

## CHAPTER 4

### INVESTIGATIONS AND ENQUIRIES

4.1 In Part 19 of the CB, we propose to enhance the provisions relating to company investigations and enquiries currently set out in sections 142 to 152F of the CO and to explicitly provide a new power for the Registrar to obtain documents, records and information for the purposes of ascertaining, as a start, whether any conduct that would constitute an offence relating to false or misleading statements has taken place. This chapter provides background information on the proposals in Part 19 and invites comments on the proposals.

#### Powers exercised by the FS

##### Background

4.2 Currently, the CO provides the following:

- (a) **investigation of a company's affairs:** the FS may appoint an inspector with extensive powers to conduct an investigation into the affairs of a company (sections 142 to 151). The appointment may be made under section 142 on members' application (in the case of a company having a share capital, by either not less than 100 members or members holding not less than one-tenth of the shares issued; in the case of a company not having a share capital, by not less than one-tenth in number of the members) or under section 143 in the following circumstances: (i) on the FS's own initiative where there is fraud or mismanagement involved, (ii) upon an order made by the court<sup>35</sup> or (iii) on application by a company which passed a special resolution to make the request; and
- (b) **inspection of books and papers:** the FS or a person authorised by him may, in specified circumstances, require a company and any person who appears to be in possession of the company's books and papers to produce those documents and to provide an explanation of them (sections 152A to 152F). This power may provide a discreet and less costly way to assess whether an investigation is warranted upon receiving an application from members under section 142 of the CO. The FS may also invoke the power where there is "good reason" to do so.

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<sup>35</sup> The appointment must be made under this scenario.

- 4.3 According to our records, the FS has in the past invoked section 142 or 143 of the CO to appoint inspectors to investigate the affairs of 38 companies. The last appointment was made in 1999. The power to inspect books and papers has never been invoked.

### **Need for the powers**

- 4.4 Many of the previous investigations undertaken by inspectors involve listed companies or their related companies. Developments in the regulatory framework of listed companies in recent years have reduced the need for the FS to appoint inspectors under the CO to investigate into the affairs of listed companies. Since the coming into operation of the SFO in April 2003, the SFC has greater powers to investigate into market misconduct involving listed companies. The FRC was established in 2006 to conduct independent investigations of possible auditing and reporting irregularities in relation to listed companies. This may help explain the absence of any new investigation by inspectors appointed under the CO in recent years.
- 4.5 Nonetheless, we cannot rule out the possibility of FS using the investigation and enquiry powers<sup>36</sup> in future cases where there are sufficient grounds to do so, especially since the investigation and enquiry powers could cover all types of companies formed or operating in Hong Kong. The provisions should be retained in the CB as “reserve” or “last resort” powers as a supplement to the powers contained in specialised Ordinances, such as the SFO and the Banking Ordinance (Cap 155)) targeting certain types of companies.

### **Enhancing the provisions**

- 4.6 The SFO and the FRCO both have provisions which empower the SFC and the FRC respectively to carry out investigations. We have made reference to these two pieces of legislation in modernising the provisions in the CB<sup>37</sup>.

#### *Strengthening investigatory powers of an inspector*

- 4.7 We propose to enhance the investigatory powers of an inspector. For example, we propose to require a person under investigation to preserve records or documents and, by statutory declaration, to verify statements made to the inspector.

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<sup>36</sup> In Part 19 of the CB, the power to inspect books and papers under the CO is referred to as power to “enquire into company’s affairs” (or “enquiry power” in short) to better described the nature of the power.

<sup>37</sup> There has been no major amendment to the relevant provisions in the CO since 1994.

### *Extending scope to cover companies incorporated elsewhere*

- 4.8 We also propose to extend the categories of companies that may be subject to investigation to cover companies incorporated elsewhere that are doing business in Hong Kong.
- 4.9 As regards the appointment of inspectors on the application of members, we will also extend the right to cover registered non-Hong Kong companies, i.e. those companies registered under Part 16 of the CB.

### *Improving safeguards for confidentiality*

- 4.10 In line with similar provisions provided for in SFO and FRCO, we consider it appropriate to provide better safeguards for confidentiality of information and protection of informers.
- 4.11 Details on the three proposals above can be found in the Explanatory Notes on Part 19 and the draft clauses in Divisions 1 to 3 and 5 in Part 19.

### *Threshold for application to FS for appointment of an inspector*

- 4.12 Currently, the threshold for members of a company with share capital to apply to the FS for the appointment of an inspector under section 142 of the CO is:
- (a) members holding not less than one-tenth of the shares issued; or
  - (b) not less than 100 members.

For a company without share capital, the threshold is one-tenth in number of the persons of the company's register of members.

- 4.13 The SCCLR had previously recommended that the number of members making a request under (b) above should be reduced from 100 to 50 while the other thresholds should remain unchanged. The current threshold of 100 members is already lower than similar thresholds in the UK and Singapore (both requiring at least 200 members). Nevertheless, the SCCLR's recommendation had taken into account the current shareholding structure and regime. Currently, a vast majority of the shares in listed companies are held in CCASS, and hence in the name of HKSCC Nominees Limited rather than in the name of the investor that actually holds the beneficial interest in the shares. Moreover, considerable processing time and cost is needed for the beneficial owner to withdraw the shares from

CCASS and register them in his/her own name<sup>38</sup>. We note that the SFC, HKEx and Federation of Share Registrars Limited have recently put forward a joint proposal for implementing a scripless securities market in Hong Kong which, if implemented, will facilitate investors to hold shares in their own names<sup>39</sup>. In view of this, we have retained the existing threshold of “not less than 100 members” in **Clause 19.3** of the draft Bill.

### **Question 3**

**Do you have any comments on the proposed changes to the provisions concerning the investigation of a company’s affairs and enquiry into company’s affairs that may be exercised by the FS described in paragraphs 4.6 to 4.13, the Explanatory Notes on Part 19 and Divisions 1 to 3 and 5 in Part 19 of the CB?**

### **Enquiries by Registrar**

- 4.14 We will also explicitly provide for a new but limited power for the Registrar to obtain documents, records and information for the purposes of ascertaining whether any conduct that would constitute certain offences under the CB, as a start, in relation to **Clauses 15.7(7)** (the equivalent of section 291AA(14) in the CO concerning giving false or misleading information in connection with an application for deregistration of a company) and **20.1(1)** (the equivalent of section 349 in the CO concerning making a statement that is misleading, false or deceptive in any material particular) has taken place.
- 4.15 The two offences, which relate to the provision of false information in documents delivered to the CR help safeguard the integrity of the Companies Register and the quality of information disclosed to the public.
- 4.16 The proposed power would enhance the CR’s enforcement efforts and facilitate the handling of public complaints by improving the quality of the evidence needed for successful prosecution against breaches of the relevant obligations under the CB. As the focus would be on breaches related to filing and routine operational requirements (e.g. complaints against incorrect particulars in a notification of change of particulars of secretary and director, annual return, etc), such enforcement work falls strictly within CR’s purview, and would not duplicate efforts of other regulatory bodies.

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<sup>38</sup> The issues involving CCASS are discussed in greater details in FSTB, *Consultation Paper on Draft Companies Bill – First Phase Consultation* (December 2009), paragraphs 6.13 and 6.14.

<sup>39</sup> SFC, HKEx and Federation of Share Registrars Limited, *Joint Consultation Paper on a Proposed Operational Model for Implementing a Scripless Securities Market in Hong Kong* (December 2009).

4.17 The details of the proposed new power can be found in the Explanatory Notes on Part 19 and the draft clauses in Divisions 1, 4 and 5 in Part 19.

**Question 4**

**Do you have any comments on the proposed new powers for the Registrar to obtain documents, records and information as described in paragraphs 4.14 to 4.17, the Explanatory Notes on Part 19 and Divisions 1, 4 and 5 in Part 19 of the CB?**