

Standing Committee on Company Law Reform

The Thirty-First Annual Report

2014 / 2015

Standing Committee on Company Law Reform (SCCLR)

Thirty-First Annual Report

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PREFACE

(i)

Terms of Reference of the Standing Committee on Company Law Reform

- (1) To advise the Financial Secretary on amendments to the Companies Ordinance and the Companies (Winding Up and Miscellaneous Provisions) Ordinance as and when experience shows them to be necessary.
- (2) To report annually to the Financial Secretary on those amendments to the Companies Ordinance and the Companies (Winding Up and Miscellaneous Provisions) 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 and Futures Ordinance on matters relating to corporate governance and shareholders' protection.

(ii)

Membership of the Standing Committee for 2014/2015

<u>Chairman</u>	:	Mr Anderson CHOW Ka-ming, S.C.	(up to 27.06.2014)
		Mr John SCOTT, S.C.	(from 01.10.2014)
<u>Members</u>	:	Mr Bruno ARBOIT	(from 01.02.2015)
		Mr Stephen BIRKETT	
		Ms Bonnie CHAN Yiting	(from 01.02.2015)
		Mr Rock CHEN Chung-nin, B.B.S., J.P.	
		Mr CHEW Fook-aun	(up to 31.01.2015)
		Professor David DONALD	
		Professor GOO Say-hak	(up to 31.01.2015)
		Ms Roxanne ISMAIL, S.C.	
		Mr David KIDD	
		Mr Johnson KONG Chi-how	(up to 31.01.2015)
		Mr Rainier LAM Hok-chung	
		Professor John LOWRY	(from 01.02.2015)

Dr Lewis LUK Tei, J.P.
Mrs Catherine MORLEY (up to 31.01.2015)
Mr Kenneth NG Sing-yip
Mr Keith POGSON (from 01.02.2015)
Dr Kelvin WONG Tin-yau, J.P.
Ms Benita YU Ka-po
Ms Wendy YUNG Wen-yee

Ex-Officio

Ms Ada CHUNG, J.P.

Members :

Ms Teresa WONG, J.P.
Official Receiver

Mr Patrick HO, J.P.
Deputy Secretary for Financial Services and the
Treasury (Financial Services)

Professor Edward L G TYLER (up to 31.12.2014)
Senior Assistant Law Officer (Civil Law)
Department of Justice

Mr Stefan LO (from 01.01.2015)
Senior Assistant Law Officer (Civil Law) (Ag)
Department of Justice

Mr Andrew YOUNG
Chief Counsel, Legal Services Division
Securities and Futures Commission

Mr David GRAHAM
Chief Regulatory Officer and Head of Listing
Hong Kong Exchanges and Clearing Limited

Mr Stefan GANNON, J.P.
General Counsel
Hong Kong Monetary Authority

Secretary : Mrs Karen HO

(iii)

Meetings held during 2014/2015

223rd Meeting	-	25.06.2014
224th Meeting	-	12.11.2014

(iv)

Information Papers circulated during 2014/2015

Section 408 of the New Companies Ordinance	-	17.06.2014
Sponsor Regulation	-	22.08.2014
The Committee's Discussion on Shares with Different Voting Rights in 1987	-	28.10.2014

(v)

Discussion Papers circulated during 2014/2015

Detailed Proposals on a New Statutory Corporate Rescue Procedure and Insolvent Trading Provisions	-	16.06.2014
Consultation Conclusions on Corporate Insolvency Law Improvement Exercise	-	16.06.2014
Concept Paper on Weighted Voting Rights	-	Aug 2014

REPORT

The Standing Committee on Company Law Reform (“SCCLR”) was formed in 1984. It advises the Financial Secretary (“FS”) on amendments to the Companies Ordinance (Chapter 622) (“CO”) and the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32) (“CWUMPO”), and to the Securities and Futures Ordinance (Chapter 571) on matters relating to corporate governance and shareholders’ protection. The SCCLR reports annually to the FS through the Secretary for Financial Services and the Treasury on amendments that are under consideration.

2. The SCCLR received three information papers from the Government during the year on section 408 of the CO, sponsor regulation and the Committee’s previous discussions on shares with different voting rights in 1987 (please also refer to paragraph 13 of this report).
3. From 1 April 2014 to 31 March 2015, the SCCLR held two meetings and considered three discussion papers.

Discussion Paper on “Detailed Proposals on a New Statutory Corporate Rescue Procedure and Insolvent Trading Provisions”

Background

4. At the 223rd meeting held on 25 June 2014, representatives from the Financial Services and the Treasury Bureau (“FSTB”) and the Official Receiver’s Office (“ORO”) presented detailed proposals on a new statutory corporate rescue procedure and insolvent trading provisions.

5. As background, the SCCLR was informed that following the consultation exercise in 2009-10 on the conceptual framework of and some specific issues¹ concerning the proposed statutory corporate rescue procedure and the insolvent trading

¹ Please see Chapter 3 of the SCCLR Annual Report for the year 2010/11 which is available at the Companies Registry’s website www.cr.gov.hk. The consultation paper “Review of Corporate Rescue Procedure Legislative Proposals” issued in October 2009 and the consultation conclusions issued in July 2010 are available at FSTB’s website www.fstb.gov.hk.

provisions, the Government had developed a package of detailed proposals which were announced in May 2014. The Government then briefed members on the detailed proposals.

Discussion Outcomes

6. Members generally supported the detailed proposals.

7. With regard to the proposed requirement that a company must obtain the prior consent of its major secured creditor before initiating the statutory corporate rescue procedure, some members suggested if it would be appropriate to impose a requirement on the company to give advance notice of initiation of the procedure to its major secured creditor instead. The Government noted that the requirement would in effect give a window (i.e. the period of the advance notification) for the major secured creditor to take action to enforce his charge if he so decided, and thus could afford the major secured creditor similar protection as with a previous proposal of the major secured creditor's power to veto the initiation process of corporate rescue procedure. This could alleviate concerns that with the previous proposal, the major secured creditor would only have very limited time to consider and determine whether to exercise his right to veto or not. In addition, while noting that the Government would consider further the initiation arrangements in case the company concerned did not have any major secured creditor, members were generally against the idea of requiring the consent of all secured creditors before the company could initiate the procedure because there would be practicability issues in obtaining secured creditors' consent and this requirement would likely cause delay to the process.

8. With regard to the scope of the statutory defence for a director's liability for the company's insolvent trading, members noted the Government's proposal that it would be a statutory defence if the director had taken all reasonable steps to prevent the company from incurring the debt in question or if the incurring of the debt was part and parcel of the steps taken by the director to initiate the corporate rescue procedure. Some members considered that the proposed statutory defence was sufficient to strike a proper balance, while some other members suggested that the statutory defence could be extended to cover the situation where the debt in question was incurred in the course of an "arrangement or compromise" under the CO or an informal workout when the directors were trying to salvage the company. Members noted that the Government would take into account the views of the Committee and other stakeholders when preparing the draft legislation.

Consultation Conclusions on Corporate Insolvency Law Improvement Exercise

Background

9. At the 223rd meeting held on 25 June 2014, representatives from the FSTB and the ORO presented the discussion paper “Consultation Conclusions on Corporate Insolvency Law Improvement Exercise”.

10. Members were briefed on the outcome of the public consultation on the corporate insolvency law improvement exercise and the Government’s responses to respondents’ comments². Members were informed that the legislative proposals to improve the corporate insolvency and winding-up provisions in the CWUMPO were supported by a majority of respondents to the public consultation.

Discussion Outcomes

11. On the consultation proposal to clarify the duties and powers of different types of provisional liquidators appointed under section 194 of the CWUMPO³, members noted that it was originally proposed to designate all “provisional liquidators” who took office upon and after the making of a winding-up order under different sub-sections of section 194 of the CWUMPO as “liquidators”, but having regard to respondents’ comments, the Government had modified the proposal by introducing specific provisions to clarify the powers, duties, remunerations, etc. of the different types of provisional liquidators under section 194. Under the modified proposal, there would be two types of provisional liquidators having different roles but both would carry the

² Please see the SCCLR Annual Report for the year 2013/14 which is available at the Companies Registry’s website www.cr.gov.hk. The consultation document and the consultation conclusions together with a compendium of the respondents’ submissions and the responses by the Government are available at FSTB’s website www.fsb.gov.hk.

³ Under section 194 of the CWUMPO, the following office-holders who take office upon and after the making of a winding-up order are all called the “provisional liquidator”—

- (a) except where a person other than the Official Receiver acts as a provisional liquidator under section 194(1)(aa), the Official Receiver by virtue of his office becomes the provisional liquidator under section 194(1)(a) upon the making of the winding-up order;
- (b) where a person other than the Official Receiver has been appointed as a provisional liquidator by the court under section 193 of the CWUMPO before the making of the winding-up order, this person continues to act as the provisional liquidator by virtue of section 194(1)(aa); and
- (c) the Official Receiver as the provisional liquidator under (a) may appoint one or more persons as provisional liquidator under section 194(1A) in place of himself.

same title as the “provisional liquidators” (i.e. provisional liquidators appointed under section 193 of CWUMPO and provisional liquidators who take office under section 194 of CWUMPO). Some members were concerned that there would be confusion and suggested that different terms should be used for different types of office-holders. The Government clarified that as the key consideration was to make clear the position of powers and duties of the different types of provisional liquidators in the current winding-up regime, the modified proposal was considered most appropriate as further changes in the nomenclature under the modified proposal could be confusing. Besides, the modified proposal was actually suggested by many respondents in the consultation.

12. On the proposal that liquidators should not be absolved from liabilities under section 276⁴ of the CWUMPO notwithstanding their release by the court, a member expressed concern that the proposal might be unfair to liquidators who had duly completed their work. The Government explained that a measure had been introduced in the proposal to minimise the risk of frivolous litigation i.e. where the court had already granted a release to the liquidator, the power to make application under section 276 would only be exercisable with the leave of the court.

Concept Paper on Weighted Voting Rights

Background

13. At the 224th meeting held on 12 November 2014, representatives from the Hong Kong Exchanges and Clearing Limited (“HKEx”) briefed members on the contents of the Concept Paper issued by the Stock Exchange of Hong Kong (“SEHK”)⁵ in August 2014 and sought members’ views on the issues raised in the Concept Paper. To facilitate discussion, the Secretary to the SCCLR had also circulated an information

⁴ Section 276 of the CWUMPO provides that if, in the course of winding up of a company, it appears that any past or present liquidator of the company has become liable or accountable for any money or property of the company, or has been guilty of any misfeasance or breach of duty in relation to the company, the court may make orders to compel such person to repay or restore the money or property or to contribute such sum to the assets of the company by way of compensation in respect of such misapplication, retainer, misfeasance or breach of trust as the court thinks fit.

⁵ The Concept Paper is available at HKEx’s website www.hkex.com.hk.

paper summarising the Committee’s discussions on the issues relating to shares with different voting rights in 1987 for members’ reference⁶.

Discussion Outcomes

14. On the question of whether the SEHK should permit weighted voting rights (“WVR”) structures for listed companies, some members supported the notion in principle as they considered that being an international financial centre, Hong Kong’s financial system should evolve with the changing global landscape to maintain our competitiveness. On the other hand, some members had reservations as they considered that WVR structures would result in entrenchment of rights, taking control and extension of that control for an indefinite period of time which would invariably affect minority shareholders’ interests and hence would not be suitable for listed companies.

15. Members’ views were sought on the issue of whether WVR structures, if permissible, should be open to all listed companies, or whether they should be limited to new listing applicants or listed companies from particular industries e.g. information technology companies or innovative companies. Members’ views were diverse on the question. Some members considered that WVR structures should be limited to new listing applicants only as shareholders of existing listed companies had made their investment decisions on the basis of “one share one vote” structure. Some members raised the issue of whether an existing listed company could circumvent this restriction by way of restructuring its business or “spin-off”, and some other members also expressed reservations on the idea of limiting its application to certain categories of listed companies only as it would be difficult to differentiate or define the different types of companies.

16. Members generally agreed that if WVR structures were to be permitted for listed companies, it would be quintessential to put in place specific measures to ensure a high standard of corporate governance in such listed companies with the ultimate aim of

⁶ In gist, the SCCLR was asked in 1987 to advise whether or not the ability of companies to issue shares with voting rights disproportionate to their nominal value was in the general interest of shareholders, and in the public interest, and if not, to identify whether any changes to the legislative framework were desirable. The Committee’s views were documented in the “Third Interim Report of the Standing Committee on Company Law Reform: B Share” attached to the SCCLR Annual Report for the year 1987, which is available at the Companies Registry website www.cr.gov.hk.

enhancing the protection of minority shareholders' interest. Additional safeguards, such as limitation on the entrenchment of rights and more extensive scrutiny of connected party transactions, should also be considered in such a scenario. Some members also suggested that listed companies with WVR structures, if permitted, should be traded on a separate board and subject to separate rules.

17. Members noted that their views and comments would be reflected to the SEHK for reference. Depending on the public responses to the Concept Paper, the SEHK might conduct further consultation on detailed proposals and the SCCLR would be consulted again on the detailed proposals if the matter was to be pursued further⁷.

⁷ The Listing Committee of The Stock Exchange of Hong Kong Limited announced on 5 October 2015 that after considering the views of the board of the Securities and Futures Commission, it would not proceed with its draft proposal on WVR at this time.