

CHAPTER 3

DIRECTORS' REMUNERATION REPORT

- 3.1 We would like to seek further views on whether the CB should require (a) all listed companies incorporated in Hong Kong, and (b) unlisted companies incorporated in Hong Kong where members holding not less than 5% of the total voting rights have so requested, to prepare separate directors' remuneration reports, before taking a final decision on the matter.

Background

- 3.2 At present, section 161 of the CO requires all companies to set out the aggregate amount of the emoluments and pensions of, and compensation paid in relation to loss of office to directors and past directors in the accounts of the company.
- 3.3 All listed companies in Hong Kong are required under the Listing Rules²⁷ to disclose in its financial statements, on a named basis, details of directors' and past directors' emoluments. Such details include the directors' fees for the financial year, their basic salaries as well as other allowances (e.g. housing allowances) and benefits in kind, contributions to pension schemes and bonuses paid for directors, etc.
- 3.4 In view of the increasing public concern over the remuneration of directors, the SCCLR has recommended during Phase II of the CGR that the level of transparency in respect of the disclosure of directors' remuneration packages should be enhanced. To this end, the SCCLR suggested that the CO should be amended to:
- (a) require listed companies to disclose individual directors' remuneration packages by name in their annual accounts; and
 - (b) require unlisted public companies or private companies incorporated in Hong Kong to disclose full details of all elements of individual directors' remuneration packages by name in their annual accounts if members holding not less than 5% of the issued share capital so request.

²⁷ See paragraph 17.07 in Chapter 17 and paragraphs 24 and 28 of Appendix 16 of the Listing Rules (Main Board).

- 3.5 To take forward SCCLR's recommendations, the Joint Government/HKICPA Working Group²⁸ ("Working Group") proposed that a separate directors' remuneration report should be prepared by all listed companies and those unlisted companies whose members have so requested, subject to the thresholds in paragraph 3.4(b).
- 3.6 The Working Group further proposed that the requirements under the CB should be similar to the requirements in Schedule 7A to the UK Companies Act 1985. The requirements are substantially re-enacted in Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 ("UK Regulations"), relevant extract from the UK Regulations is at **Appendix 2**. The requirements under the UK Regulations are detailed and prescriptive in nature. In gist, the report covers various types of benefits given to individual directors by name, including the basic salary, fees, expenses allowances, benefits in kind, pension benefits and contributions, bonuses, compensation for loss of office, share options and long-term incentive schemes. The information in relation to the directors' benefits is subject to audit and the report should be approved by the board of directors and signed on behalf of the board by a director.
- 3.7 We consulted the public in 2007 on whether the Working Group's proposal should be adopted²⁹. A majority of the respondents supported the proposal regarding the preparation of a separate directors' remuneration report while some of them highlighted the need to strike a balance between transparency and privacy. Views were, however, diverse on the details of disclosure and whether disclosure should be made by name of individual directors³⁰.

Considerations

- 3.8 In Part 9 of the draft CB, we have tentatively provided for a requirement for all listed companies incorporated in Hong Kong and unlisted companies incorporated in Hong Kong if the required number of members have so requested to prepare separate directors' remuneration reports³¹. The detailed requirements would be set out in regulations to be made by the FS

²⁸ It was established in March 2002 to undertake a comprehensive review of the accounting and auditing provisions in Part IV of the CO, which, to a large extent, were not examined in the context of the SCCLR's report on the recommendations of a consultancy report of the review of the CO published in February 2000.

²⁹ See FSTB, *Consultation Paper on Accounting and Auditing Provisions* (March 2007), paragraphs 4.9 to 4.12 (available at http://www.fstb.gov.hk/fsb/co_rewrite).

³⁰ Most respondents supported the proposal in principle. However, views on the details of disclosure were divided. Some respondents considered that all shareholders should have the right to require full disclosure of remuneration packages to directors while others suggested that the disclosure could be limited to remuneration bands rather than by name of each individual director.

³¹ See **Clauses 9.34** and **9.35** in Part 9.

after the CB is enacted. Nevertheless, we have reflected on the desirability of such an approach in consultation with the SFC and HKEx. Our concerns are two-fold.

- 3.9 First, the CO should provide for a legal framework which is applicable to both listed and unlisted companies. Additional requirements on listed companies due to their nature should be set out in the Listing Rules, or if statutory backing is considered necessary, in the SFO³². Currently, all listed companies are already required to disclose in their financial statements detailed information concerning the remuneration of individual directors and past directors under the Listing Rules³³. If regulations based on the UK Regulations are introduced under the CO, listed companies incorporated in Hong Kong would be subject to statutory and prescriptive rules while those incorporated outside Hong Kong would continue to be regulated by non-statutory Listing Rules which are more principle-based. Such a complex regulatory framework with two different sets of rules is difficult to justify, especially as the majority of listed companies are incorporated outside Hong Kong. To avoid confusion and to ensure a level-playing field, any improvements to the disclosure of the remuneration of directors of listed companies is better pursued through amendments to the Listing Rules and/or SFO.
- 3.10 Second, the requirements on directors' remuneration reports under the UK Regulations are designed primarily for listed companies and might be too onerous for unlisted companies. It would increase the compliance costs as most of the information in the directors' remuneration report has to be audited. While the mechanism for members holding not less than 5% of issued shares/voting rights to request a company to prepare such a report is intended to protect the interests of minority shareholders, it could be used as a means to impose an extra burden on the directors or management in case of shareholder disputes. The existing requirements under section 161 of the CO for accounts to include information on directors' emoluments, pensions and compensation for loss of office will be modified to include new disclosures³⁴. Such requirements will be set out in regulations to be made under **Clause 9.27** of Part 9. As the vast majority of unlisted companies in Hong Kong are SMEs and most of them are closely held, the disclosures required under the new regulations should be sufficient.

³² This may involve amending the SFO to empower the SFC to make relevant rules.

³³ HKEx has been conducting a Financial Statements Review Programme, which is a continuous programme of review of a sample of 100 financial reports of listed issuers each year. In the latest report on the programme's findings issued in June 2009, HKEx did not identify any significant non-compliance with the Listing Rules in respect of directors' remuneration disclosures.

³⁴ The additional information required to be disclosed includes the amount of money or benefits received or receivable by directors under the long term incentive schemes and share options, or by third parties in respect of directors' services; and the nature and value of any benefit in kind, or damages or settlement sum for breach of contract, made to directors for loss of office.

3.11 Subject to the public's views, we are inclined not to introduce any requirement in the CB for listed or unlisted companies incorporated in Hong Kong to prepare separate directors' remuneration reports. Any improvements to the disclosure of the remuneration of directors of listed companies may be considered under the Listing Rules and/or the SFO. We would keep under review the need for introducing any statutory disclosure requirements for listed companies in the light of local and international market experience.

Question 2

Do you agree that there is no need to impose a statutory requirement in the CB for all listed companies incorporated in Hong Kong and unlisted companies incorporated in Hong Kong where members holding not less than 5% of voting rights have so requested to prepare separate directors' remuneration reports?