

Company Types

Types of Companies

There are mainly three types of companies which can be selected for forming business entities in Hong Kong, namely sole proprietorship, partnership and incorporated company. Different company types imply different ownership structures and the companies formed have different legal status. Liabilities borne by company members and registration formalities for setting up business under each type of company are also different from one another.

A sole proprietorship, partnership or an incorporated company must be registered with the Business Registration Office of the Inland Revenue Department (IRD), and its valid business registration certificate must also be displayed in a conspicuous place at the address where the business is carried on. For details of the business registration fee and levy, please refer to IRD's website (<https://www.ird.gov.hk/eng/tax/bre.htm>).

However, the issuance of a business registration certificate does not mean that the business can be commenced immediately as some businesses are subject to other kinds of licensing requirements or operators of the businesses are required to possess recognised professional qualifications. Business operators should check with relevant departments about applications for various licences and stipulations concerning recognised professional qualifications before commencement of business.

Sole Proprietorship

Sole proprietorship is a business run by a single individual in the name of that person. A sole proprietor can hire employees to assist in business operations. However, a sole proprietor will have to be accountable for the profit, loss and debts of the company.

It is very simple to form a sole proprietorship. A person only needs to register the business with the Business Registration Office of the IRD within one month of the commencement of the business. Business registration has to be renewed every year.

As it is very simple and easy to form a sole proprietorship company in that the sole proprietor only needs to be responsible to himself/herself without any constraints from investors, sole proprietorship can be regarded as the most flexible business entity. If a business starter has sufficient capital and possesses relevant business expertise, or wants to keep the trade secrets from other investors or staff, he/she can consider operating business in the form of a sole proprietorship.

A sole proprietor in general has to bear all the risks and liabilities of the company. If the business becomes insolvent, the sole proprietor is still personally liable to business debts, and the liabilities to be borne is unlimited.

The greatest challenge faced by a sole proprietorship in general is the need to raise all the working capital by himself/herself. As the saying goes, “two heads are better than one”, many business issues may not be solved merely by personal efforts. A sole proprietor can consider employing staff, consulting advisors, or seeking assistance from business partners.

Partnership

According to the Partnership Ordinance, Chapter 38, Laws of Hong Kong, partnership is the relation which subsists between persons carrying on a business in common with a view of profit. Partnership is a business entity formed by two or more partners.

The characteristic of partnership is that every partner is an agent of the company and all the other partners. Acts taken by any partner in the course of running the business can bind the company and all the other partners. As a result, partners have to share all the debts of a partnership in a joint and several manner.

Business starters can form –

- i. **Limited Partnership** – According to the Limited Partnerships Ordinance, Chapter 37, Laws of Hong Kong, a limited partnership must consist of one or more persons called general partners, who shall be liable for all debts and obligations of the company, and one or more persons called limited partners, who shall, at the time of entering into such partnership, contribute thereto a sum or sums as capital or property valued at a stated amount, and who shall not be liable for the debts or obligations of the company beyond the amount so contributed. The Ordinance also stipulates that a limited partner shall not take part in the management of the partnership, and shall not have power to bind the firm.
- ii. **General partnership** – Each limited partner must be registered under the aforesaid Ordinance. If not registered, it must be regarded as a general partnership, and each limited partner must be regarded as general partner.

Moreover, limited partnership must also be registered with the Registrar of Companies. As there are more restrictions for limited partnership in comparison with general partnership, business starters in general tend to run their business in general partnership or limited company.

It is also quite simple to form a partnership. However, since a partnership involves the cooperation and rights among the partners, partners should enter into a contract in the first place. A contract can be drawn up by partners themselves, or be prepared by a lawyer after negotiation among partners. While verbal agreement is also a kind of contract, business starters should draw up a written contract in order to avoid disputes over the rights and obligations of partners in the future.

As partners have enormous obligations to themselves and to the business of the partnership, a contract should preferably be drawn up before the partnership is established and the company commences operation. A contract should include the following –

- Formation date and name of the partnership
- Names and particulars, ownership percentage and investment amount of the partners
- Role, work, rights and obligations of the partners
- Way and ratio in which profits and losses are shared, and way of handling partnership property
- Way of handling disputes among partners
- Mechanism for the withdrawal of existing partners and the joining of new partners
- Terms and way of dissolving the partnership

Partnership is an operation mode which combines capital and people. It is certainly better than sole proprietorship in terms of availability of resources. Partnership nevertheless has its disadvantages. As partnership involves several partners, lack of communication, disagreement or even mutual distrust among partners could greatly disrupt business operations and potentially lead to dissolution of the partnership. The risk of partnership mainly arises from the trust among the partners and trust relationship with the company, as well as its characteristic of unlimited liabilities on the partners. The liabilities caused by a wrong commercial decision made by a partner have to be borne unlimitedly by all the partners. Business starters are advised to consider thoroughly before joining partnership.

Incorporation

Hong Kong company law is mainly specified in the Companies Ordinance, Chapter 622, Laws of Hong Kong. Any one or more persons can form an incorporated company with limited liability or incorporated company without limited liability for a legitimate purpose according to all the provisions concerning the formation and registration of companies in the Companies Ordinance.

From the legal perspective, an incorporated company is a separate legal entity, that is, investors and the business operated by them are two separate legal entities. A sole proprietor or partners in a partnership can sue or be prosecuted because of the company business, while an incorporated company can enter into contracts, sue or be prosecuted in the name of a company.

Incorporated companies formed under the Companies Ordinance can be classified into the following three categories in respect of members' liabilities –

- i. Company limited by shares – The liabilities of members of the company limited by shares are limited to any amount unpaid on the shares held by the members. Any person who subscribes for or holds shares in a company becomes member of the company regardless of whether it is made in personal capacity or in the name of other incorporated companies. As members are holders of shares in a company, they are also

called shareholders. Most of the incorporated companies in Hong Kong are registered in the form of company limited by shares.

- ii. Company limited by guarantee – Company limited by guarantee does not have a share capital and the liabilities of the members are limited by the articles of association of the company to the amount that the members respectively undertake to contribute to the assets of the company in the event of its being wound up. Some non-profit-making organisations in Hong Kong are registered in the form of company limited by guarantee.
- iii. Unlimited company – Similar to a partnership, there is no limit on the liabilities of members of an unlimited company. Unlike a partnership, an unlimited company enjoys a separate legal entity status. Since an unlimited company is similar to a partnership, most business start-ups tend to form a company in the form of partnership to dispense with the registration procedures and requirements for incorporating a company.

In addition, company limited by shares can be classified into the following two categories –

- i. Private company limited by shares – Section 11 of the Companies Ordinance stipulates that a company is a private company if –
 - (a) the following restrictions are imposed in its articles of association:
 - 1. restrict a member’s right to transfer shares;
 - 2. limit the number of members to 50 (excluding a member who is an employee of the company, as well as a person who was a member while being an employee of the company and who continues to be a member after ceasing to be such an employee); and
 - 3. prohibit any invitation to the public to subscribe for any shares or debentures of the company; and
 - (b) it is not a company limited by guarantee.
- ii. Public company limited by shares – Section 12 of the Companies Ordinance stipulates that a company is a public company if it is not a private company and it is not a company limited by guarantee. It should be noted that a company must be incorporated as a public company if its number of members exceeds 50. Meanwhile, there is no such a restriction in a public company’s articles of association that prohibits any invitation to the public to subscribe for shares or debentures. The public can therefore become a shareholder of a company by purchasing its shares. A public company is called a listed company if the share dealings are conducted in various approved stock exchanges. Furthermore, a public company does not enjoy the rights and immunity that a private company does. For instance, under Section 662 of the Companies Ordinance, a public company must deliver to the Companies Registry an annual return which includes a financial statement containing auditor’s report and directors’ report, while a private company is not required to deliver account-related information to the Companies Registry.

Basically, the organisation of an incorporated company can be divided into two parts: (i) Shareholders are members forming a company as well as a company’s investors. Interests of a company are also the interests of

all the shareholders. Although shareholders are holders of the company's shares, it does not mean that they are the persons responsible for a company's operations because business management and shareholding of an incorporated company are separated. (ii) Management, namely the directors of a company, are responsible for management and operations, as well as protection of shareholders' interests. Directors do not necessarily hold shares of a company unless they are also the company's shareholders.

The procedure of forming an incorporated company is more complicated when compared with that of a sole proprietorship and a partnership. Taking a company limited by shares as an example, the relevant company registration procedure is as follows:

- i. Choosing a company name. A registration application in which the intended company name is same as those already registered will not be accepted by the Companies Registry. Therefore, business start-ups should first find out whether the intended company name has already been registered before by conducting a company name search free of charge through the Companies Registry's e-Services Portal (www.e-services.cr.gov.hk) or onsite at the Registry's e-Services Centre (13th Floor, Queensway Government Offices, 66 Queensway).
- ii. Compiling the company's articles of association and completing Form NNC1 "Incorporation Form (Company Limited by Shares)" specified by the Registrar of Companies, together with IRD's IRBR1 "Notice to Business Registration Office", and then delivering them with the fee payable to the Companies Registry either in electronic form (through the Companies Registry's e-Services Portal) or in hard copy form. For information regarding a company's articles of association, business start-ups can consult the schedules of the Companies (Model Articles) Notice (Chapter 622H). Schedule 1 and Schedule 2 thereto prescribe the model articles of association to be adopted by public companies limited by shares and private companies limited by shares respectively. Business start-ups can also use samples of articles of association of different types of companies provided by e-Services Portal for applications delivered in electronic form. The full text of the Companies Ordinance and the aforementioned Notice are available at www.elegislation.gov.hk. Details of the fees are available at the Companies Registry's website (www.cr.gov.hk) and the IRD's website (www.ird.gov.hk). The aforementioned forms NNC1 and IRBR1 can be downloaded from the Companies Registry's website (www.cr.gov.hk).
- iii. In general, if a registration application is delivered in electronic form, an electronic Certificate of Incorporation ("C.I." in short) and Business Registration Certificate will be issued to the company within an hour; if a registration application is delivered in hard copy, certificates in hard copy will normally be issued within 4 working days (excluding the day of delivery). Certificates in electronic form or hard copy have the same legal effect. After incorporation, a company must comply with the requirement of the Companies Ordinance to deliver statutory returns to the Companies Registry timely for registration. Relevant information pamphlets and forms can be downloaded from the Companies Registry's website (www.cr.gov.hk).

Business start-ups can also appoint accountants, lawyers or commercial secretary firms to act on their behalf for completing the procedures for incorporation of limited company.

There are many advantages of forming an incorporated company. First of all, it is a separate legal entity which can own property, operate and enter into contracts in the name of the company. In addition, given the separation of management rights and shareholding, the continuity of a company will not be affected even if there is a change in company's directors and shareholders. Shareholders can also transfer their shares to others at any time without affecting the company's operations. More importantly, if a company is registered as a limited company, shareholders' liabilities are "limited" in the sense that the liabilities are limited to the amount of investment of the shareholders only. If a company is being wound up due to debt problems, shareholders are not required to repay the debt with personal property. Thus, the operational risk faced by business start-ups is reduced to a predictable level.

Nevertheless, the procedures of forming an incorporated company and the annual reporting and auditing procedures are complicated. Apart from incorporation fees, a company also needs to bear the expenses of auditing and company secretarial fees every year. A company must deliver its annual return to the Companies Registry every year to report particulars of the company such as capital structure, shareholders and management, which are made available for public inspection. A public company is required to disclose even more information including financial statements containing auditor's report and directors' report. On the other hand, there is no minimum requirement on an incorporated company's share capital. A company limited by shares can be formed by just one person who signs the articles of association.

Many banks or financial institutions will require shareholders or directors of a company to provide personal guarantees when lending to limited companies with limited share capital. Quite a number of landlords of commercial buildings or shops will also impose similar requirements on these company tenants.

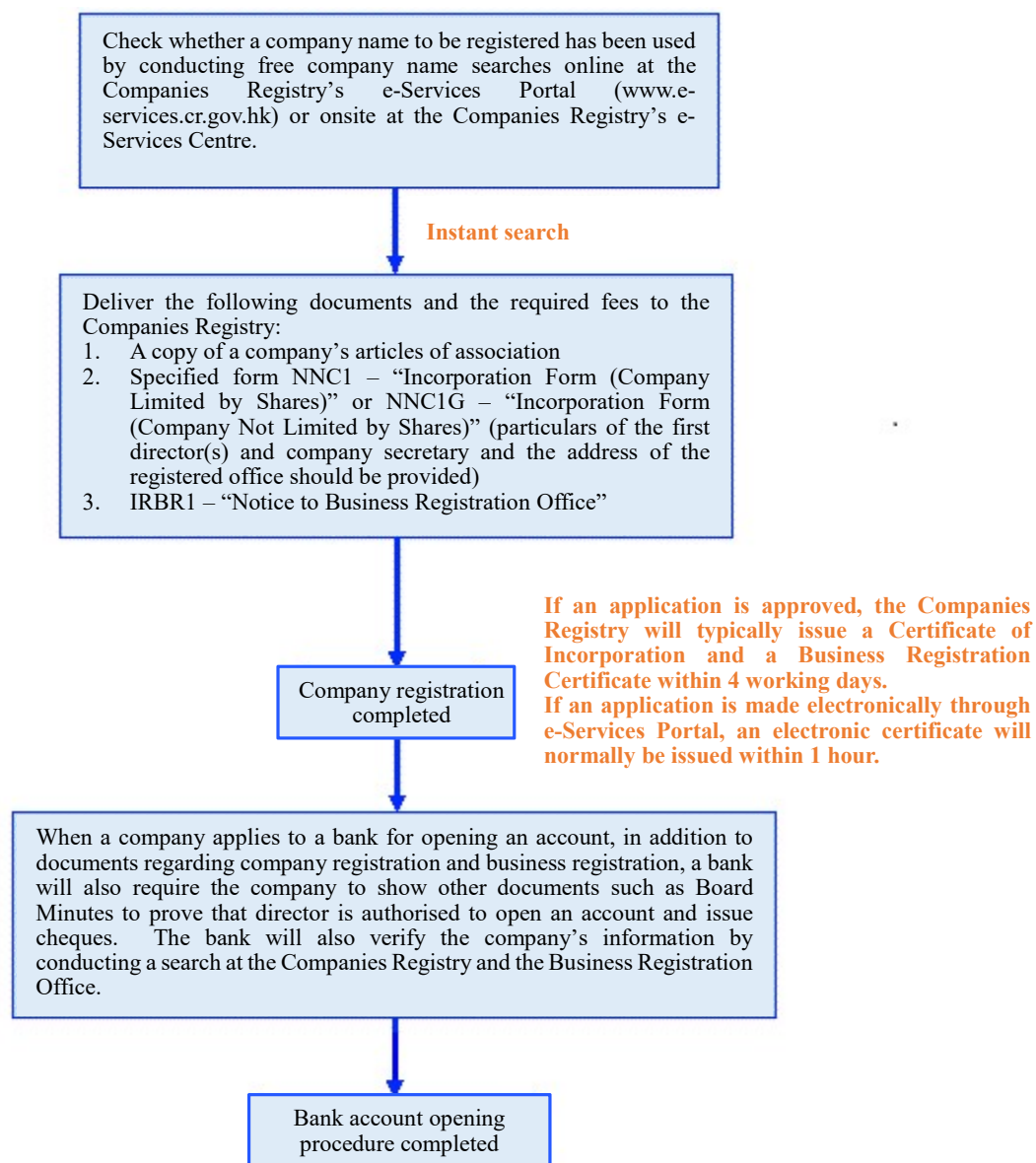
Comparison of Sole Proprietorship, Partnership and Incorporated Company

	Sole Proprietorship	Partnership	Incorporated Company
Start-up Procedure	Register the business within one month from the date of commencement of business.	Partners enter into a contract and register the business within one month from the date of commencement of business.	Register the company and business after drawing up the shareholding and directorship structure. Consideration may be given to engage an accountant or lawyer for handling the above procedures.
Fees and Expenses Thereafter	For details of business registration fee and levy, please visit the IRD website at https://www.ird.gov.hk/eng/tax/bre.htm .	Same as sole proprietorship.	Required to pay the company registration fee, business registration fee and the levy for the Protection of Wages on Insolvency Fund. (For details of the company registration procedures and fees, please visit the website at www.cr.gov.hk .) Additional fees apply if an accountant or lawyer is engaged. Annual payments have to be made thereafter for registration fees for annual returns and audit fees of the accountant which depend on the complexity of the accounts.
Debts / Liabilities	The operator shall bear unlimited debts and liabilities of the firm.	Partners shall share all the debt obligations, debts and liabilities arising from operation without ceiling (except limited partnership).	The obligations are limited to the assets held by the company, and the obligations of a shareholder are limited to the amount of investment in shares only and no personal property is involved. The above are not applicable to unlimited companies.

	Sole Proprietorship	Partnership	Incorporated Company
Number of Operators	1 person.	2 or more persons.	1 or more persons. A company with more than 50 shareholders shall be registered as a public company.
Management and Ownership of the Company	The operator has managerial control over all the titles of the company.	The contract among partners will stipulate the details of the management and titles of the partnership. All partners have equal management and titles if there is no specific stipulation.	The directors have managerial control over the company. The shareholders share the titles of the company according to the shareholding ratio but do not have managerial control.
Taxation	The operator is assessed to personal income tax with reference to the profits. The owner may be granted tax allowances by electing Personal Assessment.	Partnership firm is assessed to Profits Tax. An individual partner may be granted tax allowances by electing Personal Assessment.	An incorporated company is assessed to Corporate Profits Tax. After-tax profits may be distributed to shareholders as dividends. Shareholders shall not be taxed again for the dividends.
Continuity of the Company	The transfer, bankruptcy or cessation of the company by the operator will lead to the end of business.	Under the Partnership Ordinance, a partnership is dissolved by the death, bankruptcy or mental disorder of any partner or in situations specified under other ordinances, subject to any agreement between the partners.	An incorporated company is a separate legal entity. Transfer of shares, bankruptcy or death of an individual shareholder will not lead to the end of business.
Audits by Auditors	Not necessary.	Not necessary.	Under Section 394 of the Companies Ordinance, the company must appoint an auditor for audits each year.

	Sole Proprietorship	Partnership	Incorporated Company
Capital and Assets	All capital is raised by the sole proprietor who also owns all the assets personally.	Capital is raised by the partners. Assets are wholly or partially owned by the partners (subject to the details in the partnership agreement).	Capital is raised by the company members. Assets are held in the name of the company.

Flowchart of an Incorporated Company from Incorporation to Bank Account Opening



Note: For information such as bank account opening process, information required and contact details of banks, please visit the Hong Kong Monetary Authority's webpage at <https://www.hkma.gov.hk/eng/smart-consumers/account-opening/>.

Source: “Guide for Starting Business in Hong Kong”, which is published online in Chinese on Support and Consultation Centre for SMEs (SUCCESS)’ Website at https://www.success.tid.gov.hk/tc_chi/sgbook/chapter_00.html. The information provided is an English translation of the original publication.