

New Companies Ordinance

Briefing Notes on Part 14

Remedies for Protection of Companies' or Members' Interests

INTRODUCTION

Part 14 (Remedies for Protection of Companies' or Members' Interests) of the new Companies Ordinance ("new CO") contains provisions relating to the remedies available for protection of companies' or members' interests. These include the unfair prejudice remedy, the statutory injunction order restraining conduct that constitutes contravention of the new CO, the statutory derivative action, and the right to seek a court order for inspection of company records.

POLICY OBJECTIVES AND MAJOR CHANGES

2. The provisions on shareholder remedies were substantially revised by the Companies (Amendment) Ordinance 2004 with a view to enhancing legal remedies available to members of a company. The amendments included –

- (a) providing for a statutory derivative action that may be taken on behalf of a company by a member of the company (subsequently extended to cover multiple derivative action through Companies (Amendment) Ordinance 2010);
- (b) facilitating members to exercise their rights to obtain access to company records;
- (c) empowering the court, on application by an affected person or the Financial Secretary, to grant an injunction restraining any person from engaging in conduct which constitutes contravention of the Companies Ordinance (Cap. 32) ("Cap. 32") or a breach of his fiduciary or other duties owed to a company; and

(d) improving the unfair prejudice remedy in section 168A of Cap. 32 to provide the court with a power to award damages to the members of a company where it was found that their interests had been unfairly prejudiced and to award such interest on the damages as the court thinks fit. The scope of the remedy has also been extended to allow past members (and their personal representatives) of local companies and members and past members (and their personal representatives) of non-Hong Kong companies to commence legal action under that section

3. Part 14 of the new CO mainly restates the existing provisions with improved drafting, while at the same time introduces the following initiatives that aim at fostering shareholder protection, namely –

(a) extending the scope of the unfair prejudice remedy to cover proposed acts and omissions (paragraphs 5 to 6 below); and

(b) enhancing the court's discretion in granting relief in cases of unfair prejudice (paragraphs 7 to 8 below).

There is also a new provision for an express power for the Chief Justice to make rules relating to unfair prejudice proceedings (paragraphs 9 & 10 below).

4. The details of the major changes in Part 14 are set out in paragraphs 5 to 10 below. The multiple derivative action provisions are restated in Part 14 (paragraphs 11 and 12 below).

Extending the scope of the unfair prejudice remedy to cover proposed acts and omissions (section 724)

Position under Cap. 32

5. Section 168A(1) of Cap. 32 provides that a member of a company may petition to the court if the affairs of the company are being or have been conducted in a manner unfairly prejudicial to the interests of the members generally or of some part of the members. There is some uncertainty whether, under the provisions of Cap. 32, a member can bring an action for unfair prejudice where a course of action is only at the proposal stage, or where there is only a threat to do or not to do something.

Position and key provisions under the new CO

6. The scope of the unfair prejudice remedy is extended to cover proposed acts and omissions. **Sections 723 to 726** restate the unfair prejudice remedy provisions under section 168A of Cap. 32. **Section 724(1)(b)** provides that the court may exercise the power to grant remedies under these provisions if there is any actual or proposed act or omission of the company (including one done or made on behalf of the company) which is or would be prejudicial to the interests of the members. The remedies that may be granted by the court under **section 725** are therefore extended to cover an order restraining the proposed act or requiring the doing of an act that the company has proposed to omit to do.

Enhancing the court's discretion in granting relief in cases of unfair prejudice (section 725)

Position under Cap. 32

7. Section 168A(2) of Cap. 32 provides that orders made by the court (other than for payment of damages and interest) must be "with a view to bringing to an end the matters complained of". This prevents the court from granting a remedy which is unable to meet that requirement.

Position and key provision under the new CO

8. To enhance the court's discretion in granting relief in cases of unfair prejudice, **section 725** provides that the court may make any order that it thinks fit for giving relief in respect of the matter complained of.

Providing for an express power for the Chief Justice to make rules (section 727)

Position under Cap. 32

9. Under Cap. 32, the rules in the Companies (Winding-up) Rules made under section 296 apply to proceedings under section 168A in so far as they are applicable.

Position and key provision under the new CO

10. **Section 727** of the new CO provides for an express power for the Chief Justice, subject to the approval of the Legislative Council, to make rules in relation to unfair prejudice proceedings.

Allowing a member of an associated company to bring a statutory derivative action (section 732)

Position under Cap. 32

11. Prior to the amendment brought about by Part 4 of the Companies (Amendment) Ordinance 2010, the statutory derivative action (“SDA”) provisions in Part IVAA of Cap. 32 only allow a member of a specified corporation to bring an action or intervene in proceedings on behalf of the corporation in respect of misfeasance committed against the corporation. The amendment allows a member of a related company to bring or to intervene in an action on behalf of the corporation, thus expanding the scope of the SDA provisions to cover multiple derivative actions. Sections 731 to 738 of the new CO basically restate the amended provisions.

Position and key provisions under the new CO

12. **Section 732** gives standing to members of associated companies to bring or intervene in proceedings on behalf of the corporation in respect of “misconduct” committed against the company. “Associated company” is defined in section 2(1) to mean a subsidiary or a holding company of a body corporate or a subsidiary of such a holding company. “Misconduct” is defined in **section 731** to mean fraud, negligence, breach of duty, or default in compliance with any Ordinance or rule of law.

TRANSITIONAL AND SAVING ARRANGEMENTS

13. Transitional and saving arrangements are set out in **sections 124 to 127 of Schedule 11** to the new CO and are basically as follows :-

- Section 168A of Cap. 32 and the Companies (Winding-up) Rules continue to apply to an unfair prejudice petition presented before the commencement of Division 2 of Part 14.

- Section 350B(1)(g) and (h) of Cap. 32 continue to apply to an application for injunction made before the commencement of Division 3 of Part 14.
- Part IVAA of Cap. 32 continues to apply to an application for statutory derivative action made and proceedings brought or intervened in before the commencement of Division 4 of Part 14.
- Sections 152FA to 152FE of Cap. 32 continue to apply to an application for an order for inspection of a company's records and an inspection made before the commencement of Division 5 of Part 14.

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