying on a business in common with a view of profit”. Thus, it is this relationship which must exist before a partnership can come into existence.

1.035 Partnership requires carrying on of business. The concept of a partnership requires that there be the carrying on of a business. The business is usually a continuing one (e.g., operating some retail business), although it is possible for a partnership to be formed in relation to a single undertaking.⁴² The concept of a business, however, is distinguished from activities which are not in the nature of a commercial or business enterprise. For example, the mere fact that two or more persons jointly own investment property and jointly derive profits from the investment does not mean that there is a partnership.⁴³ However the courts take a wide view of the concept of “business” for the purpose of the Partnership Ordinance. It has been held that where parties purchase property with a view to its subsequent sale to make a gain, this may constitute a partnership even if the venture might not be regarded as a “business” for tax purposes.⁴⁴

1.036 Partnership business must be carried on in common. For there to be a partnership, the business must be carried on in common. This is distinguished from a situation where an undertaking can be said to be constituted of separate businesses rather than one business being carried on in common.⁴⁵ The following factors, although not necessarily decisive in themselves, may be relevant in indicating that the venture is not carried on in common: where the parties are responsible for different aspects of the

⁴⁰ *Smith v Anderson* (1880) 15 Ch D 247.

⁴¹ *Cox v Hickman* (1860) 8 HL Cas 268.

⁴² See e.g. *Winsor v Schroeder* (1979) 129 NLJ 1266.

⁴³ See Cap.38 s.4(a) and para. 1.037.

⁴⁴ *Patel v Barlows Solicitors (a firm)* [2021] 1 BCLC 231, [112]–[114] (partnership existed where the enterprise for purchase and resale encompassed three properties, though the court appeared to take the view that there could be a partnership even in the case of a “one-off” acquisition for the purpose of resale). Cf. *Taylor v Good* [1974] 1 WLR 556.

⁴⁵ *Blues Hairshop v Customs and Excise Commissioners* 2000 SC 936, *Strathearn Gordon Associates Ltd v Commissioners of Customs & Excise* [1985] VATTR 79.

undertaking,⁴⁶ where the parties have full control over their areas of responsibility and no joint control over the management of the entire scheme; where the parties do not intend to carry on the business as principals, nor as agents of each other;⁴⁷ where the parties do not intend to be severally liable for obligations to third parties;⁴⁸ and where the parties do not share the net profits.⁴⁹

Partnership relationship. Section 4 of the Partnership Ordinance also sets out factors that are to be taken into account when ascertaining whether a person is in a partnership relationship with others:

- Joint ownership of property does not of itself create a partnership.
- Sharing of gross returns does not of itself create a partnership.
- Receipt by a person of a share of profits in a business is *prima facie* evidence that the person is a partner in the business. But the receipt of a payment contingent on or varying with the profits of a business does not of itself make the person a partner. Accordingly: (i) receipt of a debt out of profits of a business does not of itself make the creditor a partner; (ii) remuneration of an employee or agent by a share of the profits does not of itself make the employee or agent a partner; (iii) a widow or child of a deceased partner who receives a part of the profits of a business as annuity is not a partner by reason only of such receipt; (iv) a lender who receives a rate of interest varying with the profits of a business is not a partner by reason of such receipt alone (provided that the contract of loan is in writing and signed); and (v) a person receiving a portion of the profits of a business in consideration of the sale by the person of the goodwill of the business is not a partner by reason only of such receipt.

Mansell case: no partnership as no intention to carry on business as partners. For example, in *Keith Spicer Ltd v Mansell*,⁵⁰ Bishop and Mansell agreed to form a company to carry on a restaurant business. While they were still looking for suitable premises, Bishop ordered goods for the restaurant and had them delivered to Mansell's premises.⁵¹ The business was never established. Bishop was bankrupt. The suppliers sued Mansell for payment for the goods. It was argued that Mansell should be liable on the basis that there was a partnership between him and Bishop. The court held that there was no partnership as there had not been any intention on the part of the parties

⁴⁶ *Barton v Hanson* (1809) 2 Taunt 49; *Lyon v Knowles* (1864) 5 B & S 751; *Television Broadcasters Ltd v Ashton & Nominees Pty Ltd* (1979) 22 SASR 552.

⁴⁷ *Canadian Pacific Ltd v Telesat Canada* (1982) 133 DLR (3d) 321; *Mann v D'Arcy* [1968] 1 WLR 893.

⁴⁸ *Television Broadcasters Ltd v Ashton & Nominees Pty Ltd* (1979) 22 SASR 552; *Beckingham v Port Jackson & Manly Steamship Co* (1957) SR (NSW) 403; *Lang v James Morrison & Co Ltd* (1911) 13 CLR 1, 11.

⁴⁹ *Cox v Coulson* [1916] 2 KB 177; *United Dominions Corporation Ltd v Brian Pty Ltd* (1985) 60 ALR 741, 750; *ARM Constructions Pty Ltd v FCT* (1987) 87 ATC 4790; *Cannings v Lewis* (unrep., Federal Court of Australia, 2 August 1991).

⁵⁰ [1970] 1 All ER 462.

⁵¹ The letter from the supplier of the goods was addressed to “B T Bishop, Esq, BM Vending Ingredients Sales (London) Ltd”, and the invoices were addressed to “BM Vending Ingredients Sales (London) Ltd”.

to carry on business as partners. Their intention was to create a company, and what was done were simply acts preparatory to the carrying on of a business.

1.039 Partnership can come into existence before trading commences if relevant intention present. However, where the parties do intend to operate their business as a partnership, the partnership can come into existence even before the commencement of trading. Where the parties contemplate that the business will be run as a partnership, and they take significant steps to conduct the business, then there will be a partnership in existence even before the business is opened to customers.⁵²

1.040 Chan case: partnership held to exist in light of agreement. In *Chan Sau-kut v Gray and Iron Construction and Engineering Co (a firm)*,⁵³ the court considered the question of whether a party who provided funds to another for a project for drainage works under a construction sub-contract was in a partnership with the other. The court held that it was a partnership in light of the following circumstances: the recital to the agreement stating that the parties wished to cooperate in the drainage works (suggesting a community of interest); a clause in the agreement providing that all the parties were to observe and perform the terms and conditions of the sub-contract (suggesting joint obligations under the sub-contract); a clause establishing a joint bank account; a clause providing that the parties would have joint management and control over how the funds were to be used and that there were to be fortnightly meetings between the parties regarding work in progress. In the court's view, the terms of the agreement indicated a partnership rather than a creditor-debtor relationship between the parties.

3.3.3 Registration

1.041 Registration of partnership required. The carrying on of a business as a partnership requires registration under the Business Registration Ordinance (Cap.310). The partnership can carry on business under the names of its partners or under some business name registered under the Ordinance.

3.3.4 Nature of a partnership

1.042 Partnership not a legal entity separate to its members. A partnership might be referred to as a "firm", but a partnership is not a legal entity that is separate from its members (the partners).⁵⁴ This is illustrated by some of the principles below dealing with the legal rights and liabilities of partners.

3.3.5 Partnership property

1.043 Partnership property and separate property: different treatment. Property used for the purposes of the partnership business can be categorised either as partnership property (belonging to all the partners) or separate property belonging solely to one or more individual partners. It is important to ascertain whether property is partnership property or not — for example, because partnership property must be applied

⁵² *Khan v Miah* [2000] 1 WLR 2123.

⁵³ [1986] HKLR 84.

⁵⁴ *Scott-Hake v Frost* [2021] 2 BCLC 460, [24].

exclusively for the purposes of the partnership and in accordance with the partnership agreement;⁵⁵ and treatment of the property on a winding-up of the partnership (or upon bankruptcy of individual partners) differs depending on whether the property is partnership property or not.⁵⁶

Partnership property jointly owned by partners. Where property is partnership property, the property is not owned by any entity separate from the partners. Rather, the property is owned jointly by the partners, with each having a form of equitable proprietary interest in the partnership assets.⁵⁷ 1.044

Ascertaining whether property belongs to the partnership. Whether property is partnership property or not is ascertained from either the express agreement of the parties or by reasonable inference from the manner in which the partners have dealt with the property during the subsistence of the partnership.⁵⁸ 1.045

Miles case: in absence of express or implied agreement court will only treat property as "partnership property" if required to give business efficacy to arrangements. In *Miles v Clarke*,⁵⁹ a fashion photography business was operated as a partnership between the plaintiff and the defendant. When the business was wound up, it was necessary to ascertain who was entitled to which assets used in the business. There was no express agreement between the partners whether the assets were partnership property or not. The court held that in the absence of express agreement and any other indications of an implied agreement, the court would treat property brought by each of the parties into the business as partnership property only as far as necessary to give business efficacy to the arrangements. In this case, the court took the view that for the business to operate, the stock in trade of the business (such as film) must be the property of the partnership. However, ownership of other assets could have remained with the original owner. Thus, the defendant, who had originally operated the business on his own account, and who had originally acquired a lease of premises for the business and had provided the equipment and furniture for the business, was entitled to those assets (not being partnership property). Goodwill brought by the plaintiff to the partnership remained the property of the plaintiff. It was not necessary for these assets to be treated as assets of the partnership business in order for the business to operate. For example, the partnership can be regarded as being entitled to use of the premises for the business on the basis of a licence granted by the defendant. 1.046

Law case: facts. In *Law Chou Shing v Chow Wing Kun*,⁶⁰ a Mr Law set up a business in the timber trade. Mr Lam and Mr Chow became partners in the business. In 1988 Mr Chow purchased residential premises in Tai Po — he intended to live in those premises with a Miss Poon whom he was to marry. The property was purchased in the names of 1.047

⁵⁵ Partnership Ordinance (Cap.38) s.22.

⁵⁶ See Bankruptcy Ordinance (Cap.6) s.38(7).

⁵⁷ See *Popat v Schonchhatra* [1997] 3 All ER 800; *Canny Gabriel Castle Jackson Advertising Pty Ltd v Volume Sales (Finance) Pty Ltd* (1974) 131 CLR 321; *Federal Commissioner of Taxation v Everett* (1980) 54 ALJR 196.

⁵⁸ See *Miles v Clarke* [1953] 1 All ER 779; *Law Chou Shing & Anor v Chow Wing Kun & Anor* [1994] 2 HKC 531; *Kelly v Kelly* (1990) 92 ALR 74.

⁵⁹ [1953] 1 All ER 779.

⁶⁰ [1994] 2 HKC 531.

Mr Chow and Miss Poon but was to be in the first instance paid for by the partnership under the following arrangement: the partnership was to make the loan repayments to the mortgagee under a mortgage obtained for the purchase of the property; at the same time, the amount of the loan repayments was to be debited in an account between Mr Chow and the partnership. Under these arrangements, ultimately Mr Chow would need to effectively make the payments. Similar arrangements were already in place with the partnership for certain property owned by Mr Law.

1.048 **Law case: in absence of express agreement intentions and actions of parties critical to determining what constitutes partnership property.** Subsequently, the partnership broke down, and a dispute arose regarding whether the Tai Po premises were partnership property or not. There was no express agreement on this matter. The court examined various factors in ascertaining the implied agreement of the parties and concluded that the parties' intentions were that the property would be the separate property of Mr Chow and Miss Poon (and not partnership property). The court took into account the following factors:

- The attitude of Mr Chow and Miss Poon as to the decorations in the flat when they purchased it. The evidence was that they had chosen the flat because the existing decorations were adequate and it was not necessary for extra spending to re-decorate the place. This indicated the parties' intentions that Mr Chow and Miss Poon were to bear the costs in relation to the flat and that the premises were to be theirs.
- In the partnership accounts, debits were made to Mr Chow's account with the firm with the effect that Mr Chow would ultimately pay for the cost of the purchase. This was the same treatment in the accounts as for Mr Law's own residential property.
- When the partnership had entered into difficulty, the partners had arranged for the Tai Po property to be mortgaged under an all-monies mortgage with funds being used for the partnership. Miss Poon had been very reluctant about this arrangement, and although she finally agreed, the court took her reaction as an indication that she was the owner of the premises (otherwise she would not have been so concerned with the property being used for the purposes of the business).

3.3.6 Financing

1.049 **Capital or loan financing.** Partners may contribute funds to the partnership by way of capital or loan. There are different legal consequences depending on whether amounts are provided by partners as capital or loan.⁶¹ In ascertaining the form in which money is paid over by one party, it is necessary to look at the terms of the agreement.⁶² For

an example of where the court needed to ascertain whether amounts paid by a partner were in the nature of capital or loan, see *Chan Sau-kut v Gray and Iron Construction and Engineering Co (a firm)*, discussed above at para.1.040.

External loan financing. The partnership can also seek external loan financing, for example from banks. **1.050**

3.3.7 Relationship between partners

Rights and liabilities of partners between themselves. The rights and liabilities of the partners *inter se* (between themselves) depend on the partnership agreement (effective on the basis of contract law principles), the provisions of the Partnership Ordinance, as well as the general law. **1.051**

Rights and duties under Partnership Ordinance (Cap.38). Section 26 of the Partnership Ordinance sets out rights and duties; however, s.26 is subject to agreement between the partners to the contrary (whether expressed or implied). Under s.26: **1.052**

- partners share equally in the capital and profits of the business, and must contribute equally to the losses;
- partners are entitled to an indemnity from the partnership in respect of payments and personal liabilities incurred: (i) in the ordinary and proper conduct of the business of the firm, or (ii) in or about anything necessarily done for the preservation of the business or property of the firm;
- a partner making a payment or advance beyond the agreed capital contribution is entitled to interest of 8 per cent per annum;
- a partner is not entitled, before the ascertainment of profits, to interest on the capital subscribed by him;
- every partner may take part in the management of the business;
- no partner is entitled to remuneration;
- no person may be introduced as partner without the consent of all partners;
- any difference arising as to ordinary matters connected with the partnership business may be decided by a majority of the partners, but no change may be made in the nature of the partnership business without the consent of all partners; and
- partnership books are to be kept at the place of business of the partnership (or the principal place, if there are more places than one), and every partner may have access to and inspect and copy any of them.

Fiduciary duties owed by partners to each other. Partners are fiduciaries and owe fiduciary duties to each other. Fiduciary duties are imposed in equity on certain categories of persons, such as partners. Some of the fiduciary duties are also reflected in the Partnership Ordinance.⁶³ **1.053**

⁶¹ See, e.g., Partnership Ordinance, ss.26(c), 26(d), 46(b).

⁶² See *Bronester Ltd v Priddle* [1961] 3 All ER 471; *London Financial Association v Kelk* [1884] 26 Ch D 107; *SEC Construction Material Ltd v Tan Kin* (unrep., HCA 423/2001, [2002] HKEC 1551).

⁶³ See ss.31 and 32.