# Standing Committee on Company Law Reform (SCCLR)

## The Twelfth Annual Report

## 1995/96

**Standing Committee on Company Law Reform (SCCLR)**

**Twelfth Report to His Excellency the Governor in Council**

**Subjects considered by the**

**Standing Committee during 1995/96**

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## Terms of Reference of the Standing Committee on Company Law Reform

(1) To advise the Financial Secretary on amendments to the Companies Ordinance as and when experience shows them to be necessary.

(2) To report annually through the Secretary for Monetary Affairs to the Governor in Council on those amendments to the Companies Ordinance that are under consideration from time to time by the Standing Committee.

(3) To advise the Financial Secretary on amendments required to the Securities Ordinance and the Protection of Investors Ordinance with the objective of providing support to the Securities and Futures Commission in its role of administering those Ordinances.

(ii)

## Membership of the Standing Committee for 1995/96

Chairman : The Hon Mr Justice Rogers

Members : Mr J T Allen

Mr Richard E T Bennett

Mr Christopher M de Boer

Mr John R Brewer

Mr Dennis G D Cassidy

Mr Marvin Cheung Kin-Tung, OBE, JP

Mr CHOW Man Yiu, Paul

Mr Henry FAN Hung-ling

Mr Jason Felton

Mr David W Gairns, JP

Mr Robert G Kotewall, Q.C.

Mrs Angelina P L Lee, JP

Mr David Shaw

Mr Alan Smith, JP

Professor Edward L G Tyler

Ex-officio Members :

Mr A R Hearder, JP
The Official Receiver

Mr Gordon Jones, JP
The Registrar of Companies

Mr David T R Carse, OBE, JP
Deputy Chief Executive (Banking)

Mrs Lessie Wei
Deputy Secretary for Financial Services

Mr Gerard McMahon, JP
Securities & Futures
Commission

In Attendance : Mr Ermanno Pascutto

Secretary : Mr E T O'Connell

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**Meetings held during 1995/96**

| | | |
|---|---|---|
| One Hundredth and Fifth Meeting | - | 18th March |
| One Hundredth and Sixth Meeting | - | 13th May |
| One Hundredth and Seventh Meeting | - | 8th July |
| One Hundredth and Eighth Meeting | - | 30th September |
| One Hundredth and Ninth Meeting | - | 18th November |
| On Hundredth and Tenth Meeting | - | 27th January |

(iv)

**Executive Summary of Recommendations/Remarks**

| Chapter | Subject Matter | Recommendations/Remarks |
|---|---|---|
| 1 | Corporate Governance | It was important to promote corporate governance and business ethics to attract overseas institutional investors to HK. |
| 2 | Declarations of Solvency in a Member's Voluntary Winding-up - Section 233 of the Companies Ordinance | Amend Section 233 of the Companies Ordinance to allow for the making of the declaration of solvency outside the meeting of directors. |
| 3 | Section 168A of the Companies Ordinance - The Alternative Remedy to Winding-up | No changes to the current legislation. However, it was agreed to refer the matter to Mr. Pascutto for him to consider in the context of the Overall Review. |
| 4 | Powers of the court to order a compulsory winding-up to be conducted as a creditor's voluntary winding-up : Sections 209A & 209B of the Companies Ordinance | Discussions deferred to await the outcome of a Court of Appeal decision on the subject. |
| 5 | Statutory Protection for Auditors | Discussions deferred to see if the HKSA and the Administration could reach agreement. |
| 6 | Statutory Declarations of Compliance with regard to the requirements for the Incorporation of a Company - Section 18(2) of the Companies Ordinance | No changes to the present legislation. |
| 7 | Corporate Communications | Greater efforts to be made, with the advent of the central clearing and settlement system for the trading of shares on the HKSE, to ensure that beneficial owners of shares receive corporate communications. |

| Chapter | Subject Matter | Recommendations/Remarks |
|---|---|---|
| 8 | Applications to the Financial Secretary to Override the Statutory Accounts Disclosure Requirements: Sections 123(4); 126(3); 128(3); 129(3); 129A(2), and Paragraphs 6(b), 13(2), 18(4) & 27(i) of the Tenth Schedule of the Companies Ordinance | Amend Section 126(2) of the Companies Ordinance to allow directors to explain why a holding company and its subsidiary company do not have coinciding financial years instead of having to apply to the Financial Secretary for relief. No changes to the other sections. |
| 9 | Declaration of Interests by Members of Advisory Boards and Committees | SCCLR agreed to adopt a 'general declaration of interests' system. |
| 10 | Procedures for the Replacement of Lost Share Certificate - Section 71A of the Companies Ordinance | Discussions deferred to enable the HKSE and the Federation of Share Registrars to reach agreement. |
| 11 | Definition of the term 'Place of Business' - Overseas Companies and Section 341 of the Companies Ordinance | No changes to the legislation. It was agreed to refer the subject to Mr. Pascutto for consideration within the context of the Overall Review. |
| 12 | Resignation of the Auditor of a Company Sections 140A(2)(a) and 140A(3)(b) of the Companies Ordinance | Amend both sections so that firstly an auditor's resignation statement should be filed with the Companies Registry and secondly to model them more closely on 1985 UKCA provisions. |
| 13 | Disqualification of Company Directors - Part IVA of the Companies Ordinance and Amendments to the Securities & Futures Commission Ordinance to Provide for Powers for Disqualification of Directors | Various amendments to the SFCO and the CO to broaden the grounds for disqualification of directors. |
| 14 | Transparency of Advisory Boards and Committees | No changes to the present status of the SCCLR and its requirement to report annually. |

| Chapter | Subject Matter | Recommendations/Remarks |
|---|---|---|
| 15 | De-Regulation of Company Forms - The Five Statutory Forms Contained in the 2nd, 4th and 5th (Parts II, IIA & III) Schedules to the Ordinance; the 48 Statutory Forms in the Companies (Forms) Regulations | De-regulate various statutory forms in the Companies Ordinance so that future changes to their form and content can be undertaken administratively. |
| 16 | A Guide for Directors of Listed Companies; Guidelines for Directors 1995 | Two guidelines issued by the HKSE and Institute of Directors tabled for discussion and comment. |
| 17 | KPMG Corporate Fraud Surveys for 1994 and 1995 | Two Corporate Fraud Surveys for 1994 and 1995 tabled for discussion and comment. |
| 18 | Authorised Representatives of Overseas Companies Section 333A of the Companies Ordinance | No change to the present legislation. |
| 19 | Corporate Rescue and Insolvent Trading | Consultative paper of the Insolvency Law Reform Sub-committee tabled for discussion and comment. |
| 20 | The Companies Registry Annual Report for 1994/95 | Companies Registry Annual Report tabled for discussion. |
| 21 | The Official Receiver's Report for 1994/95 | Official Receiver's Annual Report tabled for discussion. |
| 22 | The Auditors' Report - Section 141 of the Companies Ordinance | Discussions deferred to allow LegCo Sub-Panel on Financial Services to consider in the context of statutory immunity for auditors. |
| 23 | Overall Review of the Companies Ordinance | Various papers and reports tabled for comment and discussion. |

## Chapter 1

## Corporate Governance

1.1 A corporate governance survey of Hong Kong, undertaken by the international accounting firm of Price Waterhouse, was tabled for discussion at the 105th meeting of the Standing Committee.

1.2 The principal findings of the survey concluded that :

- the average number of full board meetings held in a year was 6.14 whilst more than half the companies exceed the requirements of the HKSE listing rules to have at least two non-executive directors as board members;

- one in three companies had formal policies on corporate governance and business ethics;

- eight in ten companies had no remuneration committee;

- almost half of the companies surveyed had policies for disseminating information to the market place;

- over 50% of the companies ensured that price sensitive information was released to the stock

exchange at the same time it was given elsewhere;

- relatively few of the companies had formal policies for dealing with investors' complaints;

- almost half of the companies had an internal audit department;

- one in three companies had no procedures manuals for regulating their internal management; and

- almost three in four companies believed that there was room for improvement in corporate governance and business ethics. Most, however, would not like to see more legislation, preferring instead more self-regulation and a tightening of the existing rules;

1.3 During the course of discussions, members were very keen to endorse the great importance of 'corporate governance' and the promotion of a high standard of business ethics if the Hong Kong stock market was to develop into one of the leading markets in the world. The liquidity to achieve this would only come from large overseas institutional investors who themselves were bound by fiduciary duties and obligations to their investors as to how the funds under their control were invested. It was highly probable

that they would not invest in companies which were not properly governed.

1.4 Certain members were strongly of the view that many directors of listed companies simply did not understand or appreciate their duties or responsibilities. It was common for such directors, who effectively owned their companies through their respective shareholdings, to believe that their personal interests and those of the companies they controlled coincided. As a consequence the task of educating them and their professional advisers as to what their duties were was an important and continuing obligation. The Hong Kong Stock Exchange was about to introduce training courses for directors of PRC companies listed on the stock exchange.

1.5 In conclusion, members agreed to keep the issue under review. It was hoped that the Institute of Directors in Hong Kong would assist in the education process by issuing its own code on directors' duties - otherwise the whole question of the statutory codification of directors' duties would need to be revisited. (N.B. The Institute of Directors has since issued its own set of voluntary guidelines.)

## Chapter 2

## Declarations of Solvency in a Member's Voluntary Winding-up - Section 233 of the Companies Ordinance

### 2. Summary of Recommendations

2.1 At the 105th meeting of the Standing Committee, members endorsed in principle the proposal of the Hong Kong Institute of Company Secretaries to amend Section 233 of the Companies Ordinance to allow the directors of a company to make the statutory declaration of solvency outside the meeting of directors once the making of it has been authorised by way of a board resolution.

### Background

2.2 Under Section 228(1) of the Companies Ordinance, a company may be wound-up voluntarily in the following circumstances :

(a) when the period fixed by the articles for the duration of the company expires or when the company resolves to be wound-up voluntarily following on from the happening of an event which determines its existence, occurs;

(b) if the company resolves by special resolution to be wound-up voluntarily;

(c) if the company resolves by special resolution, because of its liabilities, that it is advisable to wind-up; and

(d) if the directors (or in the case of a company having more than 2, the majority) make and deliver to the Registrar of Companies a statutory declaration pursuant to Section 228A(1). (This section provides for a special procedure for the winding-up of a company which is unable to continue its business).

2.3 Under Section 230, the winding-up is deemed to commence when the resolution is passed and notice must be printed in the Gazette within 14 days of the resolution. The special resolution referred to in paragraph 2.2(b) supra must also be registered with the Registrar of Companies within 15 days.

2.4 When a member's voluntary winding-up is proposed, the directors, at a meeting of the directors, are obliged to make a statutory declaration stating that they have made inquiry into the affairs of the company and that they have formed the opinion the company will be able to pay its debts in full within a maximum of 12 months from the date the resolution to wind-up was passed. Section 233(2)

states that the statutory declaration must be made within the five weeks preceding the resolution, or on the day of the resolution but before the resolution has been passed. Thereafter the declaration of solvency is delivered to the Registrar of Companies for registration. It must contain a statement of the company's assets and liabilities as at the latest practicable date before the making of the declaration.

2.5 In support of its proposal the Institute of Company Secretaries had stated :

> "The statutory declaration required of Section 233 in advance of a member's voluntary winding-up is required to be made at a meeting of the directors. In practice, this declaration is sanctioned by a Board resolution and then made outside the meeting, perhaps at a district office or otherwise in the presence of an individual with capacity to administer the declaration. We believe that the provision should be amended to reflect reality."

2.6 After due consideration, it was agreed that the Institute of Company Secretaries, in conjunction with the Companies Registry, would prepare a new prescribed form of statutory declaration which would then be re-submitted to the Standing Committee for its approval.

## Chapter 3

## Section 168A of the Companies Ordinance - The Alternative Remedy to Winding-up

### 3. Summary of Recommendations

3.1 At the 105th Meeting of the Standing Committee, members agreed that further discussion on the proposal of the Hong Kong Bar Association - viz that the alternative remedies to winding-up available to shareholders of Hong Kong incorporated companies under the provisions of Section 168A of the Companies Ordinance should be extended to companies incorporated outside Hong Kong - should be deferred to enable Mr. Pascutto, who was undertaking the 'Overall Review' of the Companies Ordinance, to consider the subject in conjunction with those other provisions which governed the position of overseas companies in Hong Kong. It was thought desirable to see if a broad approach to the regulation of the affairs of overseas companies could be achieved, and this should include the question of Section 168A.

### Background

3.2 Section 168A provides that any member of a company who complains that the affairs of a company are being or have been conducted in a manner unfairly prejudicial to the

interests of the members generally or some part of the members may make an application to the court by petition for an order. The court on hearing the application may :

- make an order restraining the commission of any such act or the continuance of such conduct;

- order that proceedings shall be brought in the name of the company against such person and on such terms as the court may order;

- appoint a receiver or manager of the whole or part of the company's property;

- make such order as it thinks fit including the purchase of certain members' shares by other members;

3.3 A company is defined by Section 2 of the Ordinance in the following terms :

" Company means a company formed and registered under this ordinance or an existing company."

By definition therefore, such a company cannot include an overseas company for the purposes of proceedings under Section 168A.

3.4 In support of its proposal the Bar Association stated :

> " In the light of the substantial increase of companies (listed and unlisted) having offshore domiciles, consideration should be given to whether, for the protection of minority shareholders, Section 168A should be extended to companies incorporated outside Hong Kong. At present, shareholders of such companies can only petition to wind-up the company on the just and equitable ground under Section 327(3)(c) of the ordinance."

3.5 During the course of deliberations it was pointed out that whilst the Securities & Futures Commission had certain powers under Sections 37A and 29A of the Securities & Futures Commission Ordinance to take action on behalf of aggrieved minorities of listed companies, irrespective of where they were domiciled, this did not extend to shareholders of private companies or to minorities of listed companies where the SFC declined to act.

3.6 A further consideration was the importance of not extending Hong Kong laws extra-territorially. Under Private International law, it was a cardinal principle that it was for the law of the country of incorporation to regulate the internal affairs of a company. Overseas companies with genuine international business connections e.g. Sony or

IBM, as opposed to those just having most of their assets in Hong Kong, could have serious reservations with regard to the seeking of a secondary listing in Hong Kong if the legislation were to be amended to afford their shareholders resident in Hong Kong the right to seek redress in the Hong Kong courts.

3.7 Other members pointed out that it was illogical for the Hong Kong courts to have the power to wind up overseas or unregistered companies on the just and equitable ground pursuant to Section 177 of the Companies Ordinance but not the jurisdiction to entertain a Section 168A petition.

3.8 According to an analysis of the numbers of overseas companies registered under Part XI of the Companies Ordinance as at 31 December 1994, there were in total 3,956 foreign companies registered in Hong Kong. A copy of that analysis is at Appendix 1. It was clear that the vast majority of such companies had the bulk of their assets and central boards of management outside of Hong Kong and many members were of the view that management disputes and shareholders' fights should be determined by their respective countries of incorporation.

3.9 As against that, however, it was clear that a large proportion of listed companies with overseas domiciles were, to all intents and purposes, Hong Kong companies with

the bulk of their assets and their central boards of management located in Hong Kong. It was right that shareholders of such companies should enjoy the same rights as those of Hong Kong incorporated entities.

3.10 In conclusion, members agreed that the issue raised was of sufficient importance for it to be referred to Mr. Pascutto for him to examine within the context of the overall review.

Appendix 1

## ANALYSIS ACCORDING TO COUNTRIES OF ORIGIN FOR COMPANIES INCORPORATED OUTSIDE HONG KONG WHICH HAVE ESTABLISHED A PLACE OF BUSINESS IN HONG KONG AND REGISTERED DOCUMENTS UNDER PART XI OF THE COMPANIES ORDINANCE

| | Registered as at 31.12.1993 | New Registrations from 1.1.1994 to 31.12.1994 | Registrations Closed 1.1.1994 to 31.12.1994 | Register as at 31.12.19 |
|---|---|---|---|---|
| Algeria | 1 | 0 | 0 | 1 |
| Argentina | 1 | 0 | 0 | 1 |
| Aruba | 2 | 0 | 1 | 1 |
| Australia | 99 | 12 | 1 | 110 |
| Austria | 4 | 0 | 0 | 4 |
| Bahamas | 32 | 9 | 3 | 38 |
| Bahrain | 4 | 0 | 0 | 4 |
| Barbados | 1 | 0 | 0 | 1 |
| Belgium | 17 | 1 | 2 | 16 |
| Belize | 0 | 1 | 0 | 1 |
| Bermuda | 298 | 54 | 3 | 349 |
| Brazil | 4 | 0 | 0 | 4 |
| British Virgin Islands | 572 | 217 | 33 | 756 |
| Brunei | 3 | 0 | 0 | 3 |
| Canada | 66 | 3 | 3 | 66 |
| Cayman Islands | 98 | 22 | 0 | 120 |
| Cook Islands | 19 | 2 | 3 | 18 |
| Cyprus | 1 | 0 | 0 | 1 |
| Denmark | 8 | 1 | 1 | 8 |
| Dubai, United Arab Emirates | 2 | 0 | 0 | 2 |
| Egypt | 1 | 0 | 0 | 1 |
| Finland | 4 | 1 | 0 | 5 |
| France | 51 | 6 | 1 | 56 |
| Federal Republic of Germany | 31 | 3 | 1 | 33 |
| Gibraltar | 6 | 1 | 1 | 6 |
| India | 15 | 2 | 0 | 17 |
| Indonesia | 10 | 0 | 0 | 10 |
| Iran | 2 | 0 | 0 | 2 |
| Israel | 1 | 0 | 0 | 1 |
| Italy | 22 | 1 | 3 | 20 |
| Jamaica | 1 | 0 | 0 | 1 |
| Japan | 318 | 30 | 12 | 336 |
| Liberia | 135 | 9 | 5 | 139 |
| Liechtenstein | 2 | 0 | 0 | 2 |
| Luxembourg | 5 | 1 | 0 | 6 |
| Malaysia | 37 | 0 | 1 | 36 |
| Commonwealth of the Northern Mariana Islands | 1 | 0 | 0 | 1 |
| Mauritius | 2 | 0 | 0 | 2 |
| Mexico | 1 | 0 | 0 | 1 |
| Morocco | 2 | 0 | 0 | 2 |
| Nauru | 12 | 0 | 1 | 11 |
| Nepal | 1 | 0 | 0 | 1 |

| | Registered as at 31.12.1993 | New Registrations from 1.1.1994 to 31.12.1994 | Registrations Closed 1.1.1994 to 31.12.1994 | Register as at 31.12.19 |
|---|---|---|---|---|
| Netherlands Antilles | 6 | 0 | 0 | 6 |
| Netherlands | 41 | 3 | 3 | 41 |
| New Guinea | 1 | 0 | 0 | 1 |
| New Zealand | 31 | 5 | 3 | 33 |
| Norway | 10 | 1 | 0 | 11 |
| Pakistan | 6 | 0 | 0 | 6 |
| Panama | 83 | 3 | 3 | 83 |
| the People's Republic of China | 44 | 10 | 1 | 53 |
| Philippines | 25 | 1 | 0 | 26 |
| Portugal (Macau) | 11 | 2 | 0 | 13 |
| Republic of Korea | 39 | 2 | 1 | 40 |
| Republic of Ireland | 4 | 5 | 0 | 9 |
| Republic of the Marshall Islands | 1 | 0 | 0 | 1 |
| Republic of Vanuatu (formerly New Hebrides) | 6 | 5 | 2 | 9 |
| Republic of Zambia | 1 | 0 | 0 | 1 |
| Russia | 2 | 0 | 0 | 2 |
| Saudi Arabia | 2 | 0 | 0 | 2 |
| Singapore | 148 | 14 | 6 | 156 |
| Socialist Republic of Vietnam | 0 | 1 | 0 | 1 |
| South Africa | 3 | 1 | 0 | 4 |
| Spain | 9 | 1 | 0 | 10 |
| Sri Lanka | 1 | 0 | 0 | 1 |
| Sweden | 16 | 0 | 1 | 15 |
| Switzerland | 42 | 5 | 2 | 45 |
| Taiwan | 23 | 7 | 2 | 28 |
| Tanzania | 1 | 0 | 0 | 1 |
| Thailand | 17 | 0 | 1 | 16 |
| Turks & Caicos Islands | 3 | 1 | 0 | 4 |
| Union of Myanmar | 3 | 0 | 0 | 3 |
| United Kingdom | 373 | 35 | 25 | 383 |
| United States of America | 694 | 88 | 35 | 747 |
| Venezuela | 1 | 0 | 0 | 1 |
| Western Samoa | 5 | 7 | 1 | 11 |
| Total: | 3544 | 573 | 161 | 3956 |

## Chapter 4

## Powers of the court to order a compulsory winding-up to be conducted as a creditor's voluntary winding-up : Sections 209A & 209B of the Companies Ordinance

### 4. Summary of Recommendations

4.1 At the 105th Meeting of the Standing Committee members agreed to defer further discussion and to await the outcome of a Court of Appeal decision which was expected to have a direct bearing on the matter in hand.

**Background**

4.2 The Hong Kong Bar Association had proposed that the cross reference in Section 209B of the Companies Ordinance (this section sets out the consequences once a compulsory winding-up has been converted into a creditor's voluntary winding-up under Section 209A) to Sections 182, 183 and 186 should be deleted. Those latter sections only applied to compulsory windings-up. In support of its proposal, the Bar Association contended :

> "The purpose of a voluntary winding-up, whether members or creditors, is to divorce its control from the court, including the right to bring proceedings

against the company in liquidation. Thus it is difficult to see any basis for the application of Sections 182, 183 and 186 in the case of a voluntary winding-up converted from a compulsory winding-up when an ordinary member's or creditor's voluntary winding-up is not governed by any of these provisions. Moreover Section 182 does not apply once a company has been ordered to be wound-up as all directors become functus. No liquidator has ever applied to the court for the disposal of an asset under that provision as its powers and duties are governed by the ordinance. In the circumstances, it is all the more puzzling why Section 182 remains applicable to a creditor's voluntary winding-up."

4.3 Section 209A was enacted in 1984. This empowered a court to convert a compulsory winding-up into a creditor's voluntary winding-up on the application of the liquidator. Its genesis can be found in the second report of the Hong Kong Companies Law Revision Committee in 1973 which adopted the recommendation of the Cohen Committee set up by the Department of Trade and Industry in the UK to consider Company Law Reform. However, it was never enacted in the UK nor in any other comparable common law system.

4.4 In 1990, section 209A was amended and as a consequence Section 209B was enacted. The reasons justifying the changes were :

- the right to convert under the old provisions could (and did) adversely affect the financing of the Official Receiver's Office;

- the discretion of the court when considering the application should also take into account questions of fraud and misfeasance by former directors and not just the wishes of creditors and contributories;

- there were technical deficiencies in the legislation which could only be cured by granting the court a general power to give consequential directions once a conversion had been ordered;

4.5 Part V of the Companies Ordinance which deals with all modes of winding-up is divided into five parts :

- Part I deals with preliminary matters such as the modes of winding-up;

- Part II regulates winding-up by the court and includes Sections 182, 183, 186, 209A and 209B;

- Part IIA sets out the provisions for the winding-up by the court by way of a regulating order;

- Part IIB provides for the winding-up of companies by

way of summary procedure;

- Part III determines how voluntary windings-up, members and creditors, should be followed;

- Part IV was repealed in 1984;

- Part V sets out the provisions applicable to every mode of winding-up and includes the proof and ranking of claims, set-off, preferential payments, fraudulent preference etc.;

4.6 In addition, members' attention was also drawn to Section 255 of the Ordinance which empowered a liquidator in a creditor's voluntary winding-up to apply to court to have questions determined or powers exercised. The court was entitled to exercise any of the powers it has in relation to compulsory winding-up when considering the application.

4.7 Members however believed that it was best to await the outcome of the Court of Appeal case - In re Conso (Far East) Electronics Ltd. - before considering the matter further.

## Chapter 5

## Statutory Protection for Auditors

### 5. Summary of Recommendations

5.1 At the 106th meeting of the Standing Committee, members agreed, in light of the Hong Kong Society of Accountants' (HKSA) opposition to the proposal, to defer further discussions to enable the Financial Services Branch and the HKSA to liaise further to see if an agreement could be reached as to whether auditors of listed companies should be granted statutory immunity from civil actions when they reported suspicions of fraud to the regulatory authorities.

### Background

5.2 At the 96th meeting of the Standing Committee, a proposal to grant statutory immunity to auditors when they reported fraud was tabled for discussion. The Standing Committee supported the proposals in principle but requested that it be consulted again when the draft bill was ready.

5.3 The original proposal was limited to the provision of statutory protection to auditors of listed companies. However, after due consideration by the Administration, it was decided to expand the scope of protection to cover

auditors of unlisted companies. In addition, as more than half of the listed companies on the HKSE were domiciled overseas, it was also decided to include auditors of such companies who were appointed in Hong Kong. As regards auditors of overseas companies who were appointed outside of Hong Kong, the statutory protection could not be extended to them. This was because they would be subject to the law of the place they were appointed - Hong Kong could not extend its law extraterritorially.

5.4 During the course of deliberations, members were advised of the very serious reservations of the HKSA with regard to the proposals. Certain members of the Standing Committee shared those reservations. In short they were :

- the proposed criteria for reporting fraud, and other misconduct were too broad and imprecise. As auditors were not legal experts, it might be difficult for them to form a view as to what constituted fraud or misconduct;

- there was a general over expectation of the frequency of reportable offences and of the ability of an auditor to recognise fraud from an examination of individual transactions;

- the proposals might destroy the client auditor relationship. Cases of actual fraud within companies were very infrequent;

5.5 In view of this, and the ongoing discussions between the Administration and the HKSA, members agreed to adjourn discussions for the time being.

## Chapter 6

## Statutory Declarations of Compliance with regard to the requirements for the Incorporation of a Company - Section 18(2) of the Companies Ordinance

### 6. Summary of Recommendations

6.1 At the 106th Meeting of the Standing Committee, members rejected a proposal by the Hong Kong Institute of Company Secretaries that Section 18(2) of the Companies Ordinance be amended so that only professional company secretaries, solicitors or professional accountants could make the statutory declaration of compliance with regard to the formalities of incorporation.

**Background**

6.2 Under Section 18 of the Companies Ordinance, once a certificate of incorporation is issued, it is conclusive evidence that :

(a) all the requirements of the ordinance in respect of registration have been compiled with; and

(b) the association is a company authorised to be registered and is duly registered.

6.3 From the date of incorporation the subscribers to the memorandum together with future members constitute a body corporate with all the attendant rights, duties and benefits conferred by other sections of the ordinance.

6.4 In support of its proposal the HKICS had stated :

> "Incorporation has been part of commercial life since the days of England's Middle Ages and the relatively simple demands of incorporation by way of registration ..... are already 150 years old. However, the number of new incorporations has grown exponentially in recent years and it is now fair to say that Hong Kong incorporated company has achieved commodity status - it is readily available in relatively standard form and at a relatively low price.
>
> We are concerned, however, that despite the obligations placed on those who make statutory declarations when delivering incorporation papers for registration, the quality of what is drafted - particularly in Articles of Association - leaves much to be desired. We are concerned to ensure that the regulations which private individuals and their professional advisers must administer provide clear and unambiguous direction .....

Very many incorporations are undertaken through the offices of professionally qualified individuals such as company secretaries, lawyers and accountants. On the other hand, there are many instances of printers who have extended their financial interest from printing memoranda and Articles of Association to incorporation. Their ability to do this is found in the wording of Section 18(2) of the Companies Ordinance which provides that (as an alternative to a solicitor) a person named as director or secretary may make the required form of statutory declaration. The reason for the statutory declaration is ..... to remove from the Registrar of Companies a burden that he would otherwise assume under Section 18(1). Whilst the wording in Section 18(2) might in the days of the joint stock company have been expected to be taken seriously by those named as the first directors or secretary, the commodity nature of today's incorporation business has changed matters considerably. Several jurisdictions where incorporation has similarly become a commonplace matter have already introduced this requirement ..... professional company secretaries, solicitors or professional accountants ..... all of whom are expected by their relevant professional bodies to have knowledge of HK Company Law and who are trained to understand the seriousness and expectations of a statutory declaration."

6.5 During the course of discussions, members pointed out that the purpose of the statutory declaration was to assure the Registrar of Companies that the incorporation formalities had been complied with and that the incorporation was for a lawful purpose. As this was a formality, they were of the view that the legislation should remain unchanged. Other members felt that as a matter of principle the law should remain flexible enough to enable businessmen themselves, if they so wished, to undertake the task rather than have to consult with or use professionals.

## Chapter 7

## Corporate Communications

### 7. Summary of Recommendations

7.1 At the 106th Meeting of the Standing Committee, members recommended that greater efforts should be made to ensure that the beneficial owners of shares, whose shares were registered in the names of nominees because of the introduction of the central clearing and settlement system (CCASS), received corporate communications regarding the affairs and activities of listed companies.

**Background**

7.2 The Corporate Finance Association of Hong Kong had requested the Standing Committee to review the way in which corporate communications were distributed to shareholders of listed companies. This concern had arisen because of the introduction of CCASS for publicly listed companies.

7.3 In support of its submission the CFA had stated :

> "The introduction of a central clearing and settlement system (CCASS) for publicly traded securities has raised a number of concerns regarding the transparency of company ownership and the

effectiveness of corporate communications. The CCASS system operated on a nominee ownership basis, so that the register of members of most listed companies now shows a very significant percentage of shares as held in the name of HKSCC Nominee and other custodial names.

So far as the HKSCC is concerned the shares are held by its participants, who are limited to brokers and custodians. This means that only the CCASS participants know who the beneficial owners are. The result is that share ownership is now multi-tiered and corporate communications and distributions have to be "cascaded" through the various tiers before they reach the beneficial owners.

In practice this means that the register of members is fairly meaningless and that important documents such as circulars to shareholders no longer reach the beneficial owners. For example, only one copy of a rights issue prospectus needs to be sent to the HKSCC under the Companies Ordinance. Under the listing rules of the Stock Exchange a copy must be sent to every broker, but the beneficial owner does not receive one. Instead he may receive a phone call or fax from his broker asking for instructions. Many of our members believe that this is not satisfactory and the way in which corporate communications are distributed should be reviewed."

7.4 CCASS was set up in 1991 following one of the main recommendations of the Securities Review Committee which reported to Government in 1988.

7.5 During the course of discussions it was pointed out that this was not a new problem brought on by the introduction of CCASS but had existed for some time before, as many shareholders commonly deposited their shares into nominee accounts maintained by banks, or broker firms. The setting up of CCASS, however, had ensured that many more investors, because of its operational efficiency and trading convenience, were choosing not to take physical delivery of their shares but instead keeping them with their brokers who kept them registered with the central depository maintained by the Hong Kong Securities Clearing Co. Ltd.

7.6 In view of this, however, members accepted the need to improve corporate communications between listed companies and the beneficial owners of their shares. One suggestion to improve the dissemination of information was to require CCASS to draw up and send to the registrars of listed companies a list of beneficial owners. The companies could then arrange for their documentation to be forwarded direct thus bypassing the nominees. If on the other hand nominees were required to pass on the information, this could lead to a significant increase in cost which ultimately the beneficial owners would most probably bear. Members were

also advised that the Hong Kong Stock Exchange was reviewing the position. It too was concerned to ensure that corporate information was despatched to those entitled to receive it and as a consequence was considering possible changes to its own listing rules.

## Chapter 8

## Applications to the Financial Secretary to Override the Statutory Accounts Disclosure Requirements : Sections 123(4); 126(3); 128(3); 129(3); 129A(2), and Paragraphs 6(b), 13(2), 18(4) & 27(i) of the Tenth Schedule of the Companies Ordinance

### 8. Summary of Recommendations

8.1 At the 108th meeting of the Standing Committee members recommended that Section 126(2) of the Companies Ordinance should be amended so as to empower the directors of a holding company, with regard to the non-coinciding of a subsidiary's financial year with that of its holding company, to provide an explanation in the group accounts as to why a deviation was necessary without having to apply to the Financial Secretary for permission. With regard to Sections 123(4), 126(3), 128(3), 129(3), 129A(2) of the Companies Ordinance and paragraphs 6b, 13(2), 18(4) and 27(1) of the Tenth Schedule to the Companies Ordinance which mandated the disclosure of information in the accounts unless exempted from doing so by the Financial Secretary, it was agreed that further discussion should be deferred until such time as the consultative paper of the Hong Kong Society of Accountants on the accounts disclosure requirements set out in the Companies Ordinance was available.

**Background**

8.2 The Hong Kong Society of Accountants had recommended amendments to Sections 123(4) and 126(3) of the Companies Ordinance by deleting the requirement for the directors of companies to apply to the Financial Secretary for sanction when they sought to override the statutory accounts disclosure requirements set out in the Tenth Schedule to the Companies Ordinance.

8.3 In support of its proposal the HKSA had stated :

> "Sub-section (4) of section 123 dealing with companies accounts, and sub-section (3) of section 126 dealing with group accounts provide the Financial Secretary with the power to override statutory accounts disclosure requirements (contained in the Tenth Schedule), subject to the power being exercised in such a way as not to prejudice the requirement for the accounts to show a true and fair view.
>
> We are not aware that this power has ever been exercised, and question the necessity and appropriateness of putting this additional responsibility on the Financial Secretary."

8.4 A further examination of the legislation disclosed that there were several other provisions which empowered the Financial Secretary, upon application, to waive the accounts disclosure requirements if there were good reason for doing so. The genesis for these mandatory disclosure requirements were to be found in a number of successive UK Companies Acts. The underlying purpose was to ensure that the published accounts and the annexed reports were much more informative than they had been previously regarding a company's relationship with other companies in the same group. During the course of discussions, members remarked that it was impossible to anticipate all of the reasons behind a company seeking an exemption from the disclosure requirements. The key issue was whether it was right and proper for the company itself to decide whether or not to deviate from the disclosure requirements or whether it should be with the consent of some official body, as was the case now. Any step to remove a substantive provision for disclosure in the accounts was unwise and a retrograde step.

8.5 However, it was accepted that with regard to Section 126(2) different considerations applied. It was unnecessary for directors to apply to the Financial Secretary for permission to non-coincide a subsidiary's accounts with those of its holding company. It was sufficient for an explanation to be given in the accounts.

## Chapter 9

## Declaration of Interests by Members of Advisory Boards and Committees

### 9. Summary of Recommendations

9.1 At the 106th meeting of the Standing Committee, members endorsed the Administration's proposal that a "general declaration of interests system" should be formally adopted by the Standing Committee.

### Background

9.2 At a LegCo Panel discussion meeting on Constitutional Development held on 12 September 1994, it was pointed out that many members of the boards and committees which advised Government on various policy matters had privileged information which could be used for personal benefit. Government therefore had a duty to ensure that controls were in place to prevent members from taking advantage of their membership. The present voluntary reporting systems in place for the declaration by members of their interests should be made mandatory for all boards and committees so as to sustain public confidence in the consultative system. It was proposed therefore that a declaration of interests system should be formally adopted by the Standing Committee.

9.3 Broadly speaking, there were two systems of voluntary declaration of interests in place. The first, the two tier system, was recommended for statutory authorities and advisory committees with extensive influence over policy and financial matter. Under this system, the chairman and members of the board were required to register their general pecuniary and personal interests on first appointment and this would be updated when necessary and made available for public inspection. The second, the general declaration of interests, required the chairman and members to declare an interest as and when a matter was raised for discussion which raised a potential for a conflict of interest.

9.4 After a short discussion, members unanimously supported the chairman's suggestion that henceforward the general declaration of interests system should be adopted.

## Chapter 10

## Procedures for the Replacement of Lost Share Certificate - Section 71A of the Companies Ordinance

### 10. Summary of Recommendations

10.1 At the 110th meeting of the Standing Committee members agreed to defer further discussion on the proposal of the Hong Kong Institute of Company Secretaries to replace the cumbersome procedures provided for by Section 71A with the much simpler requirement of a letter of indemnity. The position was under review by both the Hong Kong Stock Exchange and the Federation of Share Registrars and it was felt that both bodies should liaise further to try and reach agreement on what changes should be brought about to the current legislative requirements.

### Background

10.2 The Hong Kong Institute of Company Secretaries had proposed that Section 71A of the Companies Ordinance should be amended to allow for the use of letters of indemnity in place of the current stringent legal regime. In support of its proposal, the Institute had stated :

> "With the advent of central clearing, the procedure contained in Section 71A for replacement of lost

share certificates in respect of listed companies is rapidly becoming out of date. A number of listed company secretaries have suggested that it would cause the companies concerned no great problem to substitute Section 71A arrangements with the rather simpler requirement for a letter of indemnity. We accordingly recommend such a change."

10.3 The provisions for dealing with the replacement of lost share certificates in listed companies are set out in Section 71A. Any person who is a registered holder of shares or who claims to be entitled to have his name entered in the register of members may, if his share certificate is lost, apply to the company for a new certificate. The application must be accompanied by a statutory declaration which should include the following details :

- when the original certificate was last in his possession and how he stopped having possession;

- whether he executed any transfer in respect of that share, in blank or otherwise;

- a statement that no person is entitled to have his name entered in the register;

- such other particulars as may be necessary to verify the grounds on which the application is made;

10.4 If the company intends to issue a new certificate it must publish a notice advertising its intention to do so :

- if the shares are worth less than $20,000.00 and the application is made by the holder or with his consent, the notice must be published once in an English language newspaper and a Chinese language newspaper and published in the Gazette;

- if the shares are worth more than $20,000.00 or the application is made by a person other than the registered owner without his consent, the notice must be published in the Gazette once a month for three months;

10.5 Publication of the notice will only be valid if :

- the company has delivered a copy to the Unified Exchange to be exhibited there; and

- if the application is made other than by the registered holder or without his consent the company must have served notice on the registered holder by registered post to his last address appearing in the register and three months have expired since.

10.6 An authorised officer of the Unified Exchange must certify that the copy is being exhibited at a conspicuous place set aside for such notices. The notice must be exhibited for one month in the case of a registered holder's application where the value of the shares is less than $20,000.00. In every other case, it must be exhibited for three months.

10.7 During discussions, it emerged that there were also problems with regard to the procedures for the replacement of lost share certificates of overseas companies listed on the HKSE. As they now accounted for more than 60% of all listed companies it was important to achieve a uniform solution. In view of this, it was agreed to defer further debate to enable the Hong Kong Stock Exchange to continue discussions with the Federation of Share Registrars on the best way forward. Once agreement had been reached, a further position paper would be tabled before the Standing Committee.

## Chapter 11

## Definition of the term 'Place of Business' - Overseas Companies and Section 341 of the Companies Ordinance

### 11. Summary of Recommendations

11.1 At the 107th meeting of the Standing Committee, members agreed to defer further debate and to allow Mr. Ermanno Pascutto in the context of the Overall Review of the Companies Ordinance, to consider the definition of a 'Place of Business' in conjunction with his examination of the status of overseas companies currently provided for in the companies legislation.

**Background**

11.2 The Hong Kong Bar Association had asked the Standing Committee to consider the unsatisfactory definition of 'Place of business' set out in Section 341 of the Companies Ordinance. This is defined as :

> "Place of business includes a share transfer or share registration office and any place used for the manufacture or warehousing of any goods but does not include a place not used by the company to transact any business which creates legal obligations."

11.3 Under Part XI of the Companies Ordinance, registration as a foreign company is only required when such a company has established a place of business in Hong Kong. Whether or not such a company has established a place of business is largely a question of fact. In the case of :

"Owners of a cargo lately laden on board the ship Artemis v Artemis Transportation Company (1983) HKLR 364", the Court of Appeal held that to prove the existence of a place of business it was necessary to consider three separate issues :-

- The acts relied upon to show that an agent is carrying on business must have continued for a lengthy period of time;

- The acts should have taken place at a fixed place of business;

- The agent should be present in the form of a person carrying on business;

11.4 If an overseas corporation contemplated leasing, equipping and staffing office premises in Hong Kong it would be establishing a place where business could be transacted. The question arose as to whether such an office in Hong Kong would be used to transact business which created

legal obligations. Business could mean the ordinary business of the company so that it might not include matters incidental to that business such as hiring staff or renting office space etc. Many professional advisers were of the view that the intention of the legislation was to permit, without requiring registration, the existence of representative offices not involved in the negotiation or conclusion of contracts with customers or clients. However the point was arguable. The concept of business was extremely wide. Certain UK cases such as South India Shipping Corporation Ltd. v Export-Import Bank of Korea 1985 2A11 ER 219 and the Oriel 1985 3A11 ER tended to support the view that a representative or liaison officer could amount to the establishment of a 'place of business'.

11.5 During the course of discussions, members emphasised the following points :

- although the definition of 'place of business' was unclear and unhelpful, a piecemeal approach to amending the legislation was unsatisfactory. It was necessary to undertake an overall review of the position and status of foreign companies;

- the genesis of the term 'place of business' in the companies legislation arose out of the need to have a

place where legal process could be served;

- the concept of 'place of business' was quite different from the term carrying on business;

11.6 It was also pointed out that the subject had been reviewed by the Standing Committee some three years before when it was agreed that there was no easy legislative solution to what was a complex and difficult issue. It was suggested, and members accepted, that the matter should be examined further in the context of the overall review of the Companies Ordinance and in particular the module dealing with the position of overseas companies undertaking business in Hong Kong.

## Chapter 12

## Resignation of the Auditor of a Company
## Sections 140A(2)(a) and 140A(3)(b)
## of the Companies Ordinance

### 12. Summary of Recommendations

12.1 At the 107th meeting of the Standing Committee members endorsed the proposal of Mr. Marvin K.T. Cheung to amend Sections 140A(2)(a) and 140A(3)(b) of the Companies Ordinance to provide firstly that where the auditor of a company has resigned, notice of the resignation should be filed with the Registrar of Companies and secondly, that the legislation should be more closely modelled on similar provisions contained in the 1985 UK Companies Act.

### Background

12.2 Under Section 140A, an auditor may resign at any time by depositing notice in writing at the registered office of the company. The notice must contain either :-

(a) a statement that there are no circumstances connected with his resignation which he considers should be brought to the notice of members or creditors of the company; or

(b) a statement of such circumstances.

12.3 Within 14 days, a public company must send a copy to the Registrar and, where the notice included a statement setting out reasons for his registration, a copy to every person entitled to receive a copy of the auditor's report. Under Section 129G(1) of the Companies Ordinance, a copy of the auditor's report together with the balance sheet, profit and loss account and director's report must be sent to every member of the company and every debenture holder and all other persons so entitled. It was not clear whether the phrase 'other persons so entitled' could include creditors. The present practice was to send those papers only to the members of the company to whom the auditor was reporting.

12.4 Section 140A was broadly modelled on Sections 392, 392A and 394 of the 1985 UK Companies Act. In support of the proposal, the proponent Mr. Marvin K.T. Cheung opined :

> "Section 140A(2)(a) of the Ordinance requires a statement from the auditor for matters to be brought to the attention of members or creditors. Under Section 140A(3)(b), only those persons who have the rights to receive annual accounts would have the rights to receive the statement. Major creditors of a company (e.g. banks and trade creditors) may not

have the right to receive the auditor's statement which provides vital information to them for assessing their credit risk exposures. Such deficiency in the current regime would undermine the protection of creditor's interests."

12.5 The following passage from the third edition of Farrar's Company Law clearly explains the underlying policy for the legislation :

"As far as the removal, replacement or resignation of auditors is concerned the legislative provisions reflect a trend towards strengthening the position of auditors vis-a-vis the management so that the auditors are in a better position to promote the accountability of management to the shareholders and indirectly thereby to serve the public interest by ensuring the efficient use of company's assets. Although auditors may always be removed by ordinary resolution, any resolution to remove or replace auditors requires special notice. Furthermore auditors who for any reason cease to hold office must deposit with the company a statement setting out any relevant circumstances which they consider should be brought to the attention of members or creditors, or, if there are none the statement must say so. If the statement does set out relevant circumstances the

company must send a copy to everyone entitled to receive the accounts. If auditors are being removed or replaced a general meeting will necessarily be held but if auditors resign and state that there are relevant circumstances they may requisition a general meeting. Prior to any such meeting the auditors may require the company to circulate a statement. Auditors due to be replaced will have the right to attend and speak at the meeting by virtue of still being auditors until they are replaced. This right is specifically extended to auditors who have been removed, or who have resigned notwithstanding that they are no longer in office."

12.6 During the course of discussions the following points were made :

- Whilst it would be difficult to ascertain at any moment in time who exactly the creditors of a company were, a simpler solution would be to file the notice of resignation with the Registrar of Companies. This would then be available as a public document available for inspection;

- There was insufficient 'Public Interest' in the reasons underlying the resignation to warrant the gazetting or advertising of the notice of resignation;

- Under the UK legislation, it was possible for a company to apply to a court to prevent a mischievous auditor from publicising his reasons for resignation prior to publication. In Hong Kong, however, because of the wording of the legislation there was some doubt as to whether this could be done which accounted for the proposal to bring the HK legislation into kilter with the UK legislation;

- It was important for creditors as well as shareholders to be made aware of the auditor's reasons for resignation;

## Chapter 13

## Disqualification of Company Directors - Part IVA of the Companies Ordinance and Amendments to the Securities & Futures Commission Ordinance to Provide for Powers for Disqualification of Directors

### 13. Summary of Recommendations

13.1 At the 110th meeting of the Standing Committee members supported proposals to amend the Companies Ordinance and the Securities & Futures Commission Ordinance with regard to the disqualification of directors in the following manner :

The Companies Ordinance

(a) For the purposes of Part IVA which deals with the disqualification of directors, to extend the definition of the word 'company' to include an overseas company but only if it was actually carrying on business in Hong Kong. In addition, it was proposed to amend the legislation to empower the court, when it made a finding of misfeasance or other breach of fiduciary duty against a director, to disqualify a director.

The Securities & Futures Commission Ordinance (SFCO)

(b) To amend Section 37A of the SFCO by giving power to the court to grant disqualification orders on the ground that a 'relevant officer' had acted dishonestly or had been in breach of his fiduciary duty;

(c) Such a disqualification order, if granted, should prevent a person from participating in any way in the affairs of :

(i) any listed company;

(ii) any subsidiary or associate company of such a listed company; and

(iii) any other company which may be specified in the order.

(d) The Securities & Futures Commission should be empowered to petition for such an order after consultation with the Financial Secretary.

(e) The petition could be against any person who is or had been, at the relevant time, a director, secretary, manager or other officer of a listed

company (whether or not at the time it was listed).

(f) The person may be prohibited for such period as is set out in the order from acting as a director etc. of a listed company or be in any way concerned with the management of a listed company. This order would extend to associate and subsidiary companies as well as any other company set out in the order.

**Background**

13.2 Part IVA of the Companies Ordinance which was enacted in 1994 effected wide ranging changes to the grounds upon which unfit directors and others could be disqualified. However, it was brought to the attention of the authorities that the word 'company' which is defined in the ordinance as being formed and registered in Hong Kong did not include overseas companies. Although Section 168D of the ordinance prohibited a disqualified person from being a director or taking part in the management of a company it would not prevent the disqualified person from being a director of a foreign company carrying on business in Hong Kong. It was therefore proposed and this was endorsed by members that an amendment should be effected to extend the term 'company' to overseas companies carrying on business in Hong Kong to prevent disqualified persons from being directors of such companies.

13.3 With regard to the amendments to the SFCO it was pointed out by Mr. Justice Rogers in Re: Chesterfield Limited, MP No. 3504 of 1994 that the wording of Section 37A did not empower the court to hand down disqualification orders against delinquent directors and officers of a company. In view of the very serious allegations of misfeasance which were eventually proved to the satisfaction of the court it seemed somewhat inconsistent that the court was empowered to restrain directors from managing or being involved in the affairs of a company but not to disqualify them. The proposed amendments would address this.

13.4 If the SFCO was to be amended to empower the court to disqualify unfit directors etc. where they have been guilty of conducting the affairs of a company in a manner unfairly prejudicial to its members or a part thereof, then it also seemed logical to amend the Companies Ordinance in a similar manner so that the two ordinances were in kilter in this regard. It was important to note that the remit of the SFC was limited to listed companies. Other regulatory authorities, such as the Official Receiver's Office, should be given similar powers when dealing with e.g. insolvent private companies and this accounted for the need to change the Companies Ordinance along similar lines.

## Chapter 14

## Transparency of Advisory Boards and Committees

### 14. Summary of Recommendations

14.1 At the 107th meeting of the Standing Committee members recommended that a brief summary of the main recommendations arising from their deliberations at each meeting should be released shortly thereafter. Neither the meetings themselves nor the minutes of meetings should be open to the Public or be made available for Public scrutiny.

### Background

14.2 A LegCo Panel on Home Affairs had requested that all advisory boards and committees set up by Government should operate with a higher degree of openness and transparency than they had hitherto. Specifically, the Panel had recommended to Government that :

(a) advisory bodies should hold their meetings in public (reasons should be given for any committees which had decided not to do so); and

(b) the agenda and minutes of meetings of advisory committee should be made available to members of the public.

14.3 During the course of discussions members stressed the following points :

- the annual report of the Standing Committee was distributed to LegCo, ExCo, newspapers and the various business, professional and commercial bodies which the SCCLR normally consults;

- if the meetings were to be opened up, a much larger room and simultaneous translation facilities would have to be provided;

- opening up the minutes and the meetings would in all probability inhibit full and proper debate as members would be individually quoted;

- the recommendations of the SCCLR, if they were to be legislatively enacted, were fully aired in ExCo and LegCo beforehand;

- the SCCLR was analogous to a 'think tank' and like other 'think tanks' set up by Government should not therefore be open to Public Inspection in the manner suggested;

14.4 Certain members accepted that the trend was clearly towards having greater transparency in the workings of

Government committees. But the majority of members believed that the present regime should remain undisturbed for the reasons set out in paragraph 14.3 above.

## Chapter 15

## De-Regulation of Company Forms - The Five Statutory Forms Contained in the 2nd, 4th and 5th (Parts II, IIA & III) Schedules to the Ordinance; the 48 Statutory Forms in the Companies (Forms) Regulations

### 15. Summary of Recommendations

15.1 At the 107th meeting of the Standing Committee, members endorsed the proposal of the Registrar of Companies that the statutory forms contained in the Second, Fourth and Fifth (Parts II, IIA & III) Schedules to the Companies Ordinance and the 48 statutory forms set out in the Companies (Forms) Regulations be de-regulated and that the Registrar of Companies be empowered, within certain broad parameters laid down in the relevant sections of the Companies Ordinance, to determine the content and format of those forms. Details of the statutory forms contained in the Second, Fourth and Fifth Schedules and the 48 statutory forms set out in the Companies (Forms) Regulations are set out in Appendices 1 and 2 herein respectively.

**Background**

15.2 For some time, the Registrar of Companies had been

considering the desirability of de-regulating most of the statutory forms provided for in the companies legislation. Much of the corporate data filed with the Companies Registry had to be filed on the statutory forms prescribed in either the Second, Fourth and Fifth Schedules or the Companies (Forms) Regulations. By virtue of Sections 359A and 360(3)(a) of the Companies Ordinance the Governor-in-Council may amend the Companies (Forms) Regulations and those forms set out in Parts II, IIA and III of the Fifth Schedule. The forms in Second and Fourth Schedules can only be amended by the Legislative Council. Any amendments, therefore, to those forms could take up a considerable amount of time and tie up resources.

15.3 In addition the Companies Registry was of the view that there was a pressing need to completely revise all of those forms to make them more 'user friendly' and 'computer compatible'. The current forms were designed a long time ago in an era when the number of registered companies and the consequential data received by the Companies Registry was a fraction of current levels. The complexity and length of some of those forms was a disincentive for small companies, in particular, to comply with the provisions of the ordinance.

15.4 Whilst it would be possible to revise the forms by using the existing legislative procedures, the resource

implications whenever amendments were required would be formidable. A better approach would be to de-regulate them now and to deal with future amendments on an administrative basis.

15.5 During discussions it was pointed out that the SFC had undertaken a similar exercise when it was first established. The forms in use at the SFC had been approved by a specially appointed board. In addition, members were advised that the form in use with regard to the disclosure by a company of the purchase of its own shares could be changed administratively by the Companies Registry. The Commissioner for Rating & Valuation was also empowered under Section 54 of the Rating Ordinance to specify the form and content of certain forms.

15.6 Members agreed that, provided any proposed changes to the forms were circulated to the business, professional and commercial community beforehand for their consideration, the proposals should be supported.

Appendix 1

| Item No. | Description |
|---|---|
| 1. | 2nd Schedule - Form of Statement in lieu of prospectus to be delivered to Registrar by a private company on becoming a public company and reports to be set out therein. |
| 2. | 4th Schedule - Form of statement in lieu of prospectus to be delivered to Registrar by a company which does not issue a prospectus or which does not go to allotment on a prospectus issued, and reports to be set out therein. |
| 3. | Part II Fifth Schedule - Annual return of a company having a share capital and not being a private company. |
| 4. | Part IIA Fifth Schedule - Annual return of a private company having a share capital. |
| 5. | Part III Fifth Schedule - Annual return of a company not having a share capital |

List of Forms in the Schedule

| Form number | Relevant section | Nature of Form |
|---|---|---|
| IA | 19(1) | Application by an unregistered company to be re-registered as limited. |
| IB | 45 | Return of allotments. |
| I | 45(2) | Particulars of a contract relating to shares. |
| II | 46(1)(e)(i) & (d) | Statement of the amount or rate per cent of the commission payable in respect of shares and of the number of shares which persons have agreed for a commission to subscribe absolutely. |
| IIA(i) | 47E(6) | Declaration in relation to financial assistance for the acquisition of shares. |
| IIA(ii) | 47E(6) | Declaration by a majority of directors of a holding company in relation to financial assistance for the acquisition of shares. |
| IIB | 47G(4) | Notice of application made to the court for the cancellation of a special resolution regarding financial assistance for the acquisition of shares. |
| IIC | 49K(3) | Declaration in relation to the redemption or purchase of shares out of capital. |
| III | 55 | Notice of increase in nominal capital. |
| IIIA | 71A(1) | Application for the issue of a new share certificate. |
| IIIB(i) | 71A(3)(a) | Notice of intention to issue new share certificate. *(L.N. 298 of 1979)* |
| IIIB(ii) | 71A(3)(b) | Notice of intention to issue new share certificate. |
| IIIC | 71A(8) | Notice of cancellation of previous share certificate and issue of new certificate. |
| IIID | 74A(3) | Notice of place where a register of holders of debentures or debenture stock is kept or of any change in that place. |
| IV | 80 | Particulars of a mortgage or charge created by a company registered in Hong Kong. |
| V | 82 | Particulars of a mortgage or charge subject to which property has been acquired by a company registered in Hong Kong. |
| VI | 83(1) | Register of mortgages and charges, and of memoranda of satisfaction. |
| VII | 83(4) | Chronological index of charges entered in the Register. |
| VIIA | 88(3) | Notice of place where copies of instruments creating charges are kept or of any change in that place. |
| VIIB | 89(3) | Notice of place where register of charges is kept or of any change in that place. |
| VIIC | 95(3) | Notice of place where register of members is kept or of any change in that place. |
| VIII(i) | 107(3) | Annual return of a company having a share capital and not being a private company by certificate of no change in information contained in last return. |
| VIII(ii) | 107(3) & (4)(b) | Annual return of a private company having a share capital by certificate of no change in information contained in last return. |
| VIIIA | 119A(2) | Notice of place where minute books are kept or of any change in that place. |
| IX | 131(6) | Notice of passing of resolution removing an auditor. |
| IXA | 157D(2) | Notice of resignation of director or secretary. |
| X(i) | 158(4) | Return of first directors and secretary. |
| X(ii) | 158(4) | Notice of change of directors or secretary or in their particulars. |
| XA | 158A(2) | Notice of place where register of directors and secretaries is kept or of any change in that place. |
| XIA | 300A(1)(a) | Notice to company of appointment of receiver or manager. |
| XIB(i) | 300A(1)(b) & 300B | Statement as to affairs (Statutory Declaration). |
| XIB(ii) | 300A(1)(b) & 300B | Statement as to affairs (Statutory Declaration). |
| XIC | 300A(2) & 301(1) | Receiver or manager's abstract of receipts and payments. |
| XII | 301 | Receiver or manager's abstract of receipts and payments. |
| XIII | 9th Schedule para. 3 | Notice to dissenting shareholders. |
| XIV | 9th Schedule para. 11 | Notice to dissenting shareholders. |
| I(F) | 80 & 91 | Particulars of a mortgage or charge on property in Hong Kong created by a company incorporated outside Hong Kong. |
| II(F) | 82 & 91 | Particulars of a mortgage or charge subject to which property in Hong Kong has been acquired by a company incorporated outside Hong Kong. |
| III(F) | 333(1)(b) & (2) | List and particulars of the directors and secretary of an overseas company. |
| IV(F) | 333(1)(c) | List of (1) addresses of some one or more persons resident in Hong Kong authorized to accept service on behalf of an overseas company (2) address of the principal place of business of the company in Hong Kong and (3) the respective addresses of the principal place of business, if any, and the registered office of the company in the place of its incorporation. |
| V(F) | 335(1) | Return of alteration in the charter, statutes etc. of an overseas company. |
| VI(F) | 335(1) | Return of alteration in the names and addresses of persons resident in Hong Kong authorized to accept service on behalf of an overseas company. |
| VII(F) | 335(1) | Return of alteration in directors or secretary of an overseas company. |
| VIII(F) | 335(1) | Return of alteration in the address of the principal place of business in Hong Kong of an overseas company. |
| IX(F) | 335(1) | Return of alteration in the address of the registered office (or its equivalent) of an overseas company in the place of its incorporation. |
| X(F) | 335(2) | Return of change in the corporate name of an overseas company. |
| XI(F) | 337B(3) | Statement of name, other than corporate name, under which an overseas company proposes to carry on business in Hong Kong. |
| XII(F) | 337B(3) | Statement of name, other than corporate name, under which an overseas company proposes to carry on business in Hong Kong in substitution for name previously registered. |

*(L.N. 240 of 1975; L.N. 168 of 1984; L.N. 352 of 1991; L.N. 50 of 1994)*

## Chapter 16

## A Guide for Directors of Listed Companies; Guidelines for Directors 1995

16.1 At the 109th meeting of the Standing Committee two recently issued 'Guides for Directors' were tabled for discussion.

**A Guide for Directors of Listed Companies**

16.2 This was published in July 1995 by the Hong Kong Stock Exchange : "..... to provide a brief and practical introduction for directors concerning their responsibilities under the rules governing the listing of securities ..... the Listing Agreement entered into by all listed companies with the exchange and the declaration and undertaking with regard to directors."

The general objective underlying the publication was to provide executive and non-executive directors alike with general and specific guidelines as to their duties under the listing rules.

16.3 During discussions, members were advised that by the end of the year all listed companies would be expected to state in their annual reports if they had complied with the code of best practice details of which were set out in

both the publication and the listing rules. The Stock Exchange had also been holding workshop seminars which more than 300 directors from listed companies had attended. The objective was to conduct similar seminars every three months. Where good corporate governance was concerned it was insufficient for directors to be appraised of their duties under the Companies Ordinance - they also had to understand their obligations under both the listing rules and the common law.

16.4 Members were generally enthusiastic about the publication. It was difficult for busy directors to keep abreast of the amendments which had been effected to the listing rules over the past several years. This document went some considerable way to address this in an easily understood and digestible fashion which perhaps the two volumes of the listing rules themselves did not easily lend themselves to.

Guidelines for Directors 1995

16.5 The Hong Kong Institute of Directors was responsible for the publication of this document. As stated in the preface :

> "In compiling these guidelines the Institute of Directors has had three distinct groups of readers in mind :-

(i) Newly appointed directors, for whom it is hoped that the work will provide a reasonably brief outline of their new duties;

(ii) All those currently holding the office of director who are uncertain about the breadth and scope of their responsibilities and feel that they need a general refresher;

(iii) All practising directors who need a brief initial guide to possible courses of action in a new situation."

16.6 It was modelled on "Guidelines for Directors" published by the UK Institute of Directors, and it was an effort to summarise the law regarding the statutory, fiduciary and common law duties directors are subject to. Running to 91 closely typed pages and 347 paragraphs it could not be accused of brevity. In fact the contrast between this publication and that issued by the Stock Exchange could not have been greater. Many members opined that this was its weakness - it was over long, complex and it attempted to address far too many issues instead of concentrating on the more important points. As a consequence members did not believe it would get its message across to the very people who most needed it - directors of the smaller scale of commercial enterprise.

## Chapter 17

## KPMG Corporate Fraud Surveys for 1994 and 1995

17.1 At the 108th meeting of the Standing Committee, the results of Corporate Fraud Surveys undertaken by KPMG Peat Marwick in 1994 and 1995 were tabled for discussion and comment.

17.2 The highlights of the 1995 survey were :

- 77% of the respondents considered fraud to be a serious problem for business;

- there was growing pessimism about the future with the impending change of sovereignty, economic pressures and weakening social values being given as the reasons;

- there was a slight drop in the numbers of respondents experiencing fraud in the last 12 months;

- more than a third of respondents had experienced losses of HK$1 million or more;

- the most common types of fraud reported were purchases fraud;

- internal controls were critical to a company's strategy for fighting fraud;

- internal controls were credited as being the means of detection in more than half of cases;

- investigation and dismissal of the perpetrators were the most frequent response to fraud;

- as to fraud prevention, corporate codes of conduct have been implemented by 69% of respondents;

- 12% or so of respondents had been the victims of fraud during the previous 12 months;

17.3 During discussions members opined that it was necessary for companies to be constantly vigilant to reduce the occurrence of fraud. Many of the frauds perpetrated had little to do with the computer systems in place. Rather, "Purchases Fraud" which formed the single largest category of reported fraud was usually effected without the necessity of tampering with the computer systems. Members agreed to keep the issue under review.

## Chapter 18

## Authorised Representatives of Overseas Companies

## Section 333A of the Companies Ordinance

### 18. Summary of Recommendations

18.1 At the 108th Meeting of the Standing Committee members proposed that there should be no change to the existing legislative requirements viz that an overseas company should continue to retain for a three year period after the cessation of business the name and address of a person resident in Hong Kong who was authorised to accept service of process and notices on its behalf.

### Background

18.2 Under Section 333(1) of the Companies Ordinance a firm of accountants or solicitors can be appointed as the authorised representative of an overseas company, (in addition to natural persons) to accept the service of process and also the service of any notices on its behalf. Under Section 333A(1), an overseas company is obliged to keep registered, for a three year period following cessation of business, the name and address of a person resident in Hong Kong who is authorised to accept the service of proceedings and notices on its behalf.

18.3 The Hong Kong Society of Accountants (HKSA), in its submission on amendments to the Companies Ordinance, had recommended that the time requirement set out in Section 333A should be reduced. In support of its proposal the HKSA had stated :

> "Section 333A requires an overseas company to retain an authorised representative for three years after being de-registered. If such a company is no longer doing business in Hong Kong, it will obviously not have a representative in Hong Kong to authorise. It can of course pay somebody else to perform this function if it so chooses. However, three years would appear to be an unnecessarily long period over which such a nominee representative is required to be maintained. We suggest that the SCCLR should consider having the period reduced."

18.4 During the course of deliberations members thought that the current time requirement should remain unchanged for the following reasons :

- the three year time period was reasonable and necessary given that any problems arising after an overseas company had ceased business could take that length of time to surface;

- the issue had been very carefully considered by the Company Law Revision Committee in 1973 before its recommendations were made and that committee thought that the three year period for the retention of an authorised representative was appropriate;

- the Companies Registry had never received any complaints that the present mandatory period was burdensome or unduly onerous and in all the circumstances the system was working well.

## Chapter 19

## Corporate Rescue and Insolvent Trading

19.1 At the 109th meeting of the Standing Committee a consultation paper on Corporate Rescue and Insolvent Trading, prepared by the Law Reform Commission of Hong Kong, was tabled for discussion. A summary of the main recommendations is set out at Appendix 1. The consultation paper itself runs to some 140 pages.

19.2 Some of the key recommendations of the paper were :

- once a company had been placed into 'provisional supervision' by its board of directors following financial difficulties, there would be a 30 day moratorium against legal proceedings;

- an independent person such as an accountant or a solicitor would be charged with the responsibility of preparing a financial assessment of the company's prospects for its creditors;

- the proposal was aimed at a 'typical' medium size company and the underlying objective was to rebuild the company's financial position within a reasonable time and at reasonable cost;

- notice of provisional supervision would be given to the secured creditors who then had three working days to decide if they wished to exercise their rights under the security;

- to persuade directors to place a company in provisional supervision when it fell into financial difficulties, it was necessary to introduce a new civil offence titled : Insolvent Trading;

- if the directors allowed a company to continue trading whilst insolvent, a liquidator, in the event of it being wound up, could seek damages against the responsible persons for the civil offence of Insolvent Trading;

19.3 During the course of discussions, certain members expressed concern that the proposals for 'Corporate Rescue' did not provide for disgruntled minor creditors to enable them to apply to the courts to seek relief from a scheme for corporate rescue which may have been forced through by the larger creditors. Under the present legislative regime, (Section 166 of the Companies Ordinance which dealt with arrangements and reconstructions), notwithstanding that a proposal for a scheme of arrangement had been carried by the required two-thirds majority, a disgruntled shareholder or creditor

could still seek relief from the courts. Similar provisions should be incorporated into the corporate rescue proposals.

19.4 In response, it was pointed out that the Insolvency Sub-committee had very carefully considered the question of voting. The only 'let out' for a creditor was to apply to court to be exempted from the scheme on the grounds of hardship. The typical rescue scheme usually involved two or more banks and it was frequently the case that small creditors stymied or indefinitely delayed the scheme to obtain better terms for themselves, which could and often did, jeopardise any attempt at a corporate rescue. It was against this background that the recommendations had been made.

# THE LAW REFORM COMMISSION'S

# SUB-COMMITTEE ON INSOLVENCY

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# SUMMARY

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# CONSULTATION PAPER ON

# CORPORATE RESCUE AND INSOLVENT TRADING

## A. Corporate Rescue

1. The Law Reform Commission's sub-committee on insolvency has identified the need for a corporate rescue procedure in Hong Kong.

2. The procedure, to be known as "provisional supervision", would facilitate a company in working out a voluntary arrangement with creditors that would allow a company to continue in business rather than go into liquidation.

3. At present, the only statutory provision that can assist companies in a workout is section 166 of the Companies Ordinance, which is generally recognised as being inadequate for the purpose. The other vehicle for restructuring, receivership, would continue to operate outside of provisional supervision but it is a process initiated by a company's secured creditors, not by the company itself.

4. Several other jurisdictions have well established corporate rescue procedures including (i) the United Kingdom with two types of procedure, Voluntary Arrangement and Administration under the Insolvency Act 1986, (ii) a new provision for voluntary arrangements under the Australian Corporation Law 1992, and (iii) the Chapter 11 procedure in the United States of America.

5. Provisional supervision would facilitate a company in reaching a voluntary arrangement with its creditors. The aim is to put in place a procedure that is flexible, quick and as cheap as possible to operate. This would be achieved by the imposition of a moratorium (or stay) on proceedings against a company during provisional supervision, combined with a tight time frame within which the person who would co-ordinate the procedure, the provisional supervisor, would have to operate.

6. There are also proposals for the introduction of a provision that would make directors and certain senior managers liable to pay compensation for debts of a company incurred through insolvent trading.[1]

7. This summary makes a brief statement of the main proposals and does not address many of the technical points and procedures. For a more comprehensive understanding of the proposals, please refer to the Consultation Paper, which includes a model Bill.

*Applies to*

8. Provisional supervision would apply to all companies registered under Part I of the Companies Ordinance, that is, most companies, and to companies registered under Part XI, that is oversea companies. The procedure would not apply to industries which are already regulated by statute, such as banking, insurance, and securities and futures, though the relevant regulatory authorities would have the option of applying the procedure through their own legislation.[2]

*Purposes*

9. No restriction is placed on what may be achieved through a voluntary arrangement. A company could, for example, seek an extension of time to pay its debts, make a composition in satisfaction of its debts or vary the rating for repayment of its debts. A company could also seek a voluntary arrangement whether it was solvent or insolvent.[3]

*Initiated by*

10. The procedure should be initiated by the company through the board of directors as they would be best placed to know the financial and trading position of a company. Creditors would not generally be able to initiate though a receiver appointed by a secured creditor would have the option of consenting to the procedure being used if the directors make representations to a receiver for it to be used. The same situation would apply once a liquidator had been appointed.[4]

*The provisional supervisor*

11. The preparation of the proposal and control of the business of a company during the stay would rest with an independent professional, to be known as the provisional supervisor. The role of the provisional supervisor would be such that it could only be carried out by an experienced professional, such as a solicitor or accountant experienced in company reorganisation and insolvency matters.[5]

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[1] Chapter 19.
[2] Paragraphs 2.3 to 2.14.
[3] Paragraphs 3.1 to 3.9.
[4] Paragraphs 4.1 to 4.10.
[5] Paragraphs 7.1 to 7.6.

12. The provisional supervisor would have to be, and be seen as being, completely independent. To this end it is proposed that the provisional supervisor could not be removed by any of the parties. There would be a safeguard in that the provisional supervisor would have to apply to the court for extensions to the stay or make regular reports to the court during a long extension of the stay. If the court decided that the provisional supervisor was not acting with due diligence in his functions the court could refuse to grant further extensions to the stay.[6]

13. It is proposed that the provisional supervisor would control the business of the company. The provisional supervisor would also have extensive powers to facilitate his running of the company, such as to execute documents in the name of the company and to borrow money.[7] This would serve to give creditors confidence that the assets of the company were not being dispersed by directors hiding behind the stay provided by provisional supervision or that poor management was getting a business into even greater trouble.

14. There would be advantages in retaining capable, honest directors and management. Consequently, the provisional supervisor would have a discretion to remove and appoint directors and to delegate powers back to existing management.[8]

15. As the provisional supervisor would be operating within severe time constraints, and as he would need to ascertain the state of a company's affairs within a short time, it is proposed that directors, employees and former employees, any other relevant person should be obliged to provide or assist the provisional supervisor with the preparation of a statement of affairs of the company, the costs of which would be paid out of company assets.[9]

16. The provisional supervisor would be under a duty to do all things necessary to protect the assets of a company for the benefit of creditors. This would be subject to an overriding duty to supervise the affairs of the company and to carry out his functions. The provisional supervisor would be able to go to the court for directions on any matter.[10]

17. The provisional supervisor would not be liable for any debts of a company incurred before his appointment. The provisional supervisor would not be obliged to adopt any contract a company had entered into before his appointment and no contract could be terminated by reason only that a company had gone into provisional supervision. The provisional supervisor could, however, be personally liable on any contract entered into in performance of his functions but he would be entitled to an indemnity out of the assets of a company.[11]

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[6] Chapter 11.1 to 11.5.
[7] Paragraph 8.25.
[8] Paragraphs 8.22 to 8.24.
[9] Chapter 9.
[10] Chapter 10.1 and 10.2.
[11] Chapter 10.1 to 10.9.

18. A provisional supervisor's remuneration would be agreed, in so far as possible, before appointment and the terms would be made known to interested parties.[12]

*Secured creditors*

19. It is proposed that major secured creditors with a floating charge over the whole or substantially the whole of a company's assets should have the right to elect whether to participate in the provisional supervision. To simply impose provisional supervision on major secured creditors, usually banks, would ignore the fact that their co-operation would be required if a rescue package was to be put together and that they would probably be the supplier of additional lending. To suspend the rights of major secured lenders while provisional supervision was in place would interfere with the rights of secured lenders to appoint receivers. This is one of the primary tools of commerce and provisional supervision takes account of this. [13]

*The moratorium (or stay of proceedings)*

20. Perhaps the single most important feature of the procedure would be the imposition of a stay of proceedings against the company by the court once a company went into provisional supervision. A stay would be necessary to prevent individual creditors from exercising their normal right to take proceedings and to preserve the assets of the company while a proposal was prepared for consideration by creditors.

21. Court involvement would be necessary but an effort has been made to keep it to a minimum to save on the expense of court appearances. The court could impose a stay for up to 6 months after which, if no agreement on a voluntary arrangement had been reached by creditors it would be a matter for them whether to continue with a self imposed stay or for the company to be wound up.

22. An initial stay of 30 days would be imposed by the court, after which the provisional supervisor could apply for an extension or extensions for a further 5 months if he considered that he could complete a proposal within the time of any extension.[14]

*Super priority borrowing*

23. It is recognised that any company which is in financial difficulties, and which seeks a rescue package, will probably need additional funding to see it through any reorganisation. The problem is that a company is only likely to be able to raise capital if the lender is given security, or priority, ahead of existing debts. It is proposed that a company in provisional supervision would be able to raise capital by giving the lender what is known as a "super

[12] Chapter 10.10.
[13] Chapter 13.
[14] Chapter 5.

priority" over existing debts. It is also proposed that super priority lending should only come from a company's existing lenders.[15]

*Procedure*

24. Any proposal for a voluntary arrangement would be put to a meeting of creditors. For any resolution to pass, there would have to be a majority in number and in excess of two thirds on value of creditors voting on the resolution. This would have the effect of protecting the interests of smaller, unsecured creditors as they would usually form the majority in number, and the large secured creditors as they could be expected to hold the greater value of debt.[16]

25. If a meeting of creditors resolved not to accept a proposed voluntary arrangement put forward by a provisional supervisor, the meeting could be adjourned for modifications to the proposal to be made, or it could be resolved that provisional supervision should be terminated and the company wound up.

26. If, however, the meeting was held at or near the end of 6 months in provisional supervision, creditors might also resolve to extend the stay but, in this situation, the extension would not be court supervised.[17]

27. If creditors resolved to accept the terms of a proposed voluntary arrangement, provisional supervision would end and the company would go into supervision while the terms of a voluntary arrangement were implemented.

*Voluntary arrangement under supervision*

28. Under a voluntary arrangement, no creditor bound by the voluntary arrangement could take action against a company that would act to the detriment of the other parties to the arrangement.

29. The terms of the voluntary arrangement would be carried out by a supervisor, who would probably be the original provisional supervisor. The supervisor would have regard to the interests of all parties to the voluntary arrangement, including the creditors, the company and the shareholders of the company. It would be possible to vary the voluntary arrangement, by application to the court, should the need arise.[18]

## B. Insolvent trading

*The main features*

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[15] Chapter 12.
[16] Paragraphs 16.29 to 16.35.
[17] Chapters 14 to 16.
[18] Chapter 17.1.

30. Insolvent trading would impose a civil liability for insolvent trading on (i) directors and (ii) senior management of a company which act in the place of or on behalf of the directors or who take decisions which directors might normally be expected to take, collectively to be known as "responsible persons". Responsible persons would become subject to liability for insolvent trading once a company traded while insolvent or if the company continued to trade when there was no reasonable prospect of preventing the company becoming insolvent.

31. Two presumptions relating to insolvent trading would be introduced: (i) a presumption of continuing insolvency, and (ii) a presumption of insolvent trading where proper accounts and records of a company have not been kept.

32. Responsible persons could employ defences to show that they were not trading while insolvent or that every step had been taken to prevent insolvent trading.

33. The purpose of the provision would be to encourage responsible persons to face the fact that a company was slipping into insolvency at an early date and cause them to address the situation rather than to trade on regardless of the consequences

34. The power to make an application in respect of insolvent trading should vest in the liquidator only. A measured approach is required and the decision whether to make an application should be made on the basis of the chances of recovering compensation from responsible persons for the benefit of the company and not for revenge.

*Directors and senior management should be liable as responsible persons*

*(i) Directors*

35. A broad approach to as to who should be considered to be a director has been taken as we want to prevent directors, or those who act as directors, avoiding liability with the defence that they were not actually appointed as directors.

36. Insolvent trading should apply to all directors whether they are validly appointed directors, executive or non-executive directors, nominee companies appointed as directors, persons who hold themselves out to be directors though they have not been validly appointed, and shadow directors

37. We anticipate some directors, whether because of their particular expertise or for other reasons, will anticipate insolvent trading before the rest of the board. Such directors would face a dilemma as to what to do and should be encouraged to stay on the board rather than resign.

38. Liability for insolvent trading should not be collective and liquidators should take account of a director's actions prior to liquidation. The ability and expertise of a director would be taken into account.

*(ii) Senior management*

39. The top decision makers among senior management could be liable for insolvent trading if they failed to take appropriate action when a company was trading into insolvency.

40. It is desirable in the context of business practice in Hong Kong to include senior management in the provision, as it is common for overseas companies with subsidiary companies in Hong Kong to leave locally appointed management in control of local operations.

41. Senior management may know the day to day financial position of a company as well as the directors. If senior management finds that a company is in danger of trading into a situation of insolvency, it should warn the directors as soon as possible. Provided senior management takes appropriate action in warning the directors and in advising the directors on appropriate action, they should not be liable for insolvent trading.

*Responsible persons' duties*

42. It is not possible to define comprehensively the duties of a responsible person. We have adopted a broad, fact based, criteria which the courts could refine through a body of decisions.

43 The provision would set out the factual conditions which must be established before an application for insolvent trading can be considered. The facts that a liquidator would need to establish are (i) that a responsible person is or has been responsible person of an insolvent company at the time when the debt or debts were incurred and that (ii) the company was insolvent at that time or there was no reasonable prospect of avoiding becoming insolvent.

44. A liquidator must then consider whether a responsible person, at that time, (i) knew the company was insolvent, or (ii) ought to have known that the company was insolvent or would so become, or (iii) that there were reasonable grounds for suspecting that the company was insolvent or would become insolvent and failed to take action to prevent the company from incurring the debt. A director is, therefore, to be judged by an objective standard of the reasonable director even though he is lacking or below average in knowledge, skill or experience, but by his own standards, if, for example, his qualifications and experience are above average.

*Presumptions*

45 The concept of presumptions would be a benefit to liquidators in that they shift the burden of proving the contrary to the responsible persons

*(i) Presumption of continuing insolvency*

46 The effect of a presumption of continuing insolvency is that, if it is proved that a company was insolvent at a particular time during the 12 months ending on the date of

commencement of its winding up, it would be presumed that the company was insolvent throughout the period beginning at that time and ending with the winding up of the company.

*(ii) Presumption of failing to keep proper accounts*

47. If it is proved that a company failed to keep proper accounting records that report and explain its transactions and financial position during the 12 months before winding up, or by failing to keep such accounting records in the manner prescribed, or if the company failed to retain such accounting records for the period required by that section, there should be a presumption that the company was insolvent throughout the relevant period.

*Defences*

48. A responsible person should have a defence to an application against him for insolvent trading if he can satisfy the court that, at the time when he knew or ought to have known that the company was insolvent or would become so or that there were reasonable grounds for suspecting that the company was insolvent or would become insolvent, he took every step with a view to minimising the potential loss to the company's creditors as he ought to have taken.

*Responsible persons may be liable to compensate the company*

49. If the court finds that a responsible person is liable for trading while insolvent, it should be able to order the responsible person to pay compensation to the company equal to the amount of that loss or such other sum as the court thinks fit.

*Director may be disqualified for insolvent trading*

50. If the court makes a declaration that a responsible person, whether he is a director or senior manager, is liable to pay compensation for insolvent trading, the court should have the discretion to make an order disqualifying that person from being a director of any company under Part IV A of the Companies Ordinance.

## Chapter 20

## The Companies Registry Annual Report for 1994/95

20.1 At the 109th meeting of the Standing Committee the 1994/95 report of the Companies Registry was tabled for information and discussion. Copies of the workload statistics and the annual accounts are at Appendices A and B respectively.

20.2 During discussions, members made the following points :

- There had been a significant decrease in the numbers of new companies being incorporated from 1992/93 levels. However that year had seen an exceptional increase in the numbers of companies incorporating, mirroring perhaps the very large increase in property prices and conveyancing transactions;

- Many incorporators were choosing the British Virgin Island (BVI) as the place to incorporate their companies primarily to avoid both the payment of stamp duty provided for under the Companies Ordinance and also the more stringent regulatory regime provided for under the Hong Kong companies legislation;

- It was very difficult, if not impossible, to

ascertain if companies incorporated overseas had actually established places of business (as opposed to carrying on business) in Hong Kong.

- Under Part XI of the Companies Ordinance, a foreign company was only required to register if it had established a place of business which was not easily or readily ascertainable. It was for those overseas companies themselves to register within one month with the Companies Registry if they had established a place of business;

- There had been a huge increase in the numbers of 'striking off' actions to get rid of the 'deadwood' i.e. companies that had been inactive for years and which had repeatedly failed to file annual returns as they were required to do. A welcome effect of the exercise was to force many defaulting companies into compliance which had bolstered the Companies Registry income substantially.

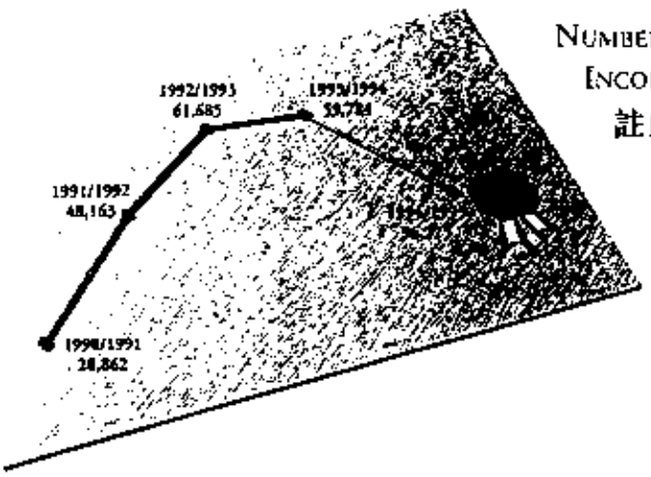
# WORKLOAD STATISTICS
# 工作量統計數字



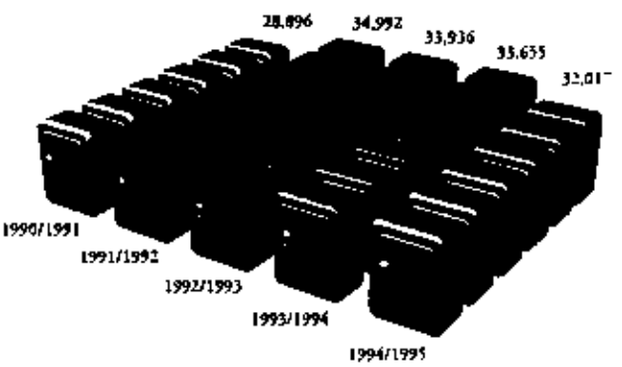
APPENDIX A
附錄 A

| | YEAR TO 31 MARCH 截至三月卅一日止年度 1995 | 1994 | INCREASE/(DECREASE) 增加(減)幅度 % |
|---|---|---|---|
| **New companies 新公司** | | | |
| Incorporations 註冊成立 | | | |
| - public 公眾公司 | 254 | 252 | 0.8 |
| - private 私人公司 | 36,521 | 59,532 | (38.7) |
| Overseas companies registered 登記的海外公司 | 592 | 517 | 14.5 |
| **General registration of documents 登記公司文件** | | | |
| Charges registered 登記的押記 | | | |
| - number 數目 | 32,017 | 33,655 | (4.9) |
| - amount secured ($m) 擔保款額 (以百萬元計) | 67,948 | 65,271 | 4.1 |
| Documents received 所收到文件的數目 | 1,179,219 | 1,252,953 | (5.9) |
| Change of name applications 更改名稱申請書 | 12,075 | 12,960 | (6.8) |
| **Search facilities 查冊設施** | | | |
| Searches made 進行查冊 | 1,936,033 | 1,936,701 | - |
| **Prosecutions 檢控** | | | |
| Summonses issued 發出傳票 | 226 | 211 | 7.1 |
| Conviction rate 定罪率 | 91% | 97% | (6.2) |
| **Striking off action 剔除行動** | | | |
| Action commenced 已展開行動 | 26,561 | 3,670 | 623.7 |
| Companies struck off 被剔除的公司 | 5,073 | 1,043 | 386.4 |
| **Liquidation 清盤** | | | |
| Proceedings commenced 已展開清盤行動 | | | |
| - voluntary 自行 | 3,128 | 2,840 | 10.1 |
| - compulsory 強制 | 421 | 449 | (6.2) |
| Companies wound-up 已清盤公司 | | | |
| - voluntarily 自行 | 2,695 | 2,899 | (7.0) |
| - compulsory 強制 | 80 | 181 | (55.8) |

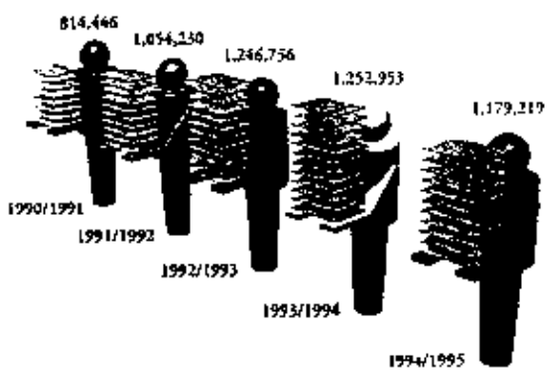
## NUMBER OF COMPANIES INCORPORATED
## 註冊成立公司總數



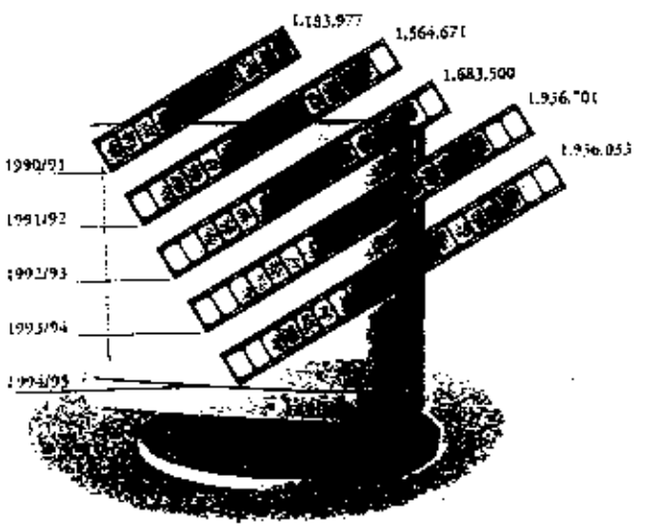

## NUMBER OF CHARGES REGISTERED
## 押記登記數目




## DOCUMENTS RECEIVED FOR FILING
## 遞交登記文件數目




## NUMBER OF SEARCHES MADE
## 查冊數目



# ANNUAL ACCOUNTS OF THE COMPANIES REGISTRY TRADING FUND FOR THE YEAR ENDED 31 MARCH 1995

# 公司註冊處營運基金在截至1995年3月31日止的周年帳目表

Prepared and submitted pursuant to section 7(4) of the Trading Funds Ordinance

按照營運基金條例第7(4)條製備及提交

# COMPANIES REGISTRY TRADING FUND PROFIT AND LOSS ACCOUNT
# 公司註冊處營運基金損益表



| | Notes 註解 | Year ended 31 March 1995 截至1995年3月31日止年度 $000 | 8 months ended 31 March 1994 截至1994年3月31日止八個月 $000 |
|---|---|---|---|
| Turnover 營業額 | (3) | 176,177 | 106,485 |
| Operating costs 經營成本 | (4) | (140,508) | (77,056) |
| **Operating profit 經營所得盈利** | | 35,669 | 29,429 |
| Other income 其他收入 | (5) | 4,178 | 1,464 |
| Interest expenses 利息支出 | (6) | (20,140) | (11,982) |
| **Profit before taxation 除稅前盈利** | | 19,699 | 18,911 |
| Taxation 稅款 | (7) | (3,186) | (3,309) |
| **Profit after taxation 除稅後盈利** | | 16,513 | 15,602 |
| Dividend 股息 | (8) | (4,954) | - |
| **Profit retained 保留盈利** | | 11,559 | 15,602 |
| Rate of return on fixed assets 固定資產回報率 | (9) | 8.1% | 6.2% |

The notes on pages 24 to 29 form part of these accounts.
第24至29頁的註釋本為此帳目的一部分

A. H. PATEL
Acting Registrar of Companies and
General Manager,
Companies Registry Trading Fund
7 August 1995

白德
署理公司註冊處處長兼
公司註冊處營運基金
總經理
一九九五年八月七日

# COMPANIES REGISTRY TRADING FUND BALANCE SHEET
# 公司註冊處營運基金資產負債表

| | Notes 註解 | As at 31 March 1995 在1995年3月31日 的結算 $000 | As at 31 March 1994 在1994年3月31日 的結算 $000 |
|---|---|---|---|
| **Assets employed : 可動用資產** | | | |
| Fixed assets 固定資產 : | (10) | 416,593 | 409,158 |
| **Current assets : 流動資產** | | | |
| Debtors 應收帳款 | | 1,119 | 908 |
| Bank deposits 銀行存款 | | 70,300 | 82,100 |
| Cash and bank balances 現金及銀行結餘 | | 3,924 | 5,353 |
| | | 75,343 | 88,361 |
| **Less : Current liabilities 減去流動負債** | | | |
| Short term borrowing 短期借款 | (11) | (27,670) | (27,670) |
| Creditors 應付帳款 | | (69,184) | (63,448) |
| Tax payable 應付稅款 | | (1,793) | (3,309) |
| Proposed dividend 擬發股息 | (8) | (4,954) | - |
| | | (103,601) | (94,427) |
| Net current liabilities 流動資產淨值 | | (28,258) | (6,066) |
| | | 388,335 | 403,092 |
| **Less : Deferred liabilities 減去遞延負債** | | | |
| Deferred taxation 遞延稅款 | (12) | (1,354) | - |
| Total net assets employed 總資產淨值 | | 386,981 | 403,092 |
| **Financed by : 財政來源** | | | |
| **Capital and reserves : 資本及儲備** | | | |
| Trading fund capital 營運基金資本 | (13) | 138,460 | 138,460 |
| Retained earnings 保留盈利 | (14) | 27,161 | 15,602 |
| | | 165,621 | 154,062 |
| Government loan 政府貸款 | (15) | 221,360 | 249,030 |
| | | 386,981 | 403,092 |

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第24至29頁的註釋本為此賬項的一部分

## COMPANIES REGISTRY TRADING FUND CASH FLOW STATEMENT
## 公司註冊處營運基金現金流量表



| | Notes 註釋 | Year ended 31 March 1995 截至1995年3月31日止年度 $000 | 8 months ended 31 March 1994 截至1994年3月31日止的8個月 $000 |
|---|---|---|---|
| **Operating activities 營運項目** | | | |
| Operating profit 營作盈利 | | 35,669 | 29,429 |
| Depreciation and amortisation 折舊及攤銷 | | 8,542 | 8,623 |
| Loss on disposal of fixed assets 售賣固定資產的虧損 | | - | 8 |
| Increase/(Decrease) in creditors 應付帳款的增加／(減少) | | (1,009) | 51,085 |
| (Increase)/Decrease in debtors 應收帳款的(增加)／減少 | | (179) | (783) |
| Net cash inflow 現金流入淨額 | | 43,023 | 88,362 |
| **Return on investments and servicing of finance 投資收入及財務支出** | | | |
| Interest received 利息收入 | | 4,138 | 1,340 |
| Interest paid 利息支出 | | (18,490) | - |
| Taxation paid 稅款支出 | | (3,349) | - |
| Net cash inflow/(outflow) 現金流入／(流出)淨額 | | (17,701) | 1,340 |
| **Capital expenditure/receipts 資本開支／收入** | | | |
| Acquisition of fixed assets 購入固定資產 | | (10,881) | (2,252) |
| Disposal of fixed assets 售賣固定資產 | | - | 3 |
| Loan repayment 償還貸款 | | (27,670) | - |
| Net cash outflow 現金流出淨額 | | (38,551) | (2,249) |
| Increase/(decrease) in cash and cash equivalents 現金及等同現金結存增加／(減少) | | (13,229) | 87,453 |
| Cash and cash equivalents at beginning of period 現金及等同現金期初結存 | | 87,453 | - |
| Cash and cash equivalents at end of period 現金及等同現金期末結存 | (16) | 74,224 | 87,453 |

The notes on pages 24 to 29 form part of these accounts.
第24至29頁的註釋本為此帳目的一部分

## 1. Status of the Companies Registry Trading Fund

The Companies Registry Trading Fund was established on 1 August 1993 under the Legislative Council Resolution passed on 30 June 1993 pursuant to Sections 3, 4 and 6 of the Trading Funds Ordinance.

## 1. 公司註冊處營運基金的地位

立法局在1993年6月30日根據營運基金條例第3、4及6條通過決議，在1993年8月1日設立公司註冊處營運基金。

## 2. Accounting policies

(a) Basis of accounting

The accounts have been prepared in accordance with generally accepted accounting principles.

(b) Fixed assets

Fixed assets appropriated to the Companies Registry Trading Fund on 1 August 1993 are stated at the value contained in the Resolution of the Legislative Council for setting up the Companies Registry Trading Fund. Fixed assets acquired since 1 August 1993 are capitalised at the actual expenditure of acquisition and installation.

(c) Depreciation and amortisation

i. Depreciation is provided on a straight-line basis calculated to write off the cost of assets less residual value over their estimated useful lives. The annual rates of depreciation used are-

| | |
|---|---|
| Building | 3.3% |
| Computer hardware and software | 20.0% |
| Furniture and Fittings | 20.0% |
| Office and Specialist Equipment | 20.0% |
| Office Car | 20.0% |

ii. No depreciation is provided in respect of land and capital projects in progress.

iii. System development and data conversion costs for computer systems are amortised over a period of 5 years from the month they are commissioned into service.

(d) Deferred taxation

Deferred taxation is provided on timing differences, using the liability method, between the accounting and tax treatment of income and expenditure. Provision is made for deferred tax only to the extent that it is probable that an actual liability will crystallise in the foreseeable future.

## 2. 會計政策

(a) 會計基準

本帳目是根據公認會計原則編備。

(b) 固定資產

1993年8月1日由政府撥歸公司註冊處營運基金的固定資產是按立法局所通過的設立營運基金決議中所列的估值入帳。從1993年8月1日起新購的固定資產則按當時用於購買及裝置設備的實際直接開支入帳。

(c) 折舊及攤銷

i. 折舊是依直線折舊法按資產原值減去其在最終使用期末的剩餘值，在預計資產可使用年期內逐年分期定額註銷。折舊年率為：

| | |
|---|---|
| 建築物 | 3.3% |
| 電腦硬件及軟件 | 20.0% |
| 傢具及裝置 | 20.0% |
| 辦公室及特殊器材 | 20.0% |
| 部門自用車輛 | 20.0% |

ii. 土地及正在進行中的資本性設備，因並無折舊。

iii. 電腦系統的發展及數據轉換成本是從使用月開始分5年攤銷。

(d) 遞延稅款

遞延稅款乃採用負債法基於在會計上和稅務評估上對於處理收入和開支上所有的時差而計算。此款項僅包括在可見將來會實現的真實負債。

## 3. Turnover 3. 營業額

| | Year ended 31 March 1995 截至1995年3月31日止年度 $000 | 8 months ended 31 March 1994 截至1994年3月31日止的8個月 $000 |
|---|---|---|
| Charges registration fees 抵押文件登記費 | 8,587 | 5,696 |
| Incorporation fees 公司註冊成立費 | 52,752 | 34,723 |
| Annual registration fees 年報表登記費 | 62,454 | 34,045 |
| Searches and copying fees 查冊及影印收費 | 39,441 | 23,803 |
| Other fees 其他費用 | 6,400 | 4,003 |
| Services to government departments 向政府部門提供服務的收費 | 6,543 | 4,215 |
| | 176,177 | 106,485 |

## 4. Operating costs 4. 運作成本

| | Year ended 31 March 1995 截至1995年3月31日止年度 $000 | 8 months ended 31 March 1994 截至1994年3月31日止的8個月 $000 |
|---|---|---|
| Staff costs 員工費用 | 102,914 | 58,871 |
| General operating expenses 一般運作開支 | 22,331 | 7,069 |
| Computer expenses 電腦開支 | 1,941 | 556 |
| Central administration overhead 中央行政開援費用 | 4,483 | 1,514 |
| Depreciation and amortisation 折舊及攤銷 | 8,542 | 8,623 |
| Loss on disposal of fixed assets 售賣固定資產的虧損 | - | 8 |
| Auditor's remuneration 核數師酬金 | 297 | 415 |
| | 140,508 | 77,056 |

## 5. Other income 5. 其他收入

| | Year ended 31 March 1995 截至1995年3月31日止年度 $000 | 8 months ended 31 March 1994 截至1994年3月31日止的8個月 $000 |
|---|---|---|
| Interest from bank deposits 銀行存款利息 | 4,170 | 1,464 |

## 6. Intgrest expenses / 6. 利息支出

| | Year ended 31 March 1995 截至1995年3月31日止年度 $000 | 8 months ended 31 March 1994 截至1994年3月31日止的8個月 $000 |
|---|---|---|
| Interest on 利息支出包括 | | |
| loan repayable within one year 應於一年內償還的貸款 | 2,816 | 1,199 |
| loan repayable after one year 應於一年後償還的貸款 | 17,324 | 10,783 |
| | 20,140 | 11,982 |

## 7. Taxation / 7. 稅款

Taxation includes the total of:

(a) the notional profits tax liability of the trading fund ascertained based on the prevailing provisions in the Inland Revenue Ordinance in respect of the year payable to the Government; and

(b) an amount representing deferred taxation.

稅款包括：

(a) 按現行稅務條例計算貿易基金在該年度內應付給政府的名義利得稅款負債及

(b) 遞延稅款

| | Year ended 31 March 1995 截至1995年3月31日止年度 $000 | *8 months ended 31 March 1994 *截至1994年3月31日止的8個月 $000 |
|---|---|---|
| Notional profits tax 名義利得稅 | 2,962 | 2,179 |
| Deferred taxation 遞延稅款 | | |
| Provision for the timing difference 因時間差異所作的準備 | 288 | 1,130 |
| Adjustment due to a change of profits tax rate 因利得稅率改變所作調整 (1995 : 16.5% ; 1994 : 17.5%) | (64) | - |
| | 224 | 1,130 |
| | 3,186 | 3,309 |

* Figures relating to the previous period have been adjusted for comparative purposes.
* 過期數字曾經調整以供比較

## 8. Dividend / 8. 股息

Dividend of $4,954,000 being 30% of the profit after taxation is proposed for the year ended 31 March 1995. (1994 : NIL)

本處擬把百分之三十的稅後盈利4954萬元作股息派發。(1994 : 無)

9. Rate of return on fixed assets

This is calculated as the percentage of operating profit and interest income after taxation to Average Net Fixed Assets (ANFA). The Companies Registry Trading Fund is expected to meet in due course a target return of 10% per annum on ANFA as determined by the Financial Secretary.

9. 固定資產回報率

這是經作盈利加上利息收入並扣除稅款後相對於固定資產平均淨值的百分率。公司註冊處營運基金每年目標回報率是按可達到固定資產平均淨值的百分之十，此數字由財政司所決定。

10. Fixed assets

10. 固定資產

| | Land & Building 土地及樓宇 | Computer System 電腦系統 | Furniture & Fittings 傢具及裝置 | Office & Specialist Equipment 辦公室及特殊器材 | Office Car 辦公自用車輛 | Total 總值 |
|---|---|---|---|---|---|---|
| | $000 | $000 | $000 | $000 | $000 | $000 |
| **Cost or valuation 成本或估值** | | | | | | |
| At 1 April 1994 在1994年4月1日 | 400,000 | 11,228 | 2,000 | 706 | 130 | 414,064 |
| Additions 年內增加 | - | 8,700 | 7,012 | 265 | - | 15,977 |
| At 31 March 1995 在1995年3月31日 | 400,000 | 19,928 | 9,012 | 971 | 130 | 430,041 |
| **Aggregate depreciation/amortisation 累計折舊／攤銷** | | | | | | |
| At 1 April 1994 在1994年4月1日 | 2,963 | 1,471 | 267 | 188 | 17 | 4,906 |
| Charge for the year 年內費用 | 4,444 | 2,897 | 860 | 315 | 26 | 8,542 |
| At 31 March 1995 在1995年3月31日 | 7,407 | 4,368 | 1,127 | 503 | 43 | 13,448 |
| **Net Book Value 帳面淨值** | | | | | | |
| At 1 April 1994 在1994年4月1日 | 397,037 | 9,757 | 1,733 | 518 | 113 | 409,158 |
| At 31 March 1995 在1995年3月31日 | 392,593 | 15,560 | 7,885 | 468 | 87 | 416,593 |

## 11. Short term borrowing 11. 短期借款

| | 1995 | 1994 |
|---|---|---|
| | $000 | $000 |
| Government loan repayable within one year as at 31 March 在3月31日一年內應付政府貸款 (see also note 15) (請亦參閱註釋15) | 27,670 | 27,670 |

## 12. Deferred taxation 12. 遞延稅款

| | $000 |
|---|---|
| At 1 April 1994 在1994年4月1日 | - |
| Deferred taxation for 1993/94 1993/94年度遞延稅款 | 1,130 |
| Deferred taxation for 1994/95 1994/95年度遞延稅款 | 224 |
| At 31 March 1995 在1995年3月31日 | 1,354 |

## 13. Trading fund capital 13. 營運基金資本

This represents Government's investment in the Companies Registry Trading Fund.

此為政府對公司註冊處營運基金的投資

| | $000 |
|---|---|
| At 1 April 1994 在1994年4月1日 | 138,460 |
| At 31 March 1995 在1995年3月31日 | 138,460 |

## 14. Retained earnings 14. 保留盈利

| | $000 |
|---|---|
| At 1 April 1994 在1994年4月1日 | 15,602 |
| Profit for the year 年內盈利 | 16,513 |
| Less : Proposed dividend 減去：擬發股息 | (4,954) |
| At 31 March 1995 在1995年3月31日 | 27,161 |

## 15. Government loan

The loan of $276,700,000 from the Capital Investment Fund was made in accordance with the resolution passed by the Legislative Council on 30 June 1993 to finance part of the net assets valued at $415,160,000 appropriated to the Companies Registry Trading Fund with effect from 1 August 1993. The loan is repayable in ten equal annual instalments of $27,670,000 starting from 1 August 1994. The instalment due to be payable on 1 August 1995 is shown as short term borrowing. The balance of $221,360,000 shown under Government Loan represents the balance of the loan after repayment of the second instalment. The loan bears interest at a rate equal to the average of the best lending rate quoted by the continuing members of the Committee of The Hong Kong Association of Banks.

## 15. 政府貸款

根據立法局1993年6月30日所通過的決議，在經歸賬基金的資產淨值4.1516億元中，2.767億元為資本投資基金向商業基金的貸款，貸款將由1994年8月1日起分十期按年等額償還，每年還款2,767萬元，到期於1995年8月1日應支付的還款，已在標目內列作短期借款，故本項目下所示的結餘2.2136億元為在繳付第二期還款後的貸款餘額。並於貸款利息，息率為香港銀行公會委員會的首席會員所公佈的最優惠貸款利率的平均息率。

## 16. Analysis of the balances of cash and cash equivalents at end of year

## 16. 年底現金結餘及等同現金結餘分析

| | 1995 | 1994 |
|---|---|---|
| | $000 | $000 |
| Cash and bank balances 現金及銀行結餘 | 3,924 | 5,353 |
| Bank deposits 銀行存款 | 70,300 | 82,100 |
| | 74,224 | 87,453 |

## 17. Capital commitments

At 31 March, the Companies Registry Trading Fund had capital commitments, as stated below:-

## 17. 資本承擔

截至3月31日止，公司註冊處營運基金有下列資本承擔

| | 1995 | 1994 |
|---|---|---|
| | $000 | $000 |
| Contracted for 已簽約 | 5,522 | 8,538 |
| Not contracted for 未簽約 | - | - |
| | 5,522 | 8,538 |

## Chapter 21

## The Official Receiver's Report for 1994/95

21.1 At the 109th meeting of the Standing Committee, the Annual Report of the Official Receiver's Office for 1994/95 was tabled for information and discussion.

21.2 Members were advised by the Official Receiver that in the year under review :

- the 16% increase in insolvencies for 1994/95 over the previous year had been sustained during the current year;

- there had been a significant increase in the numbers of personal bankruptcies;

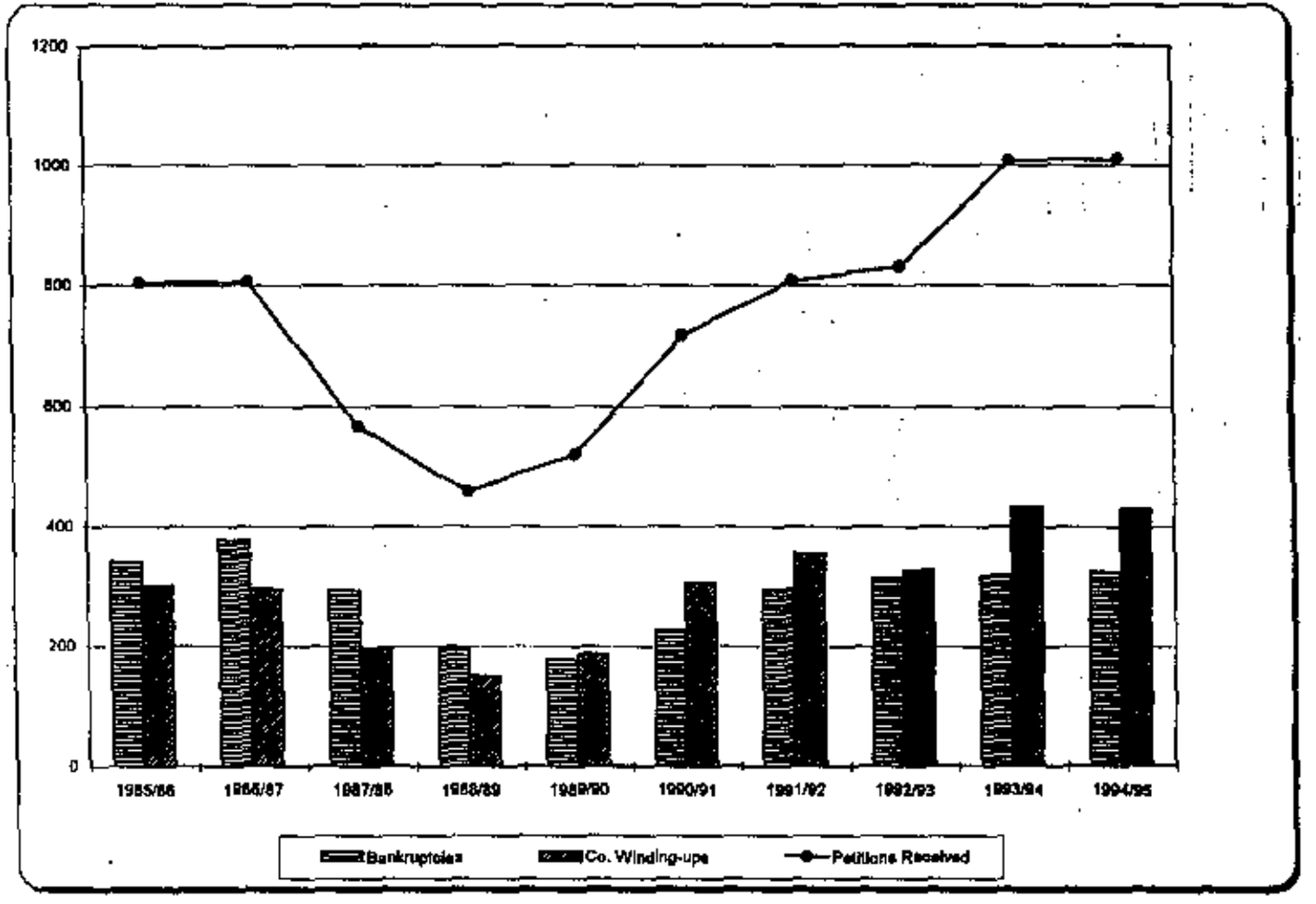
- following the enactment of Part IVA of the Companies Ordinance in 1994 - disqualification of directors - 30 disqualification orders against unfit directors had been made by the courts, with another 45 applications pending;

- a liaison trip by the Official Receiver's Office had been undertaken to the PRC which had resulted in a useful exchange of information. Further meetings were planned for the future;

21.3 At Appendix 1 is a breakdown of the numbers of receiving orders and winding up orders made between 1985 and 1995 and at Appendix 2 is an analysis of the prosecutions undertaken by the Official Receiver's Office during 1994-95.

Number of Cases Where Receiving Orders/Winding-up Orders Were Made

| | *1985/86* | *1986/87* | *1987/88* | *1988/89* | *1989/90* | *1990/91* | *1991/92* | *1992/93* | *1993/94* | *1994/95* |
|---|---|---|---|---|---|---|---|---|---|---|
| Bankruptcies | 340 | 378 | 292 | 194 | 178 | 226 | 294 | 313 | 318 | 325 |
| Co. Winding-ups | 300 | 295 | 196 | 151 | 187 | 306 | 355 | 327 | 433 | 429 |
| Total | 640 | 673 | 488 | 345 | 365 | 532 | 649 | 640 | 751 | 754 |
| Petitions Received | 805 | 807 | 667 | 469 | 521 | 717 | 810 | 832 | 1008 | 1011 |



## Analysis of Prosecutions for 1994-95

| Cap | Section | Summons | | | | Conviction | Success Rate | Amount of Fines Imposed |
|---|---|---|---|---|---|---|---|---|
| | | b/f | Issued | Pending | Heard by Magistracy | | | |
| 32 | 190 | 21 | 36 | 25 | 32 | 21 | 66% | $143,200 |
| 32 | 121/274 | 21 | 68 | 37 | 52 | 41 | 79% | $390,300 |
| 32 | 156(1) | 1 | 0 | 0 | 1 | 1 | 100% | $3,000 |
| 6 | 131 | 0 | 2 | 0 | 2 | 2 | 100% | $14,000 |
| TOTAL | | 43 | 106 | 62 | 87 | 65 | 75% | $550,500 |

Companies Ordinance

Section 190 : Failure of directors or officers to submit statement of affairs of company in time.

Section 121/274 : Failure of directors/officers to keep proper books of account.

Section 156(1) : Undischarged bankrupts acting as directors.

Bankruptcy Ordinance

Section 131 : Undischarged bankrupts trading or obtaining credit without disclosing previous bankruptcy.

## Chapter 22

## The Auditors' Report - Section 141 of the Companies Ordinance

### 22. Summary of Recommendations

22.1 At the 110th meeting of the Standing Committee, members agreed to adjourn further discussion and to await the outcome of the deliberations of the LegCo Panel on Financial Services on the vexed question of giving auditors of listed companies statutory immunity when they reported fraud or other misconduct to the regulatory authorities.

### Background

22.2 Under Section 141 of the Companies Ordinance, the auditors of a company are required to report to members on the accounts laid before the company in general meeting. The auditor is obliged to carry out such investigation as will enable him to form a view as to whether, firstly, proper books of account have been kept and , secondly, as to whether the company's balance sheet and profit and loss account agree with the Books of Accounts and returns. If not, then the auditor is obliged to state that fact in his report. There is no statutory obligation under Section 141 for the auditors to comment on the directors' report.

22.3 The Hong Kong Society of Accountants had proposed that Section 141 should be amended to enable the auditors to consider whether the information given in the directors' report was consistent with the annual accounts. In support of its proposal the Society had stated :

> "The scope of the statutory audit is restricted to the financial statements of a company consisting the balance sheet, profits and loss account and notes.
>
> However, financial information contained in a company's annual report is not confined to these statements encompassed by the auditors' report. Other financial information may be included in the statutory directors' report or in other unaudited statements such as a chairman's statement, a report on operations or a summary of past results.
>
> The auditor has no statutory responsibility in respect of these other financial information. This puts the auditor in a dilemma where the unaudited financial information issued with the audited financial information are found by the auditor to be inconsistent with the audited financial statements.
>
> For the purpose of discharging his responsibility, he may wish to refer to the inconsistent information in

his audit report. However, the qualified privilege (i.e. the defence to an action for defamation) which an audit report normally enjoys may not extend to comments on items of other financial information which appear to be inconsistent with the audited financial statements. Similarly, no qualified privilege may attach to statements made by him on such matters at a general meeting pursuant to his right under Sections 141(7) of the Companies Ordinance.

We note that the UK 1985 Companies Act has introduced an additional requirement for the auditor to consider where the information given in the directors' report for the financial year to which the annual accounts are prepared is consistent with those accounts; and if they are of opinion that it is not they shall state that fact in their report. The same provisions should be adopted for Hong Kong."

22.4 Many kinds of privileges are recognised in law. With regard to defamation, the law recognises two kinds of privilege, absolute and qualified. The doctrine of absolute privilege, which attaches to e.g. debates in LegCo and official communications arising therefrom and communications in the course of the administration of justice, wholly protects the maker from liability for

defamation. The doctrine of qualified privilege attaches to communications made by persons having a duty to make them to other persons having an interest in receiving them. It protects the maker provided the communication was not made maliciously or spitefully.

22.5 During discussions certain members believed that no change to the legislation was necessary. By and large the information contained in the directors' report was a replication of the information set out elsewhere. It was extremely rare for there to be inconsistencies and it was inappropriate for the auditor when examining the Directors Statements to comment on the content when it was clearly the directors duty to promote the business of the company. Other members felt that the proposal was enabling and should be adopted. If inconsistencies were discovered, they should be free to comment and be protected by the doctrine of qualified privilege.

22.6 The Chairman directed that further debate should be deferred until after the LegCo Panel on Financial Services, which had been asked to consider whether or not statutory immunity should be extended to auditors of listed companies when they reported fraud, had finalised its deliberations.

## Chapter 23

## Overall Review of the Companies Ordinance

23.1 In his budget speech of 1994, the Financial Secretary announced :

> "We have tried in the past to respond to developments in the corporate world through piecemeal amendment of the Companies Ordinance. I believe we have reached a stage when a thorough review has become essential. We now need an ordinance for the 21st century. I have therefore asked the Secretary for Financial Services to take this forward."

The terms of reference and the reasons for the review were set out in Chapter 10 of last year's report of the Standing Committee.

23.2 Mr. Ermanno Pascutto was subsequently appointed to undertake the review and at the 105th meeting, the 'Inception Report' was tabled for discussion. The purpose of the report was to : .....

> "provide a starting point for the Review, to give it shape and direction. The report will outline the objectives and scope of the Review, the proposed

methodology for conducting the Review, areas of substantive investigation and media and public consultations issues."

23.3 During discussions members opined that :

- it was necessary for Mr. Pascutto to closely liaise with the Standing Committee which should have a major input into the work of the review;

- the cultural aspirations and views of the business community in Hong Kong needed to be addressed by the Review;

23.4 The overall review has since been an agenda item at the 106th, 108th and 109th meetings of the Standing Committee.

23.5 **106th Meeting**

A progress report was tabled for discussion. The 'Inception Report' on the modus operandi' of the Review had been submitted to Government, letters requesting comments had been submitted to an extensive list of business, professional and commercial organisations and background reports dealing with an overview of the current legislation and its legislative history, and a comparative survey of the companies law regime in selected jurisdictions had been undertaken.

23.6 **108th Meeting**

Draft papers entitled "Overview of the Hong Kong Companies Ordinance" and "A Comparative Survey" were tabled for discussion. In addition, a written summary of the written responses from the various business, commercial and professional bodies, as well as from a large number of individuals, on the 'overall review' was circulated to members for consideration. The Comparative Survey which included an examination of the Law Reform process in Canada and New Zealand provided a useful pointer for the future direction for reforming the Hong Kong Companies legislation. Those jurisdictions had enacted entirely new companies statutes (instead of trying to amend piecemeal the existing legislation) which then ran in conjunction with the existing legislation for a transitional period of three years or so. This avoided the huge logistical problems of having to amend the existing legislation. Existing companies were given a three year period to familiarise themselves with the new legislation at the end of which the old legislation would be spent and of no further effect. In North America, prospective incorporators had numerous jurisdictions to choose from when deciding where to incorporate e.g. a New York business could choose to incorporate in Delaware rather than New York. Certain members believed however

that the concept of federalism was well established in those countries. Hong Kong was quite different.

23.7 **110th Meeting**

Two papers were tabled for discussion. The first which addressed the identification of core company law set out the aims and objectives of companies legislation viz:

- it should primarily be enabling and not regulatory;

- it should be written in simple and plain language;

- it should provide a simple, flexible and cost effective regime within which companies could operate;

- it should clearly spell out the rights, duties and powers of directors and shareholders;

- it should concentrate on core company law excluding the regulation of listed companies and financial institutions;

- it should not be used to impose social or economic policy;

With regard to securities legislation, it should be regulated by the jurisdiction where the listing or public offering was effected. Hong Kong should regulate all companies that list on the Hong Kong Stock Exchange through its Securities Legislation. As fewer than 40% of the listed companies were now locally incorporated, it was proposed that the prospectus and other provisions dealing with public offerings should be removed from the Companies Ordinance and re-enacted in an updated Securities Ordinance. The paper also recommended a new statutory disclosure regime for listed companies and that it should be an offence to mislead the 'Public' or to omit material information in the following documents:

- annual and semi-annual accounts;

- shareholders circulars;

- announcement of material/price sensitive information;

- takeover and share repurchase circulars;

A possible alternative to the proposed statutory disclosure regime is to grant statutory backing to the listing rules of the Stock Exchange.

23.8 The second paper tabled was a briefing paper on corporate formalities. Its recommendations were to be considered by the working party set up to examine its contents. This part was considered to be the 'heart' of the review and that its recommendations, if accepted by the Administration and LegCo, would provide the structure for a new ordinance.

23.9 A number of members queried the need for change. The business community had a thorough understanding of the present legal infrastructure and it was undesirable at this juncture in Hong Kong's history for there to be radical change. Other members pointed out that the decision to proceed with the review had been taken because a number of problems with the existing legislation had been identified. As a consequence the Administration had decided to proceed with the review and had approached LegCo to seek the necessary funding. Members agreed to keep the subject under close scrutiny.