

- release from buy-back contracts (s 49F);
- private company redeeming or buying back its shares out of capital (s 49L);
- establishing reserve capital (s 52);
- varying class rights (s 63A and art 4)
- reducing a company's share capital (ss 58-63 and art 47);
- removal of a director (s 157B and art 98);
- rendering the liability of the directors unlimited (s 160);
- approving the assignment of office by a director (s 164);
- resolution that the company be wound up by the court (s 177(1)(a));
- resolution to wind up the company voluntarily (s 228(1)(b));
- authorising the liquidator to accept shares as consideration for the sale of the company's property in a voluntary liquidation (s 237); and
- authorising the directors to make a statutory declaration that the company will become dormant (s 344A).<sup>53</sup>

### Ordinary Resolutions

Ordinary resolutions are appropriate for all matters except where the Ordinance or articles specifically require a special resolution. The passing of an ordinary resolution requires nothing more than a majority of votes in favour. The normal notice period for ordinary resolutions is 14 days. Although special resolutions must be registered with the Registrar of Companies within 15 days of being passed, ordinary resolutions generally need not be registered (s 117(1)).<sup>54</sup>

### Requisitions of Resolutions at AGM

Under s 115A members may by written requisition require the company to give notice to members of resolutions for consideration at the next AGM. Members must hold 5 per cent of the total voting rights or constitute 100 members holding shares on which there has been paid up an average sum per member of not less than \$2000 per member. The requisition must be deposited at the company's registered office at least six weeks before the AGM. The company has duty to circulate to all entitled members notice of any such resolutions (see s 115A).

<sup>53</sup> See *Mayson, French & Ryan on Company Law* (Blackstone Press Limited, 13th edn, 1996) at p 370-1 and Stott, above note 28 at pp 176-177.

<sup>54</sup> Certain resolutions must be registered within 15 days:

- to increase the authorised capital under s 53 (s 55(1));
- to authorise the directors to allot shares (s 57B(5));
- to vary any provision in the articles which is expressly authorised by the articles to be varied by ordinary resolution (s 117(1)(f)); and
- requiring a company to be wound up voluntarily (s 228(1)(a)).

## CHAPTER 5

# The Board of Directors

### INTRODUCTION

Since a company is an artificial legal entity it requires some organ or agent to act on its behalf, eg to allow the company to enter into contracts. The power to manage a company's affairs is usually divided between the board of directors and the members in general meeting. This principle of division of powers is often described as achieving a 'separation of ownership and control'.<sup>1</sup> However, it is important to remember that in many private companies in Hong Kong the directors and the members are the same persons. Subject to the Companies Ordinance, a company may adopt any form of articles to divide management powers among the board and the members of the company in general meeting. In most cases, the company's articles provide for the appointment of a board of directors and typically the authority to manage the company is delegated to the board of directors collectively. For example, art 82, Table A vests the general powers of management in the board of directors.

The directors have freedom to exercise the management powers assigned to them by the company's articles. However, in exercising these management powers the directors are considered fiduciaries and they are subject to judicial control in the exercise of their fiduciary powers. This control imposes limits on the purposes for which the directors' powers may be exercised. For example, directors must act *bona fide* in the best interests of the company and they must exercise their powers for the purpose for which they were given, ie the 'proper purpose' doctrine (see Chapter 7).

This chapter will begin by considering the proceedings at board of directors meetings, followed by a discussion of the division of management powers between the board of directors and the members of the company in general meeting. The way in which a company contracts with outsiders will then be reviewed, along with a few brief comments on corporate governance and the Report of the Committee on the Financial Aspects of Corporate Governance (The 'Cadbury Report').

<sup>1</sup> See SW Mayson, D French and C Ryan, *Mayson, French and Ryan on Company Law* (Blackstone Press Ltd, 13th edn, 1996) at p 444.

## PROCEEDINGS AT BOARD MEETINGS

As a general rule, directors of a company are required to conduct their business by means of board meetings to which each director should be invited.<sup>2</sup> The proceedings of board meetings are much less formalised than that of general meetings of the company (see Chapter 4). The procedure at board meetings is governed by the company's articles and by any rules made by the directors themselves under the powers granted them by the articles. Article 100 provides that the directors may meet together to discuss business, adjourn, and otherwise regulate their meetings, as they think fit. A director may, and the secretary on the requisition of a director shall, at any time summon a meeting of the directors. It is not necessary to give notice of a meeting of directors to any director for the time being absent from Hong Kong.

Generally, the directors individually have no power to act as agents of the company, rather it is the board of directors acting collectively which represents the company: see *Guinness plc v Saunders* [1990] 2 AC 663, [1990] 1 All ER 652. The directors can only exercise their powers collectively by passing resolutions at a properly convened meeting of the board of directors. Board meetings are not usually required for every decision the board makes due to its ability to delegate its decision-making powers either to a managing director (art 111) or committees of directors (art 104). Furthermore, it may be impossible or impractical for the directors to meet to discuss company matters. To enable the board to consider any matter without being required to assemble together, the articles often state that a written resolution signed by all the directors entitled to receive notice of a board meeting is as effective as if duly passed at a board meeting (see art 108). In *Runciman v Walter Runciman plc* [1992] BCLC 1084 it was held that directors can make unanimous decisions informally without the need to convene a formal board meeting.<sup>3</sup>

In accordance with art 100 all the resolutions and votes are decided at a board of directors' meeting by a majority of votes, and where

<sup>2</sup> See *Runciman v Walter Runciman plc* [1992] BCLC 1084.

<sup>3</sup> Citing *Re Bonelli's Telegraph Co*, *Collies Claim* (1871) LR 12 Eq 246 and *Charterhouse Investments Trust Ltd v Tempest Diesels Ltd* [1986] BCLC 1. Note the acceptance of board meetings held via telephone conference calls in *Magnacrete v Robert Douglas-Hill* (1988) 15 ACLR 325 and *Re Equiticorp International plc* [1989] 1 WLR 1010. However, in *Magnacrete* the court stated that the law had not yet advanced to allow board meetings to be validly held by separate telephone calls to directors. For further analysis of the informality of directors' meetings see: P Lawton, 'Board Decisions Without a Meeting and Related Issues', April 1994 Vol 4:4 *Company Secretary* 24; P Lawton, 'Bored With Meetings', May 1994 Vol 4:5 *Company Secretary* 29; and G Mann, 'Directors' Meetings', April 1991 *Company and Securities Law Journal* 85.

there are equal votes the chairman has a second or casting vote. Where a resolution is passed at an adjourned meeting of directors it is treated as having been passed on the later date and cannot be treated as if it were passed on the date of the earlier meeting (s 118(c)). The directors may elect a chairman and decide the period for which they will hold office. If the chairman is not present within five minutes of the time appointed for a meeting, the directors present may choose another person to act as chairman for the meeting (art 103). Minutes of all proceedings at directors' meetings must be entered in a book kept for such purposes and they must be signed by the chairman of the meeting: see ss 119(1) and (2). They must be kept at the company's registered office but unlike minutes of general meetings of the company, the minutes of directors' meetings are not open to inspection.<sup>4</sup>

### Notice

Article 100 provides that any one director may summon a meeting directly or by requesting the secretary to do it. Although the Ordinance and the articles are silent on this issue, prima facie, due notice must be given convening a meeting of directors and in default the meeting is irregular (this may not always be the case since the directors may decide or the articles may provide that meetings may be held at fixed times, in which case no notice of each separate meeting need be given). Where notice has to be given, it may be given verbally unless the articles require it to be given in writing and it must be given a reasonable time before the meeting.

*In deciding whether notice is sufficient a court should have regard to all the relevant circumstances, including whether notice has been given early enough to allow a director to attend.*

### **Broadview Commodities Pte Ltd v Broadview Finance Ltd** [1983] 2 HKC 578, [1983] HKLR 384

At issue in this case was the validity of a resolution passed at a board of directors' meeting of the plaintiff, a Singapore company. The resolution ratified action taken by the permanent director to

<sup>4</sup> Note the decision of Jones J of the Hong Kong High Court in *Chan Kai Hon et al v Chan Kam Wah et al* [1983] 2 HKC 638 which was decided prior to the inclusion of s 119 in the Companies Ordinance. It was held that under the common law it was not obligatory, although it was desirable, for private companies to keep minutes of meetings. The minutes of a meeting were not considered exclusive evidence of what happened there.

## CHAPTER 14

## Foreign Corporations

## INTRODUCTION

Thus far the cases and materials discussed in this book have concentrated on Hong Kong companies – that is companies formed and registered in Hong Kong under the Companies Ordinance. But, of course, there are a great many foreign companies (and other business enterprises) which carry on business in Hong Kong, own assets located in Hong Kong or merely trade with Hong Kong. It is important to note that, in general, such foreign corporations are not governed by the provisions of the Companies Ordinance. This is because, just as Hong Kong law governs the formation and dissolution of Hong Kong companies, so too a corporation incorporated in Japan is governed by Japanese law: the creation and dissolution of a corporation is governed by the law of the place of incorporation.<sup>1</sup> Likewise, the interpretation and effect of the constitution of a corporate entity (eg whether the members of the corporation stand in a contractual relationship with each other on the terms of the articles or by-laws) is a matter for the law of the State of incorporation. Thus, as a general rule, much of the Companies Ordinance (eg registration, certificates of incorporation, effect of memorandum and articles, appointment and removal of directors, shareholders' rights, etc) has never applied to foreign corporations. This point is made quite clearly by s 2 of the Companies Ordinance which specifies that, unless the context otherwise requires, the word 'company' means only a Hong Kong company.<sup>2</sup>

It should not, however, be thought that none of the provisions of the Ordinance applies to foreign corporations. Three points must be made. Firstly, Part XI of the Ordinance (entitled 'Companies Incorporated Outside Hong Kong') requires (s 333) that a foreign company that has established a place of business in Hong Kong must register as an 'oversea company' with the Registrar. (This does not, of course, mean that the foreign corporation becomes a Hong Kong company, but rather that it has to register under Part XI in Hong Kong.) A

foreign corporation falling within Part XI is required (inter alia) to register its constitution (s 333(1)(a)) and a list of directors (s 333(1)(b)), to nominate one or more persons resident in Hong Kong to accept service of process on behalf of the company (s 333(1)(c)) and to file annual returns (s 336) – although where the foreign company is in substance similar to a private company (under the Companies Ordinance) such accounts are not required (s 336(6)). Part XI also provides for service on an oversea company which has established a place of business in Hong Kong but failed properly to submit the details of a person authorized to accept service (s 338). (The position in respect of a foreign corporation which opens a so-called 'representative office' in Hong Kong is examined separately below.<sup>4</sup>) Second, any foreign corporation whether or not it has established a place of business in Hong Kong can be wound up under Part X as a so-called 'unregistered company'.<sup>5</sup> The use of winding up proceedings in relation to a foreign corporation is generally relevant where that corporation is insolvent (see s 327(3)(b)) – however, Part X also contains a 'just and equitable' ground<sup>6</sup> (see s 327(3)(c)) which might be invoked in relation to a solvent foreign corporation where a shareholder believes that the directors are running the corporation fraudulently etc. Third, although the expression 'company' does not generally include a foreign corporation, the term 'body corporate' is defined in s 2(3) as 'including a company incorporated outside Hong Kong'.<sup>7</sup> In practical terms this last point is of rather limited impact because in the overwhelming majority of instances the Ordinance does use the word 'company', whilst the expression 'body corporate' is found in only a handful of places: eg s 28A (membership of holding company), s 115 (representation of companies at meetings of other companies), and s 154A (restriction on body corporate being a director).

At the outset it may be noted that Hong Kong's company legislation has never sought to control foreign direct investment by means of the regulation of foreign corporations which carry on businesses in Hong Kong. This obviously follows from the consideration that there are no restrictions upon the right of foreign investors to hold shares in Hong Kong companies. In essence, therefore, whether a foreign company chooses either (i) to establish a branch in Hong Kong (and register under Part XI) or (ii) to incorporate a subsidiary (Hong Kong incorporated) company, will be a business decision. (This is why the Hong Kong Law Reform Commission Sub-Committee on Insolvency

1 See Dicey and Morris, *The Conflict of Laws* (London: Sweet & Maxwell, 12th edn, 1993) p 1107 and cases there cited.

2 See, for example, *Insurance Company of the State of Pennsylvania v Grand Union Insurance Co* [1988] HKC 200.

3 See further *SFC v MKI Corp Ltd*, p 527, below.

4 See *Elsinct (Asia-Pacific) Ltd v Commercial Bank of Korea Ltd*, below.

5 See *Re China Tianjin International Economic and Technical Cooperative Corp*, below.

6 See *Loch v John Blackwood Ltd* [1924] AC 783.

7 It has been held that the term 'corporation aggregate' in relation to s 20(1) of the Conveyancing and Property Ordinance (Cap 219) includes a foreign company: *Excelling Profits Investments Ltd v Sera Ltd* [1992] 2 HKC 262.

has suggested, see *Consultation Paper on Corporate Rescue and Insolvent Trading*, 1995, para 2.6, that any rescue procedure introduced in Hong Kong should be available to Part XI companies as well as Hong Kong companies: see further p 554, below.) It is fair to say that in a majority of instances it will be simpler to incorporate a Hong Kong subsidiary – which will also have the advantage of limiting the liability of the parent in respect of any losses of the Hong Kong business (and indeed vice versa). Nevertheless, as of July 1996 there were some 4,500 foreign corporations registered as overseas companies under Part XI.<sup>8</sup> Moreover, in recent years, there has been a trend for companies listed on the Hong Kong Stock Exchange to structure their businesses so as to be incorporated overseas (particularly in Bermuda) but register under Part XI and remain listed on the Stock Exchange. Indeed, roughly two-thirds of the companies currently listed in Hong Kong are overseas companies.<sup>9</sup>

### OVERSEA COMPANIES AND PART XI

Section 332 provides that Part XI shall apply to all 'overseas companies' 'that is to say, companies incorporated outside Hong Kong which ... establish a place of business in Hong Kong'. Section 332 derives from British companies legislation<sup>10</sup> and it may be noted that the terminology 'overseas company', although no doubt accurate in relation to the island of Britain, is less so when it comes to Hong Kong – a PRC corporation is not (geographically speaking) an overseas company. Nevertheless, the English precedents have generally been consistently applied in the Hong Kong courts: but there is one notable exception where the Companies Ordinance has departed from the British precedent (see *Elsinct (Asia-Pacific) Ltd v Commercial Bank of Korea*, infra).<sup>11</sup>

*A foreign company which has a branch office in Hong Kong has established a place of business in Hong Kong.*

**Alexandra Knitters Ltd v AB Hellenic**  
(1971) [1946–1972] HKC 571  
(Hong Kong High Court)

The defendant was a limited liability company incorporated in Sweden which had opened an office in Nathan Road. The defendant had regularly ordered samples from the plaintiff, those samples had normally

<sup>8</sup> Registrar of Companies (private communication).

<sup>9</sup> See p 7, above for a description of 'Bermudarisation'.

<sup>10</sup> See Companies Act 1985, Part XXIII.

<sup>11</sup> This departure (discussed below) is in relation to so-called 'representative offices'.

been sent to the Nathan Road office, although at times samples had also been sent directly to Sweden. Whenever an order for samples was received from the defendant, the plaintiff would submit a debit note to the office in Nathan Road. It was held on the facts that the defendants had established a place of business in Hong Kong.<sup>12</sup>

**Blair-Kerr SPJ:** The defendants have not complied with the provisions of Part XI of the Companies Ordinance (Cap 32). However, in October 1966 they registered themselves under the regulations made under the Business Registration Ordinance (Cap 310).<sup>13</sup> In doing so, they used Form 1(b), which is the statutory form prescribed for use by foreign bodies corporate in the registration of a business carried on by them in Hong Kong. In this form they declared that their 'registered office' was Casaplatsen 8, Gothenburg, Sweden; and the business in Hong Kong was described as 'the Hong Kong office (branch)'. The address of this Hong Kong 'branch' was Holly Mansion Building, 37 Kimberley Road, 4th floor, B flat, Kowloon. They subsequently registered their new address viz, 606 Tung Ying Building, 100 Nathan Road, Kowloon. In an affidavit filed by the defendants' manager in Hong Kong, he says:

The office of the defendants in Hong Kong is primarily an inspection office set up to inspect goods ordered by the head office normally placed by the head office direct with manufacturers in Hong Kong and documentation and correspondence sent direct from the parent company to manufacturers and vice versa.

The defendants' argument is that although they undoubtedly carry on business in Hong Kong – and for gain – within the meaning of ss 2 and 5 of the Business Registration Ordinance they cannot be said to have established a place of business within the meaning of Pt XI of the Companies Ordinance.

There are a number of decisions on this point, viz *Lord Advocate v Huron and Erie Loan and Savings Co* 1911 SC 612, *Banque des Marchands de Moscou (Koupetschesky) v Kindersley* [1951] Ch 112, *Deverall v Grant Advertising Inc* [1954] 3 All ER 389 and *Re Lloyd Generale Italiano* (1885) 29 Ch D 219. The effect of these decisions is summarised by the learned editors of *Palmer's Company Law* (20th edn) at p 761 in these words:

A company has an established place of business in Great Britain if it has a specified or identifiable place at which it carries on business, 'a local habitation of its own', eg an office; there must be some particular premises. It is not sufficient for the company to carry on business through an agent.

Sample orders, letters of confirmation, etc emanated from both the defendants' head office in Sweden and from their local office in relation to the same business transactions. Although the letter heads on such documents do not

<sup>12</sup> Though this case was decided prior to the amendment in 1984 to the s 341 definition of a place of business: see p 516 below.

<sup>13</sup> Any person or entity which carries on business in Hong Kong, subject to certain minor exceptions, is required under criminal penalties to register under the Business Registration Ordinance (Cap 310). The BRO is maintained by the Inland Revenue and its principal purpose is to provide the Revenue with the names and addresses of persons to whom profits tax returns will be sent. For details see (1971) 1 HKLJ 288.

contain anything to indicate that AB Hellenic is a company incorporated in Sweden, there is nothing to indicate that their Hong Kong office is a legal entity independent of the Swedish company. Indeed, the evidence is all the other way. The plaintiffs did not check either the Companies Registry or the register kept under the Business Registration Regulations before commencing this action. These are public registers; and it seems to me that the defendants' registration under the Business Registration Regulations constituted a notice to the world that, as a foreign incorporated body, they were carrying on business in Hong Kong.

I do not wish to say anything which might prejudice the defendants should any person institute proceedings under s 340 of the Companies Ordinance. But, in my view, the defendants have established a place of business within the meaning of Pt XI of the Companies Ordinance. If I am correct in this view, the defendants are in breach of s 333 of that Ordinance; and, if that is so, the sooner they mitigate their default the better.

*A foreign company which appoints an agent in Hong Kong and has no office or other place of business of its own in Hong Kong will not generally have an established place of business in Hong Kong.*

**MCY Finance Ltd SA v Hong Kong Shanghai (Shipping) Ltd**  
[1986] HKC 323  
(Hong Kong High Court)

The defendant, incorporated in the Bahamas, was a wholly owned subsidiary of Hongkong Bank. WSS was a wholly owned subsidiary of the defendant. WSS was the defendant's agent in Hong Kong and authorized to represent the defendant in Hong Kong in relation to the shipping finance business.

**Mayo J:** [Counsel] referred to *Artemis v Artemis Transportation Corp* [1983] HKLR 364 as authority for the proposition that the burden of proof of satisfying the court that the defendant has established a place of business in Hong Kong lay upon the plaintiffs....

Before considering the law in any detail, it is necessary for me to consider the extent to which the plaintiffs has succeeded in discharging this burden on the facts.

I am, by no means, satisfied that the functions which are performed by WSS and the defendant could remotely be described as a sham or a facade. I accept that any officer making decisions on such matters as the credit-worthiness of customers must use a number of different sources of information before deciding whether or not to advance moneys. The fact that WSS or the Hongkong Bank may make recommendations is neither here nor there. It was necessary for the defendant to get advice from Hong Kong before loans were granted. It is also highly significant to observe that nowhere in the papers is it suggested that the defendant actually made any loans in Hong Kong. Normally, arrangements were made for payments to be made in New York, if the currency concerned was US dollars.

I will now endeavour to deal with the position in relation to the law. Lord Dunedin in *Lord Advocate v Huron and Erie Loan and Savings Co* [1911] SC 612 suggested as a test the local habitation of the company. He accepted that an established place of business was an entirely different matter to carrying on business in the jurisdiction. This distinction was also accepted by Lord Cohen in *Re Tovarishestvo Manufactur Liudvig-Rabenek* [1944] Ch 404.... Assistance can also be derived from *South India Shipping Corp Ltd v Export-Import Bank of Korea* [1985] 1 WLR 585 which can readily be distinguished from the present case. Here, there is no question of the defendant having taken out a lease of the premises at China Building. *The Theodosus* [1977] 2 Lloyd's Rep 428 and *Re Oriel* [1986] 1 WLR 180 are both also of assistance. I do not think that on the law the plaintiffs have satisfied me that the defendant who is, of course, the party which is being sued, has 'an identifiable or recognizable place of habitation in the colony' which is the test according to the cases I have referred to.

The consequence of this is that the plaintiffs have not satisfied me that the defendant has established a place of business (in Hong Kong)....

#### NOTE:

The basic proposition revealed by the Hong Kong case law<sup>14</sup> is that a foreign corporation will not have established a place of business in Hong Kong if, rather than opening an office in Hong Kong, it appoints an agent in Hong Kong and that agent manages all the foreign corporations business dealings in Hong Kong. In such circumstances the place of business will be the agent's place of business – it will not be the foreign corporation's place of business. In other words, when the Ordinance talks of a foreign company which establishes a place of business in Hong Kong, that means establishes its own place of business.

Where a foreign corporation has indeed established a place of business but has failed to register, then the penalty imposed is a fine (see s 340); the Ordinance does not (as is for instance the case in many Canadian Provinces<sup>15</sup>) impose any civil disabilities upon the offending corporation.

#### REPRESENTATIVE OFFICES AND PART XI

In the English case of *South India Shipping Corp Ltd v Export-Import Bank of Korea* [1985] 2 All ER 219 the Court of Appeal held that the words place of business should be given their ordinary

<sup>14</sup> See *The Artemis* [1983] HKLR 364 and *English Sewing (HK) Ltd v Eastern Shipping Lines Inc* [1984] HKLR 5; note also *Chingman Co v Popular Fabrics Inc* [1963] HKLR 855, *Pang v Windsor Industries Inc* [1977] HKLR 271 and *Zhang You (China) Design Co v Fuyuan Landmark (Shenzhen) Ltd* [1996] 2 HKC 342 at 347.

<sup>15</sup> See, eg the Business Corporations Act 1981 (Alberta) s 266(1).