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**Panel on Financial Affairs
Meeting on 4 July 2005**

**Background Brief
on rewrite of the Companies Ordinance**

Purpose

This paper sets out the background of the Administration's proposal to conduct an exercise to rewrite the Companies Ordinance (CO) (Cap. 32), and summarizes the major views and concerns expressed by members when the relevant proposal was deliberated at the meeting of the Panel on Financial Affairs (FA Panel) on 5 July 2004.

Major reviews of the CO

2. The CO is one of the largest and most complex pieces of legislation in Hong Kong and is essentially derived from the UK Companies Act which was first enacted in 1865. Since its last review in 1984, continuous efforts have been made to update the CO to keep it attuned to business needs. The Standing Committee on Company Law Reform (SCCLR) was formed in 1984 to advise on necessary amendments to the CO on a continuous basis.

3. In the budget speech for 1994, the then Financial Secretary (FS) announced the Government's intention to undertake a comprehensive review of the CO. In November 1994, the Administration appointed Mr Ermanno Pascutto to lead the review exercise and engaged consultants to undertake relevant research. "The Consultancy Report on the Review of the Hong Kong Companies Ordinance" (the Consultancy Report) was completed in March 1997. The Administration presented the major findings of the Consultancy Report to the FA Panel at the latter's meeting on 2 June 1997.

4. The Administration then conducted a public consultation exercise on the Consultancy Report. In 1999, the SCCLR undertook further study on the subjects upon which the Consultancy Report had made recommendations and the

public had given opinions during the consultation exercise. In February 2000, the SCCLR published “The Report of the Standing Committee on Company Law Reform on the Recommendations of a Consultancy Report of the Review of the Hong Kong Companies Ordinance” (the SCCLR Report) which contained 168 recommendations covering a wide range of issues. On the basis of the recommendations in the SCCLR Report, the Administration identified a total of 62 items for legislative amendments or further study. These items are divided into four phases. Phase I involves amendments to specific sections of the CO. Phases II and III involve areas for further study and consultation. Phase IV involves an overhaul of the CO. The details are in **Appendix I**. Some of the items have been included in the Companies (Amendment) Ordinance 2003 and the Companies (Amendment) Ordinance 2004, which have been implemented; and the Companies (Amendment) Bill 2004, which was passed at the Legislative Council (LegCo) meeting on 29 June 2005.

5. In 2000, the SCCLR was tasked by the then FS to conduct a comprehensive corporate governance review. The review covered virtually all the items categorized in Phase II of the SCCLR Report (as well as many other items) and was completed in early 2004.

6. There are certain parts of the CO which have not been examined in the context of the SCCLR Report. One of them is the accounting and auditing provisions in Parts II, IIA and IV of the CO. The Joint Government/Hong Kong Society of Accountants Working Group was established in March 2002 to undertake a comprehensive review of the accounting and auditing provisions.

7. The details of the major reviews of the CO conducted by the SCCLR and other relevant parties are in **Appendix I**.

Rewrite exercise of the CO

8. As provisions in the CO are closely inter-linked and amendments to any specific section could have implications for numerous other provisions in the Ordinance, it has come to a stage where piecemeal amendments to the Ordinance are no longer desirable. The Administration considers that a complete rewrite and restructuring of the CO is appropriate to take account of the latest international practices, to upgrade Hong Kong’s corporate governance regime, and to harmonize the new and old provisions. This approach has been echoed by members of the Bills Committees studying various company amendment bills on previous occasions and the SCCLR.

9. At the meeting of the FA Panel on 5 July 2004, the Administration briefed members on its proposal to rewrite the CO, as follows:

- (a) Reference would be made to the developments in the UK company law review embarked on a few years before as the basis of the rewrite exercise of the CO.
- (b) To take forward the exercise, a Companies Bill Team (CBT) would be established in the Companies Registry (CR) to prepare a White Bill for public consultation with a view to leading to the preparation of a new Companies Bill. Working Groups (WGs) would be formed under the CBT comprising representatives nominated by the relevant professional bodies and company law academics for considering and endorsing the White Bill¹.
- (c) Assuming that the UK White Bill will be available in early 2005², the Administration envisaged that preparation for the White Bill in Hong Kong would take about 24 months from May 2005 to April 2007. The White Bill would then be released for public consultation from May to October 2007. After revising the White Bill from November 2007 to April 2008, the new Companies Bill would be introduced into LegCo by October 2008. Given the complexity of the bill, it was expected that the scrutiny period would take about 18 months up to March 2010.
- (d) The Administration had formed a working group to map out the terms of reference and the detailed work schedule for the rewrite exercise. The Administration planned to submit the necessary funding proposal for undertaking the exercise to LegCo soon.

Major views and concerns expressed by members of the FA Panel

10. At the meeting of the FA Panel on 5 July 2004, while members indicated support for the proposal to rewrite the CO in general, they expressed the following views and concerns:

- (a) Besides the UK's company law reform, whether reference should be made to company laws of other jurisdictions, such as the European Union.
- (b) To ensure the quality of the rewrite exercise and to enhance its efficiency, the Administration should recruit staff of the right calibre to join the CBT and put in place an appropriate administrative

¹ The CR planned to establish two new working groups to undertake reviews of Part II of the CO, involving provisions on share capital and debentures, and the remaining parts of the CO.

² In March 2005, the Department of Trade and Industry of the UK Government issued a White Paper to consult the public on the Company Law Reform Bill (the Bill). The White Paper set out a range of measures for the Bill and included the draft key clauses and related regulations. The consultation ended in June 2005.

structure delineating the roles and duties of the various parties involved in the process.

- (c) Given the complexity of the rewrite exercise, the Administration should closely monitor the implementation of the exercise to ensure its cost-effectiveness.
- (d) The estimated timeframe of five years for completing the rewrite exercise was considered too long. The Administration was urged to expedite the exercise so that Hong Kong's company regulatory regime could keep pace with international developments as soon as possible.

11. The extract of the minutes of the FA Panel meeting on 5 July 2004 is in **Appendix II**.

Recent developments

12. The Administration will report on its plan to take forward the rewrite exercise of the CO at the FA Panel meeting to be held on 4 July 2005. The Administration intends to submit the financial proposals relating to the review exercise to the Establishment Subcommittee and the Finance Committee in due course.

References

13. A list of relevant papers is in **Appendix III**.

Major Reviews on Company Law

MAJOR REVIEWS

Report of the Standing Committee on Company Law Reform

In February 2000, the Standing Committee on Company Law Reform (SCCLR) published a report on the recommendations of a consultancy report of the review of the CO. The SCCLR Report contained recommendations on a wide range of legislative amendments including proposals to enhance shareholders' protection, update the requirements regarding directorships, simplify the requirements for registration of foreign companies and make structural changes to modernise the Ordinance.

2. On the basis of the recommendations in the SCCLR Report, we have identified a total of 62 items for legislative amendments or further study. These items are divided into the following four phases -

- (a) Phase I: The 18 items in this phase involve amendments to specific sections of the CO;
- (b) Phase II: The 19 items in this phase are related to corporate governance matters and require either further study or consultation. These items have been also examined in the context of either the Corporate Governance Review (CGR) (see paragraph 3 below) or the review of the accounting and auditing provisions (RAAP) of the CO by the Joint Government/Hong Kong Society of Accountants Working Group (see paragraph 4 below);
- (c) Phase III: The 8 items in this phase are not related to corporate governance and require either further study or consultation;
- (d) Phase IV: This 17 items in this phase involve restructuring and rewriting the Ordinance.

Corporate Governance Review (CGR)

3. In 2000, the SCCLR was tasked by the then Financial Secretary to conduct a comprehensive corporate governance review. The review covered virtually all the items categorised in Phase II of the SCCLR Report (as well as many other items) and was

completed in early 2004.

Review of Accounting and Auditing Provisions

4. There are certain parts of the CO which have not been examined in the context of the SCCLR Report. One of them is the accounting and auditing provisions in Parts II, IIA and IV of the CO. The JWG was established in March 2002 to undertake a comprehensive review of the accounting and auditing provisions (RAAP).

PRESENT POSITION

5. We have undertaken a stock-taking exercise of all the recommendations in the SCCLR Report, CGR and RAAP. The present position can be summarized as follows -

- (a) All items in Phase I of the SCCLR Report have been included in the Companies (Amendment) Ordinance 2003 which was implemented on 13 February 2004;
- (b) Items in Phases II and III of the SCCLR Report regarding shareholders remedies and overseas companies have been included in the Companies (Amendment) Bill 2003 which is being scrutinised by the Legislative Council¹;
- (c) Several items in Phases II and III of the SCCLR Report have been included in a companies amendment bill being processed by the Securities and Futures Commission (SFC) to implement the recommendations of the Report of the Steering Committee on the Enhancement of the Financial Infrastructure, which covers scripless securities, dematerialization of shares etc;
- (d) Those remaining corporate governance related items in Phase II of the SCCLR Report and Phases I and II of the CGR requiring legislative amendments are planned to be included in the next new companies amendment bill. The remaining items involving changes to, for example, best practice are being followed up by the relevant parties;
- (e) Those proposals of the JWG which have been already finalized can be included in the companies amendment bill mentioned in (d). The remainder will be processed in the context of the rewrite of the CO;

¹ The Companies (Amendment) Bill 2003 with proposals relating to group accounts removed was passed by LegCo in July 2004 (i.e. the Companies (Amendment) Ordinance 2004). The proposals relating to group accounts were subsequently incorporated in the Companies (Amendment) Bill 2004.

- (f) Remaining items in Phases III and IV of the SCCLR Report which include the inspection and offences provisions, capital maintenance provisions, and rewriting and restructuring of the CO will be taken forward in the context of the rewrite of the CO.

(Source: Annex to the paper provided by the Administration on “Overall Review of the Companies Ordinance” at the meeting of the Panel on Financial Affairs on 5 July 2004 (LC Paper No. CB(1)2254/03-04(05)).

**Extract from the minutes of meeting
of the Panel on Financial Affairs on 5 July 2004**

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V. Progress of review of the Companies Ordinance

(LC Paper No. CB(1)2254/03-04(05) — Paper provided by the Administration)

Briefing by the Administration

36. At the Chairman's invitation, the Secretary for Financial Services and the Treasury (SFST) briefed members on the progress of the overall review of the Companies Ordinance (CO) (Cap. 32). The salient points were summarized as follows:

- (a) The CO was one of the largest and most complex pieces of legislation in Hong Kong. It was derived from the UK Companies Act, which was first enacted in 1865. Regular updates of the CO were necessary to ensure that Hong Kong's company law met the needs of modern day users and continued to provide the legal infrastructure commensurate with Hong Kong's status as a major international business and financial centre. The Standing Committee on Company Law Reform (SCCLR) had been formed in 1984 to advise on the necessary amendments to the CO on a continuous basis. Although there had been regular amendments to the CO over the past two decades, it had come to a stage where piecemeal amendments were no longer desirable. A complete rewrite and restructuring of the CO was considered appropriate to take account of the latest international practices, to upgrade Hong Kong's corporate governance regime, and to harmonize the new and old provisions.
- (b) The Administration, in consultation with the SCCLR, considered it desirable to make reference to the developments in the UK company law review embarked on a few years before as the basis of the rewrite exercise of the CO. To take forward the exercise, a Companies Bill Team (CBT) would be established in the Companies Registry (CR) to prepare a White Bill for public consultation with a view to leading to the preparation of a new Companies Bill. Working Groups (WGs) would be formed under the CBT comprising representatives nominated by the

relevant professional bodies and company law academics for considering and endorsing the White Bill.

- (c) Assuming that the UK White Bill would be available in early 2005, the Administration envisaged that preparation for the White Bill in Hong Kong would take about 24 months from May 2005 to April 2007. The White Bill would then be released for public consultation from May to October 2007. After revising the White Bill from November 2007 to April 2008, the new Companies Bill would be introduced into LegCo by October 2008. Given the complexity of the bill, it was expected that the scrutiny period would take about 18 months up to March 2010.
- (d) The Administration had formed a working group to map out the terms of reference and the detailed work schedule for the rewrite exercise. The Administration planned to submit the necessary funding proposal for undertaking the exercise to LegCo before the end of 2004.

Discussion

Timeframe for the rewrite exercise

37. Ms Emily LAU indicated support for the proposal to rewrite the CO. She however expressed concern that under the proposed timeframe, it would take five years to complete the rewrite exercise. She urged that the exercise be expedited so that Hong Kong's company regulatory regime could keep pace with international developments.

38. In response, SFST assured members that the Administration would endeavour to complete the rewrite exercise as early as practicable. Given that it would be a very complex task involving extensive legal research and numerous parties, it was prudent to adopt a conservative timetable. He stressed that the proposed timeframe was indicative only and would hinge on a number of factors. The Registrar of Companies (RC) supplemented that the Administration planned to seek LegCo's approval for the resource requirements for the exercise before the end of 2004. Subject to provision of resources and suitable staff, the rewrite exercise would commence in mid 2005.

Company law reforms in other jurisdictions

39. Whilst supporting that reference should be made to the UK White Bill, Ms Emily LAU was concerned that if the UK White Bill was not available in early 2005, the rewrite exercise in Hong Kong might be delayed. She enquired how far the UK White Bill would affect the rewrite exercise.

40. In reply, RC re-iterated that both the Administration and the SCCLR agreed that, in taking forward the rewrite exercise, due regard should be given to the results of the UK company law review, as Hong Kong's company law was essentially

derived from the UK model. However, the rewrite exercise was not necessarily bound by the results of the UK review given the cultural, social, economic and regulatory differences between the two jurisdictions. While the rewrite exercise would go in parallel with the UK company law reform, it would not be constrained by the UK legislative timetable for enactment of the new UK Companies Act.

41. Mr Henry WU enquired whether the Administration would make reference to company laws of jurisdictions of the European Union (EU) in rewriting the CO. RC said that the SCCLR had not studied EU legislation, as EU countries were civil law jurisdictions whereas Hong Kong was a common law jurisdiction. He added that the SCCLR had focused its study on company laws of US, UK, Australia and Singapore etc, in conducting previous reviews on the CO.

Structure of the rewrite exercise

42. To enhance the efficiency of the rewrite exercise, Ms Emily LAU considered it important for the Administration to put in place an appropriate administrative structure delineating the roles and duties of the various parties involved in the process. In this connection, she enquired about the roles of the SCCLR and SFST in the exercise.

43. SFST advised that a designated CBT would be established in CR to undertake the relevant research work, to prepare the White Bill and to steer the new Companies Bill through LegCo. While RC would have overall administrative control of the exercise, SFST said that he himself would oversee the exercise. RC advised that in addition to the existing Joint Government/Hong Kong Society of Accountants (HKSA) Working Group, which was responsible for reviewing the accounting and auditing provisions of the CO, two new working groups would be established to undertake reviews of Part II of the CO, involving provisions on share capital and debentures, and the remaining parts of the CO. He stressed that, in view of the complexity and far reaching implications of the rewrite exercise, the Administration was fully aware of the need to involve experts and consult relevant stakeholders in the process. Representatives from professional and commercial organizations including the HKSA, Law Society of Hong Kong, Hong Kong Bar Association and the Hong Kong Chamber of Commerce etc., would be invited to join the working groups so that balanced views from the key sectors would be taken into account.

44. As regards the role of the SCCLR, RC said that although the SCCLR would not be involved in the detailed drafting of the new Companies Bill, it would be consulted on any related policy issues which emerged in the process of the rewrite and would provide guidance on the work of the CBT and WGs.

45. Referring to paragraph 11 of the paper provided by the Administration, Ms Emily LAU agreed that it was important to recruit staff of the right calibre to join the CBT in taking forward the rewrite exercise. She enquired about the details of

recruiting these staff and whether the Administration had contingency plan in the event that suitable persons could not be identified.

46. SFST advised that the Administration shared the SCCLR's view that it was crucial to recruit staff of the right calibre to undertake the re-write exercise to make it a success. The Administration's aim was to engage legal experts and relevant professionals in the private sector to participate in the task.

Cost for the rewrite exercise

47. Ms Emily LAU and Mr Henry WU enquired about the estimated cost for undertaking the rewrite exercise. SFST said that, given the complexity of the rewrite exercise, considerable resources would be required. He informed members that the last major review of the CO conducted in mid 1990s costed over \$10 million. It was envisaged that the rewrite exercise would incur higher costs. SFST advised that the Administration would be working on the funding and manpower proposals relating to the exercise and planned to submit the proposals for LegCo's approval before end of 2004. He assured members that the Administration would be mindful of the need to conduct the rewrite exercise in a cost-effective manner.

48. Mr Henry WU remarked that the scale and complexity of the rewrite exercise were comparable to those of the exercise on the enactment of the Securities and Futures Ordinance (SFO) (Cap. 571). He sought information on the costs incurred by the Administration and the Securities and Futures Commission (SFC) in the latter exercise, including the costs involved in the whole process from the preparation and drafting of the White Bill in April 2000 and the enactment of the SFO in March 2002.

49. In respect of the costs incurred by the Administration, the Deputy Secretary for Financial Services and the Treasury (Financial Services) advised that three additional posts namely, one Directorate Staff Grade B post, one Directorate Staff Grade C post and one Senior Administrative Officer post had been created to undertake the exercise on the enactment of the SFO. As for the SFC, in addition to existing staff, it had engaged a number of outside experts to assist in the project. These experts were employed on contract basis and their posts had been deleted after completion of the exercise. SFST undertook to request the SFC to provide the details on the costs involved in the project for members' reference.

(Post-meeting note: The information provided by SFC was circulated to members vide LC Paper No. CB(1)2439/03-04(02) on 21 July 2004.)

Way forward

50. At the suggestion of Ms Emily LAU, members agreed that the Panel should continue to monitor progress of the rewrite exercise in the next legislative term.

(Post-meeting note: The item on “Comprehensive review of the Companies Ordinance” was included in the Panel’s list of outstanding items for discussion.)



Rewrite of the Companies Ordinance**List of relevant papers**
(Position as at 30 June 2005)

Paper/Report	LC Paper No.
“Consultancy Report on the Review of the Hong Kong Companies Ordinance”	CB(1)1667/96-97 <i>(issued in March 1997)</i> <i>(discussed at the FA Panel meeting on 2 June 1997)</i>
“The Report of the Standing Committee on Company Law Reform on the Recommendations of a Consultancy Report of the Review of the Hong Kong Companies Ordinance”	<i>(issued in February 2000)</i>
Administration’s paper on “Overall Review of the Companies Ordinance”	CB(1)2254/03-04(05) <i>(discussed at the FA Panel meeting on 5 July 2004)</i>
Minutes of the FA Panel meeting on 5 July 2004	CB(1)2513/03-04