

GOVERNANCE IN ACTION

Governance of NGOs in Different Legal Forms

Organizations exist in various forms and legal status in the nonprofit sector in Hong Kong. Nonprofits are commonly referred to as non-governmental organizations (NGOs) locally, although not all NGOs are necessarily “not-for-profit”. Likewise, not all nonprofits are recognized as “charities” with tax-exemption status by the Inland Revenue Department (IRD) pursuant to section 88 of the Inland Revenue Ordinance.¹ Names of NGOs often reflect the nature of their organization or the form of legal establishment, for example, “social enterprise”, “association”, “foundation”, and “society”, etc.

Legal Forms of NGOs

NGOs may be established pursuant to different ordinances that they find most suitable for their operational needs. The most common legal forms can be categorized as follows:

- 1. Society** – registered under the Societies Ordinance (Cap 151). This is more common for clubs or associations that are relatively small.
- 2. Company** – incorporated under the Companies Ordinance (Cap 622). Many charities are companies limited by guarantee where the members have pre-determined limited liability, while some NGOs which allow profit distribution or their capital and voting rights are divided by shares, would normally be incorporated as companies limited by shares.
- 3. Statutory Body** – established by the Hong Kong legislation. NGOs in this category usually have a long-standing history. For example, the Scout Association of Hong Kong Ordinance (Cap 1005) was enacted in 1927 to incorporate the Scout Association of Hong Kong. New NGOs are rarely set up as statutory bodies nowadays in ordinary cases.
- 4. Trust** – a trust company is registrable under the Trustee Ordinance (Cap 29) and individual trustees may be incorporated under the Registered Trustees Incorporation Ordinance (Cap 306). A trust is a fiduciary arrangement (not a legal entity) that allows the trustee(s) to hold assets on behalf of certain beneficiaries.

In this article, we will examine the two most prevalent forms of establishment for NGOs, namely societies and companies, to better understand their respective compliance requirements. While limited companies can be established either by guarantee or by shares, we will only focus on companies limited by guarantee, as it is the form of company that is commonly acceptable by the IRD for granting tax-exemption status.

Society vs. Company

	Society ²	Company Limited by Guarantee ³
Legislation	the Societies Ordinance (Cap 151) (SO)	the Companies Ordinance (Cap 622) (CO)
Responsible Government Department	Police Licensing Office	The Companies Registry (CR)
Requirements on Constitutional Document	Registration documents such as constitution, articles of association or minutes of a meeting are needed to establish the society and show its objects and purposes	Articles of Association (AoA) with mandatory provisions. The company may opt to adopt any or all of the provisions of the Model Articles provided under Cap 662H as the provisions of its own AoA
Legal Status	Unincorporated body (no separate legal status)	Incorporated body (separate legal entity)
Liability of Members	Depending on circumstances, members may be personally liable without limit	Liability of members is limited by the AoA to the amount that the members respectively undertake to contribute to the assets of the company in the event of its being wound up

¹ Inland Revenue Department. (2019). Tax Guide for Charitable Institutions and Trusts of a Public Character.

² Police Licensing Office. (2018). Guidance Notes - Application for Society Registration/ Exemption from Society Registration Under Societies Ordinance, Cap. 151.

³ The Companies Registry. (2017). Incorporation of a Local Limited Company. (Pamphlet)

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	Society ²	Company Limited by Guarantee ³
Liability of Office-bearers / Directors	Must fulfill the statutory obligations under the SO and the fiduciary duties of office-bearers under common law	Must comply with directors' duty of care, skill, diligence under section 465 of and all other statutory obligations under the CO, as well as other fiduciary duties under common law
Number of Responsible Persons Required for Registration	3 office-bearers	At least 2 directors who must be individuals
Company Secretary	No requirement	Must appoint a natural person or body corporate in Hong Kong
Annual Return	No requirement	Prescribed form with particulars of the company, including the address of the registered office, directors, company secretary, etc.; and certified true copies of the financial statements including directors' reports and auditors' report within the required timeline stipulated in the CO
Other Requirements	An application form for change of particulars shall be submitted within one month from the change	The company must comply with other filing and non-filing obligations, ^{4,5} under the CO, otherwise the responsible persons may be subject to a fine or imprisonment

The table above summarizes the major differences between the two forms of legal establishment. In a nutshell, the registration process and the compliance requirements for societies, as compared to companies limited by guarantee, are much simpler. Because of its stringent compliance requirements, limited companies lay down a more solid foundation for governance and urge for a board of directors with considerable expertise. A limited company's independent legal status may provide ease in certain business transactions (e.g. opening bank account, leasing office) and gives protection to their members; whereas the office-bearers of societies may bear more personal risks and responsibilities, given that there is no limit on their liabilities prescribed under the SO.

Good Governance and Directors' Duties

Overall speaking, societies may be more suitable for small NGOs carrying very low risk activities, where legal liability may be very unlikely to incur against the office-bearers and members of the society. The legal form of limited companies may be preferred by NGOs whose activities are subject to government license, legal requirements or contractual obligations, or where their members and directors may otherwise be exposed to personal liability. Yet it is important to note that, while companies as legal entities have limited liability, board members and other responsible persons of the organization may still be legally responsible for their illegal acts or negligence. Failing to perform their duties as board members or commitment of any offence may be personally subject to a fine or imprisonment. For this reason, the CR has a Guide on Directors' Duties⁶ to facilitate board members to comply with their duties. On top of that, all board members or office-bearers, including those of societies and other legal forms, also bear fiduciary duties as an organization's representatives under common law.

All in all, NGOs should decide on a legal form that is most suitable for their operation having assessed the potential legal risks in associate with their activities. Notwithstanding the legal form that an NGO chooses, good governance is still the basis of accomplishing its mission. Agencies' dedication to uphold governance principles should always be above mere compliance.

⁴ The Companies Registry. (2019). Basic Filing Obligations of a Guarantee Company under the Companies Ordinance (Cap.622).

⁵ The Companies Registry. (2019). Basic non-filing Obligations of a Guarantee Company under the Companies Ordinance (Cap. 622) and Companies (Disclosure of Company Name and Liability Status) Regulation (Cap. 622B).

⁶ The Companies Registry. (2014). A Guide on Directors' Duties.