From 1 March 2018, all Hong Kong incorporated companies (except those listed in Hong Kong) will be required to maintain a register of significant controllers (SCs). This reflects the government’s commitment to combat money laundering and terrorist financing by enhancing transparency of company ownership and control, and echoes similar requirements that have been put into place in jurisdictions such as the UK, Singapore, Cayman and BVI. The requirements will be implemented through Part 12 of the Companies Ordinance (the CO). The Companies Registry has issued guidelines (the Guidelines) on the operation of the new rules.

Overseas companies with Hong Kong incorporated subsidiaries need to be aware of the regime (but not those which only have Hong Kong branches or non-Hong Kong companies registered in Hong Kong) as each of the Hong Kong incorporated subsidiaries will fall within the scope of the regime.

The purpose of the register of SCs (the Register) is to enable law enforcement authorities to be informed, in an easily accessible manner, of certain beneficial ownership information. In broad terms, a company’s SCs are (i) natural persons and (ii) corporate entities immediately above the company in the ownership chain, with “significant control” over the company. Notably (and unlike the UK), the Register will not be publicly available. It will be a criminal offence for a company (and its officers in default) to breach the key provisions.

This briefing gives a general overview of the new regime, highlights some practical issues, and summarises what action companies need to take.

### Key Dates for Existing Hong Kong Companies

<table>
<thead>
<tr>
<th>Date</th>
<th>Action</th>
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<tbody>
<tr>
<td>1 March 2018</td>
<td>Legislation comes into force:</td>
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<tr>
<td></td>
<td>• start keeping a Register at the company’s registered office or a place in Hong Kong</td>
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<td>• record the appropriate entries (including details of designated representative). See section below entitled “Completing the Register”</td>
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<tr>
<td>From 1 March to 8 March 2018</td>
<td>In respect of a person or entity whom you know or have reasonable cause to believe is an SC on 1 March 2018:</td>
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<tr>
<td></td>
<td>• you should issue a notice to that person (or others who might know that person) between 1 March and 8 March. See the section entitled “Giving notices” for an exception to the notice requirement</td>
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<td>• in the case of a registrable legal entity (the meaning of which is explained below), if, on 1 March, you already know any of its required particulars, enter those particulars no later than 8 March. The particulars of a registrable person (the meaning of which is explained below) can only be entered after that person has confirmed all required particulars on or after 1 March</td>
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KEY ACTION POINTS FOR COMPANIES

- Take “reasonable steps” to identify SCs. This includes (but may not be limited to) reviewing your register of members, constitutional documents and any shareholder agreements.

- Obtain the required information from the SCs you have identified (or from others who might know them) generally by issuing written notices. The Guidelines contain template notices. Familiarise yourself with the required process and deadlines for issuing the notices, as well as the permitted exception.

- Produce the Register in hard copy or electronic form (see Annex A to the Guidelines for reference).

- The Register cannot be blank on Day 1 - familiarise yourself with the information that is required to be recorded in different circumstances (prescribed wording is set out in Schedule 5C to the CO). Be aware that details of a natural person require confirmation before they can be entered in the Register.

- Appoint a Hong Kong-based designated representative to act as a contact point for law enforcement officers.

- Put in place internal procedures to ensure that information required to be included in the Register can be kept up-to-date, e.g. in the event of group reorganisations.

Overview

The regime applies to any company formed and registered in Hong Kong, except where the company has shares listed in Hong Kong. Hong Kong share-listed companies are exempt as they are subject to the more stringent disclosure of interest requirements under the Securities and Futures Ordinance. The regime does not apply to any companies incorporated outside of Hong Kong (even if they are non-Hong Kong companies registered in Hong Kong). Companies that fall within scope are termed “applicable companies”.

The Register should identify any SCs of the company. Broadly, SCs are:

I. any natural person or government / local authority with “significant control” over the company (known as a registrable person); and

II. any legal entity (which does not fall within (i) above) that is a direct shareholder (i.e. a member) of the company with “significant control” over the company (known as a registrable legal entity (RLE)).

Although the primary motivation for introducing the Register is for companies to record registrable persons (which, in most cases, will be natural persons), legislators felt that, where an individual holds interest through layers of entities, recording the RLE (i.e. a corporate direct shareholder in the applicable company) in the Register would be helpful to facilitate identification of the holding structure (but it was regarded as overly burdensome to require every holding layer to be recorded).

Applicable companies must take “reasonable steps” to determine whether they have SCs (wherever the SCs are based) and if so, to establish their identity.

We expand on the key concepts below.

Significant control

A person or entity can only be a registrable person or RLE if it has “significant control” over the applicable company. This means the person or entity satisfies one or more of the following conditions (the “Specified Conditions”) in relation to the applicable company:

I. directly or indirectly holds more than 25% of the issued shares - note this condition does not distinguish between voting or non-voting shares or different classes of shares. All issued shares should be included in the denominator for the calculation;

II. directly or indirectly holds more than 25% of the voting rights;

III. directly or indirectly holds the right to appoint or remove the majority of directors - this means the right to appoint or remove directors...
holding the majority of voting rights at board meetings on all or substantially all matters;

IV. otherwise has the right to exercise, or actually exercises, significant influence or control over the company (the “Fourth Condition”);

V. has the right to exercise, or actually exercises, significant influence or control over the activities of a trust or firm (not being a legal person), whose trustees or members satisfy one or more of the first four conditions - the reference to “firm” would, for example, catch partnerships / limited partnerships without separate legal personality.

### Indirect holdings

For the first three conditions, a person indirectly holds the shares or rights if such shares or rights are held through a legal entity in which the person has a “majority stake” or through a chain of legal entities where each holds a “majority stake” in the entity below except the last one (being the applicable company). The concept of “majority stake” relates to having: (i) a majority control of voting rights or appointment or removal of a majority of directors of; or (ii) having dominant influence over, the company. The effect is that indirect interests in a company would not usually be relevant unless they are held through a chain of majority-held companies. There is no clarification on the concept of “dominant influence” and how it differs from “significant influence”.

Some illustrative scenarios of indirect holdings are set out below:

Where an applicable company has an RLE that is Hong Kong share-listed, the company must disclose the listed entity as its RLE but need not look through and trace its ownership beyond that RLE. This exemption only applies if the share-listed entity is both listed in Hong Kong and a direct shareholder (i.e. a member) of the applicable company. Interests held indirectly through trusts or partnerships are considered below.

### Meaning of “significant influence or control”

The Fourth Condition serves as a “catch-all” condition to ensure SCs cannot avoid the requirements by artificially structuring their interests so as to fall outside the scope of the first three Specified Conditions. If a person does not meet one or more of the first three Specified Conditions but nonetheless has a right to exercise significant influence or control, or actually exercises significant influence or control, over a company, then he or she will be an SC in relation to that company.

The Guidelines state the following is indicative of “control” and “significant influence” respectively:

I. “Where a person can direct the activities of a company”

II. “Where a person can ensure that a company generally adopts the activities which the person desires”

The Guidance notes that a right to exercise significant control or influence may arise from provisions in articles of association or shareholders agreement, and sets out a non-exhaustive list of examples of when such a right may arise. This includes a person having absolute decision rights or veto rights related to the running of the business, such as “adopting or amending the company’s business plan, changing the nature of the company’s business, making any additional borrowing from lenders, appointing or removing the CEO”.

Guidance in the UK (where the rules also have the “significant influence or control” wording)
clarifies that veto rights that exist for the purpose of protecting minority interests, or decision or veto rights granted to prospective buyers on a temporary basis in M&A transactions (e.g. pending competition clearance), are unlikely, on their own, to constitute significant influence or control. The Guidelines in Hong Kong do not contain similar clarifications.

Examples of a person actually exercising significant influence or control are included in the Guidelines. One example is of a person who is not a director but who is regularly consulted on board decisions and who influences the decisions of the board, such as a “shadow director” (as defined in section 2 of the CO). A further example is a person whose recommendations are always followed by shareholders who hold a majority of the voting rights.

The guidance also sets out a non-exhaustive list of “excepted roles”, which would not, on their own, result in a person being regarded as meeting the Fourth Condition. These roles include:

I. a person providing advice or direction in a professional capacity (such as lawyers and accountants); and

II. a lender under a third party commercial financing agreement.

Nonetheless, if the role has unusual features so that it materially differs from how that role is generally understood, then that person may still be regarded as someone with significant influence or control over the company.

Interests held through partnerships / trusts

There are separate provisions dealing with interests held through trusts or partnerships with no separate legal personality. In very broad terms, trustees of a trust or partners of a partnership who meet any of the first four Specified Conditions may be SCs. Where this is the case, any natural person with (i) a majority stake in such a trustee or partner or (ii) “significant influence or control” over the trust or partnership (e.g. a settlor or beneficiary who is actively involved in directing the activities of the trust), would also be an SC. The Guidelines contain various examples of “significant influence or control” over a trust or partnership.

Other relevant concepts to interpret the Specified Conditions

A joint arrangement exists if two or more persons arrange to exercise all or substantially all their shares or rights jointly in a way that is predetermined and the arrangement has “some degree of stability”. Each of these persons will have their interest combined with the other parties to the arrangement. Thus, if the joint arrangement covers more than 25% of the shares or voting rights of the company or covers the appointment / removal of directors with a majority of board level voting rights, each party to the arrangement will have significant control of the company.

The legislation provides that shares that are held by a nominee for another person are regarded as being held by that other person. Further, a right that only arises in certain circumstances will be taken into account only if those circumstances have arisen or the circumstances are within the control of the person holding the right.

Rights attached to shares which have been charged as security will be treated as held by the security provider (i.e. the chargor) if, except for the purposes of preserving the security’s value or realising the security, the rights are exercisable only in accordance with that person’s instructions or in that person’s interests. This provision, together with the “excepted role” for a lender under a third party financing agreement, means that, lenders (including those with the benefit of unenforced security over shares) will generally not be classified as SCs.

Taking “reasonable steps”

As mentioned earlier, an applicable company must take “reasonable steps” to determine whether it has an SC and, if so, to establish the identity of the SC. The Guidelines state “reasonable steps” may include: (i) a review of “readily available” information such as the register of members, articles of association, statements of capital and shareholder and other agreements; (ii)
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considering interests in the company held by individuals, legal entities, trusts or firms; and (iii) considering any evidence of joint arrangements or other arrangements where rights might ultimately be controlled by the same person. Other actions may have to be taken depending on the circumstances of each case and it will not always be straightforward to determine how far a company should go in its investigations. A company is highly encouraged to keep a record of steps taken.

Giving notices

Unless an applicable company has already been informed that a person or entity is an SC and all their Required Particulars have been provided to the company (in the case of a registrable person, by that person or with that person’s knowledge), the company must issue written notices to persons whom it has reasonable cause to believe are SCs within 7 days after the company first has that knowledge or belief.

For existing SCs, the knowledge or belief will be deemed to start from 1 March 2018 - notices should thus be issued to existing SCs between 1 March and 8 March 2018. A notice is not required to be sent to an existing SC if all the Required Particulars of that SC have been provided (in the case of a registrable person, by that person or with that person’s knowledge) on or after 1 March 2018 (when the regime comes into force) but before 8 March 2018 (the deadline to issue notices). The CO prescribes certain content requirements for the notices and the Companies Registry has provided template notices at Annex D to the Guidelines.

An applicable company also has the power to issue notices to a person (a “Third Party Addressee”) where it knows or has reasonable cause to believe that the person knows the identity of the relevant registrable person or RLE or who knows someone else likely to have that knowledge. This is a broad power and may result, for example, in notices being sent to professional advisers or family members of persons whom the applicable company may have reasonable grounds to believe is an SC.

Completing the register

The particulars of an SC required to be included in a Register (the Required Particulars) include details such as name, address, and ID, passport or registration number (as applicable). The date on which an SC became a registrable person or RLE in relation to the company, and the nature of their control over the company must also be included. The information can be in English or Chinese. For existing SCs, they should be stated in the Register as having become registrable in relation to a company on 1 March 2018.

Required Particulars of a registrable person must be (i) complete and confirmed (either by the registrable person or by another person with the registrable person’s knowledge) before those particulars can be entered in the Register and (ii) entered within 7 days after such confirmation. Confirmations provided prior to 1 March 2018 do not count.

A Required Particular of an RLE must be entered into the Register within 7 days after “the particular comes to the notice of the company”. There is no express requirement for Required Particulars of an RLE to be confirmed by the RLE prior to being recorded in the Register.

The Register can never be blank. Even if a company has no SCs, that fact should be noted. Prescribed wording set out in Schedule 5C to the CO must be included in the Register for each outcome. If the company is still in the process of identifying its SCs or awaiting confirmation on the information it has in respect of the SC, there is prescribed wording to that effect which must be entered in the Register.

In summary, on 1 March 2018, the Register of an existing company can contain the Required Particulars of SCs if those particulars are already known to them and if (in the case of a registrable person) all the Required Particulars have been confirmed by that person on (but not before) 1 March. If not, the Register should contain prescribed wording to reflect the particular circumstance (e.g. the registrable person has not yet confirmed their particulars, the company’s investigations into whether it has an SC are ongoing, or the company has no SCs).
The Register must be kept in Hong Kong. A prescribed form should be sent to the Companies Registry if the register is not kept at the applicable company’s registered office or in the same place as its register of members as previously notified to the Companies Registry.

A failure to take reasonable steps or to issue notices where required is a criminal offence for the company and its responsible officers.

**Responding to a notice**

A notice addressee has one month from the date of the notice to comply with the requirements in the notice. There are criminal sanctions for notice addressees, and any “related persons” of a corporate addressee, who fail to comply within the deadline (unless the addressee can prove the notice was frivolous or vexatious), or who knowingly or recklessly give information that is false or misleading in a material respect.

If a Third Party Addressee knows the identity of an SC, the Third Party Addressee is required to provide all the SC’s Required Particulars (except ID and passport number) to the extent it knows them. The legislation permits an addressee to withhold information on the grounds of legal professional privilege. Other than that, an addressee is required to comply with the notice even if this results in breach of, for example, a confidentiality agreement.

The template notices in Annex D to the Guidelines contemplates the addressee should disclose (to the extent it knows them) the details of each level of the chain of ownership with significant control (regardless of whether or not an intermediate company is an SC).

**Updating the Register**

Any change in SC or change to an SC’s Required Particulars that comes to the notice of the company or which the company has reasonable cause to believe has occurred will trigger the requirement to: (i) issue a notice within 7 days, unless, in the case of a registrable person, the information has already been provided to the company by him or with his knowledge or, in the case of an RLE, the company has already been informed of the change; and (ii) update the Register within 7 days after, in the case of a registrable person, all the revised particulars have been confirmed or, in the case of an RLE, the revised particular comes to the notice of the company.

**Designated representative**

An applicable company must designate at least one representative to assist law enforcement officers with the Register. A representative must be: (i) a member, director or employee of the company who is a natural person resident in Hong Kong; or (ii) an accounting or legal professional or a “trust or company service provider” licensee registered in Hong Kong. Thus, if a company does not have (or does not wish to appoint) a Hong Kong-resident shareholder, director or employee, it can appoint (for example) a Hong Kong-registered solicitor or accountant or a Hong Kong-licensed company secretarial services provider. The name and contact details of the representative must be included in the Register.

**Conclusion**

Hong Kong incorporated companies (including overseas companies with Hong Kong incorporated subsidiaries) should familiarise themselves with the SC regime. They should ensure that they have started putting together their Register template(s), have in place processes to obtain (and going forward, update) the relevant information (including template notices) and know the wording that must be entered into the Register on 1 March 2018. They should be ready to send notices to relevant persons between 1 March and 8 March 2018.

Although the legislation is intricate, for most corporate groups with wholly-owned subsidiaries the actual process of identifying and notifying registrable persons and RLEs and recording the required particulars is likely to be fairly straightforward.