

Establishing a charity in Hong Kong (Part II)

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Setting up a charity in Hong Kong may sound an attractive proposition, but they are subject to more, not less, compliance requirements than ordinary companies.

Part I of this series briefly summarised basic requirements and structures for such establishment. In this second article, the author focuses on requirements on corporate governance of charities, as well as continuing obligations for compliance after establishment.

Governance and compliance

Good corporate governance and compliance is very important to companies, businesses and organisations incorporated in Hong Kong, and the concept of corporate governance covers a lot of aspects.

While legal requirements for corporate governance differ among various types of businesses, they generally include requirements on: accountability of the board of directors, senior management and committees; auditing and reporting; relationships with shareholders and stakeholders; and internal control systems and risk management mechanisms.

Charities, as organisations incorporated and existing under the laws of Hong Kong, must

also have in place a sound governance system subject to a series of compliance requirements.

The Guide to Corporate Governance for Subvented Organisations, issued by the Social Welfare Department, outlines best governance practices for subvented organisations, including charities.

Governing Instrument

Charities must be established by a written governing instrument. In the case of companies limited by guarantee, the governing instrument is their articles of association. The governing instrument should contain clauses that cover:

- Objectives for which the charity is established;
- Limiting application of its funds to achieving stated objectives;
- Prohibiting distribution of incomes and properties among members;
- Prohibiting members of its governing body (e.g. directors, executive committee members, trustees) from receiving remuneration, except in circumstances where the charity can

demonstrate that the payment of allowance or remuneration is necessary and reasonable, in which case the prohibition may be relaxed;

- Requiring members of its governing body to disclose material interest, and not to vote in respect of a transaction, arrangement or contract in which they are interested;
- Specifying how the assets should be dealt with upon dissolution; and
- Requiring the keeping of sufficient records of income and expenditure, proper accounting books and compilation of annual financial statements.

Continuing Obligations

Since 1 August 2018, charities are required to upload audited accounts of every charity fundraising or lottery activity approved by the Social Welfare Department or Home Affairs Department to the fundraising activities page on the GovHK website.

This applies to all charities, regardless of whether exempted from profits tax under section 88 of the Inland Revenue Ordinance.

After confirmation as tax-exempt, charities are subject to the following continuing obligations:

- Submitting accounts, annual reports and other documents to the Inland Revenue Department (IRD) for review of its charitable nature, and if its activities are compatible with the governing instrument. Generally, the IRD performs a review at least every three years on each exempted charity, and the organisation is required to reply within

one month of receiving the IRD's questionnaire;

- Informing the IRD within one month of any changes to its correspondence address, alteration to its governing instrument, termination of its subsidiary body, or cessation of its operation, dissolution or winding-up. Failure of notification may lead the IRD to cease accepting it as a tax-exempt charity;
- If the organisation has earned or is beginning to earn chargeable profits, informing the IRD in writing within four months after the end of the basis period of the relevant year of assessment; and
- Reporting remuneration paid to employees for each year of assessment and preserving such remuneration records, including reporting obligations in respect of the commencement and cessation of employment.

Most charities are companies limited by guarantee, and accordingly must comply with the general requirements under the Companies Ordinance, including the following continuing obligations:

- Preserving corporate records such as the register of shareholders, directors and company secretaries, as well as meeting minutes;
- Notifying the Companies Registry within 15 days of any change to the registered correspondence address, company secretary or director, or company name;
- Companies limited by guarantee should submit an annual return within 42 days from the date of the return (i.e., the end of the nine-month period after the company's accounting reference period), along with certified true copies of the

financial statements, directors' report and accountant's report;

- For each accounting year, an annual meeting among members should be held within nine months after the end of the accounting period;
- If the number of members increases beyond the registered number, the Companies Registry should be notified within 15 days from the resolution of increasing members or the increase itself (whichever is earlier).

While governing members generally cannot receive remuneration, charities should nonetheless assume responsibilities of compliance with corporate governance

obligations with diligence and professionalism.

Qualified auditors should be engaged to audit the accounts and annual reports submitted to the IRD. The full content of annual reports, including a breakdown of received donations, main costs and expenditures, should be published on the IRD website and made publicly available at all times.

Ultimately, charities may be subject to compliance with even more obligations than an ordinary company. For this reason, prior to establishing a charity, founders are advised to thoroughly consider the issues associated with relevant continuous reporting and compliance requirements.

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