

TRAINING TIPS

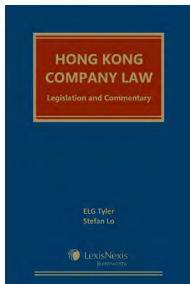
Lexis Advance® Hong Kong – Company and Corporate Law Resources



Hong Kong Corporate Law

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Hong Kong Company Law: Legislation and Commentary

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Under the circumstances of COVID-19 pandemic, business disruptions have become the new normal for dealings in the commercial context. Companies may transform or restructure themselves to enable their businesses to continue amid the COVID-19 outbreak. *Hong Kong Corporate Law* and *Hong Kong Company Law: Legislation and Commentary* equip you a comprehensive coverage and guide across different company and corporate legal topics with regular updates on legislations' amendments, case laws and some practical tips for your legal practice.

CHAPTER IX RESTRUCTURING AND WINDING UP

- CHAPTER IX Restructuring and Winding Up
 - 1. Corporate Transformation and Restructuring
 - Takeover and Acquisition of Minority Shareholding
 - 2. Company Liquidation, Winding Up and Dissolution

CHAPTER IX Restructuring and Winding Up

1. Corporate Transformation and Restructuring

[1] Methodology, Forms and Types

From time to time, companies may transform or restructure themselves, which will result in a change in the capital structure or shareholding control, with the transfer of assets and business undertakings, having exercise and reduction of debt exposure, in rescue operation including realisation of floating status as the only assets and in privatisation.

[2] Capital structure

This may involve the increase of authorised share capital, subdivision and consolidation of shares (see s.132 of Cap.622), the allotment of shares by conferring the board with general mandate to allot shares (see ss.140–141 of Cap.622), the designation of new classes of shares including those redeemable in nature (see ss.233–234 of Cap.622) or having no voting rights (see s.172 of Cap.622), buyback and redemption of shares for privatisation (see ss.233, 234, 252 and 258 of Cap.622), reduction of capital (see ss.209–212), utilisation of merger relief and group reconstruction relief (see ss.156–157 of Cap.622), distribution of profits (see ss.237, 239 of Cap.622) and utilisation of other (see such as capital redemption reserve.¹

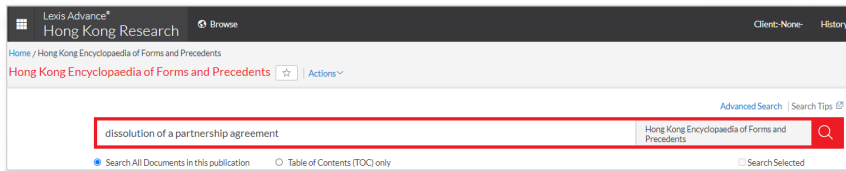
[3] Shareholding control

Control is a relative concept. It could be acquired from existing shareholders' interest or through allotment by the company.² Unfair advantage can be taken by the majority shareholders over the minority shareholding by giving a mandate to the board controlled by the majority to allot shares to them at a price below the fair market value of the shares. The existing shareholding of minority shareholders will then be diluted. The benefits (including participation in profits and voting) associated with the shareholding will comparatively be reduced. A common issue is to acquire complete control and the question is whether the minority shareholders' interest can be subject to compulsory acquisition. This can be achieved by either of the following ways:

- Through selective reduction of the company's capital.³ The majority shareholders may obtain complete and absolute control if the minority shareholding can be extinguished. The involvement of the company in the exercise by a share buyback is only possible if the minority shareholders agree to be bought out. Expropriation of shares by way of capital reduction could also be possible where this is made pursuant to the terms of issue of any preference shares, if it is not by way of redemption. A related concept is to renege or reallocate rights of shareholders from voting into non-voting. Rights attached to certain classes may then be deferred in the sense that they become valueless. Those who hold voting shares will then gain complete control of the company.⁴
- By way of a takeover: s.239 of Cap.622. As shall be seen later, the Companies Ordinance (Cap.622) contains a prescribed procedure for compulsory acquisition in respect of a takeover offer when accepted by a large majority of shareholders (60%). Further, those who acquire control are usually outsiders who may or may not be related to the majority shareholders. Acquiring complete control by way of a takeover can be pursued through a scheme of arrangement by a 'cancellation and reduction scheme' or by a 'transfer scheme'.⁵
- By way of a scheme of arrangement: s.112 of Cap.622. This section and its associated sections provide that a compromise or arrangement effected in a manner set out shall be binding on all creditors or members or classes, as appropriate, notwithstanding the fact that there may be dissenting minority.
- By way of a successful general offer to buy back its own shares in the case of a listed company pursuant to ss.238 to 243 of Cap.622.

The change is obvious. Companies issue shares to finance additional working capital for expansion or to reduce debt. Different shares may be designated to cater for different investors, though in the case of a joint venture or a closely controlled company, a share can be used to protect founding members by conferring them a right of veto on certain issues. An increase in capital plus control of those companies which are vulnerable to takeover.⁶ Rights may be reduced when the companies are under or return on capital employed. An exit venue may be conferred on an outgoing shareholder of a private company if no dividend is being over this share of the outgoing shareholder through the company redeeming or buying back its shares to shareholder. Sometimes, the articles may provide for the mechanism whereby a company will reduce its capital to acquire a shareholder's interest or to return a shareholder's share entitlement to his personal representative. The extinguishment of capital can be proceeded with by way of capital reduction where the court's sanction is required. This happens in relation to the non-voting shareholders enjoying a high fixed dividend rate well above the costs of capital and which have ended the income of the which distribution the ordinary shareholders would otherwise be entitled.

For example, our "Restructuring and Winding Up" chapter shares with you some commentaries, the relevant legislations, any recent common law cases and practice procedures should a company wishes to change its capital structure or shareholding control preventing a closure of the business.



In some unfortunate situations, partners may agree to cease their business operations. Explore more in our *Hong Kong Encyclopedia of Forms and Precedents*, *Atkin's Court Forms Hong Kong* and *Practical Guidance* and you will come across to a wide range of business organizations templates, such as agreement for dissolution, for drafting purposes. Simply search within our publication for locating a standard agreement for dissolution of a partnership.

Table of Contents

16.3 Agreement for dissolution of a partnership and closure of the business, all assets being sold

Hong Kong Encyclopaedia of Forms and Precedents

[Hong Kong Encyclopaedia of Forms and Precedents](#) > [BUSINESS ORGANISATIONS PARTNERSHIP](#) > [FORMS AND PRECEDENTS](#) > [C: PARTNERSHIP ADMINISTRATION AND DEALINGS](#) > [16: DISSOLUTION](#)

16.3 Agreement for dissolution of a partnership and closure of the business, all assets being sold ⁴

[1420]

THIS AGREEMENT is made on (date) BETWEEN:

(1) (first partner) of (insert address) ("Mr A"); and
(2) (second partner) of (insert address) ("Mr Z").

NOW IT IS AGREED as follows:

5 Assets and liabilities for disposal or discharge by the partnership

[1423]

5.1 All assets of the Partnership whatever their nature shall be sold, disposed of, collected and got in to the best advantage of the Partnership and the proceeds of them shall be paid into the Partnership's bank account.

5.2 All debts and liabilities of the Partnership shall be paid and discharged by the Partnership from the Partnership bank account.

5.3 [The provisions of clauses 5.1 and 5.2 shall be carried into effect by the Partners acting jointly.

(or)

The provisions of clauses 5.1 and 5.2 shall be carried into effect by [Mr A] acting alone. [Mr A] shall, in this respect, act to the exclusion of [Mr Z], who shall have no authority to act in any such regard on behalf of the Partnership.

[5.4 (if the 2nd version of clause 5.3 is used) [[Mr A] shall not be entitled to any reward or remuneration for the discharge of the duties conferred on him by this clause 5 (or) In consideration of the discharge by him of the duties conferred on him by this clause 5 [Mr A] shall be entitled to remuneration payable by the Partnership from its bank account as an expense of the winding up of the Partnership's affairs, which shall therefore for the purpose of preparation of the Final Accounts in accordance with clause 7 be regarded as payments to a third party. The remuneration shall be [at the rate of HK\$... a [month] from the Cessation Date until the completion of his duties, payable in advance on the first day of each month, the first and last payments being apportioned as necessary (or) equal to [10%] of the gross amount realised by him for any asset of the Partnership].]]