

立法會
Legislative Council

LC Paper No. CB(1)1386/08-09
(These minutes have been seen
by the Administration)

Ref : CB1/PL/FA/1

Panel on Financial Affairs

Minutes of meeting
held on Thursday, 26 February 2009 at 4:30 pm
in the Chamber of the Legislative Council Building

Members present : Hon CHAN Kam-lam, SBS, JP (Chairman)
Hon Ronny TONG Ka-wah, SC (Deputy Chairman)
Hon Albert HO Chun-yan
Hon James TO Kun-sun
Dr Hon Philip WONG Yu-hong, GBS
Hon Emily LAU Wai-hing, JP
Hon Abraham SHEK Lai-him, SBS, JP
Hon Vincent FANG kang, SBS, JP
Hon Jeffrey LAM Kin-fung, SBS, JP
Hon Andrew LEUNG Kwan-yuen, SBS, JP
Hon WONG Ting-kwong, BBS
Hon CHIM Pui-chung
Hon KAM Nai-wai, MH
Hon Starry LEE Wai-king
Hon Paul CHAN Mo-po, MH, JP
Hon CHAN Kin-por, JP
Hon Tanya CHAN
Hon Mrs Regina IP LAU Suk-ye, GBS, JP

Member absent : Dr Hon David LI Kwok-po, GBM, GBS, JP

Public officers attending : Agenda items IV & V
Mr CHENG Yan-chee, JP
Deputy Secretary for Financial Services and the
Treasury (Financial Services)¹

Agenda item VI

Mr John LEUNG, JP
Deputy Secretary for Financial Services and the
Treasury (Financial Services) 3

Ms Ada CHUNG
Registrar of Companies

Miss Grace KWOK
Principal Assistant Secretary for Financial Services
and the Treasury (Financial Services)

Attendance by invitation : Agenda item IV

Mr Brian HO
Executive Director
Corporate Finance Division
Securities and Futures Commission

Mr Charles GRIEVE
Senior Director
Corporate Finance Division
Securities and Futures Commission

Mr Richard WILLIAMS
Head of Listing Division
Hong Kong Exchanges and Clearing Limited

Mr Mark DICKENS, JP
Executive Vice President
Listing Division
Hong Kong Exchanges and Clearing Limited

Agenda item V

Mr Paul KENNEDY
Executive Director and Chief Operating Officer
Securities and Futures Commission

Clerk in attendance: Ms Rosalind MA
Chief Council Secretary (1)5

Staff in attendance : Mr Noel SUNG
Senior Council Secretary (1)4

Ms Haley CHEUNG
Legislative Assistant (1)8

Action

I Confirmation of minutes of meeting and matters arising

(LC Paper No. CB(1)857/08-09 — Minutes of meeting on 5 January 2009)

The minutes of the meeting held on 5 January 2009 were confirmed.

II Information papers issued since the last meeting

(LC Paper No. CB(1)769/08-09 — Letter from Mr Albert CHAN Chun-wai

LC Paper No. CB(1)793/08-09 — Submission on "sharing of consumer credit data")

2. Members noted the information papers issued since the last meeting.

III Date of next meeting and items for discussion

(LC Paper No. CB(1)854/08-09(01) — List of outstanding items for discussion

LC Paper No. CB(1)854/08-09(02) — List of follow-up actions)

3. Members agreed to discuss the following items at the next meeting scheduled for 6 April 2009:

(a) Inland Revenue (Amendment) Bill 2009; and

(b) Progress report on the work of the Financial Reporting Council.

4. In response to Ms Emily LAU's concern about the follow-up actions to be taken in respect of the Panel's previous discussions on the reports prepared by the Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC) on the Lehman Brothers Minibonds incident, the Chairman stated that, if members so wished, the Panel might invite the

Administration, HKMA and SFC to report the progress in implementing the recommendations of the reports in due course.

IV Issues related to the proposed extension of the "black out" period and introduction of quarterly financial reporting

(LC Paper No. CB(1)821/08-09(01) — Letter dated 13 February 2009 from Hon James TO and Hon KAM Nai-wai (Chinese version only)

LC Paper No. CB(1)854/08-09(03) — Paper provided by the Administration

LC Paper No. CB(1)855/08-09 — Background brief on the proposed extension of the "black out" period and introduction of quarterly financial reporting prepared by the Legislative Council Secretariat

Relevant papers issued for the special meeting on 30 December 2008

LC Paper No. CB(1)460/08-09(01) — Letter dated 17 December 2008 from Hon Abraham SHEK, Hon Vincent FANG Kang, Hon Jeffrey LAM Kin-fung and Hon CHIM Pui-chung (Chinese version only)

LC Paper No. CB(1)484/08-09(01) — Hon CHIM Pui-chung's letter dated 23 December 2008 on Hong Kong Exchanges and Clearing Limited (HKEx)'s proposed extension of blackout period (Chinese version only)

LC Paper No. CB(1)493/08-09(01) — HKEx's paper on amendments to Listing Rules arising from the Combined Consultation Paper and proposals to mandate quarterly reporting

- LC Paper No. CB(1)498/08-09(01) — Speaking note of Mr Richard Williams, Head of Listing Division of HKEx (English version only)
- LC Paper No. CB(1)696/08-09(01) — List of follow up actions for the special meeting on 30 December 2008 prepared by the Legislative Council Secretariat
- LC Paper No. CB(1)696/08-09(04) — Administration's response to members' concerns raised at the special meeting on 30 December 2008
- LC Paper No. CB(1)697/08-09(01) — Administration's preliminary response to the motion passed at the special meeting on 30 December 2008)

Briefing by the Administration

5. At the invitation of the Chairman, the Deputy Secretary for Financial Services and the Treasury (Financial Services)1 (DS(FS)1) briefed members on the latest developments with regard to the proposed extension of the "black out" period and introduction of quarterly financial reporting for companies listed on the Stock Exchange of Hong Kong (the Exchange). The motion passed at the special meeting of the Panel on Financial Affairs (FA Panel) on 30 December 2008 "requesting not to effect the amendments to the Listing Rules and launch a consultation afresh" was reflected to the Listing Committee of the Hong Kong Exchanges and Clearing Limited (HKEx). Having regard to the advice of the Securities and Futures Commission (SFC) and the findings of the Listing Division of HKEx's analysis of dealings by directors during the year ended 31 December 2008, as well as the recent comments concerning the extension of the "black out" period, the Listing Committee decided, at its meeting on 12 February 2009, to modify the "black out" proposal. The modified proposal was set out in paragraph 5 of the Administration's paper. DS(FS)1 also advised that the Administration's paper set out other measures being pursued by the Listing Committee to enhance the disclosure regime under the Securities and Futures Ordinance (SFO) (Cap. 571) and the Listing Rules.

Declaration of interests

6. Mr Paul CHAN and Mr Abraham SHEK declared that they were non-executive directors of listed companies.

Discussion

7. Mr Vincent FANG, Mr Jeffrey LAM and Dr Phillip WONG welcomed the modified proposal which would only extend the "black out" period to a maximum of three months in a year during the period between year/period end and result announcements. Mr FANG was nevertheless concerned that the subsequent introduction of quarterly financial reporting would possibly extend further the "black out" period to five months, as directors would also be prohibited from dealing in securities of their companies during the period between quarter end and result announcement. Mr FANG was of the view that the "black out" period proposal should be considered together with the proposed quarterly financial reporting as a package and enquired about the timeframe for introduction of the latter.

8. Mr Richard WILLIAMS, Head of Listing Division, HKEx (H(LD)/HKEx) said that the Listing Committee viewed quarterly financial reporting as a long term goal. For interim enhancement, the Listing Committee would explore alternative approaches and undertake a further consultation with stakeholders on the alternative formats in which listed issuers might report to shareholders on a periodic basis, in addition to annual and interim reports. HKEx was preparing documents for market consultation on some more immediate proposals to enhance the disclosure regime, which would be ready probably in the coming month or so. Subject to market response and approval of SFC, HKEx aimed to implement some of the proposals before 2010. He was nevertheless unable to provide any concrete timeframe for introduction of quarterly financial reporting as this had to be considered by the Listing Committee, taking into account the views of the market and SFC.

9. Dr Philip WONG expressed concern that frequent periodic reporting might result in listed issuers' preference for short-term business strategies over those for the long-term development of the companies, as the former could achieve quicker returns and present more attractive results to the shareholders in the periodic reports. Mrs Regina IP supported the modified proposal for the extension of the "black out" period but objected to implementation of quarterly financial reporting. They both observed the problem of short-sightedness in some US companies as a result of frequent reporting. Mrs IP also pointed out that as the stock market of Hong Kong was susceptible to volatility due to dealings by hedge funds and the interests of the directors of listed issuers were in fact more aligned with those of the minority shareholders,

imposing too many restrictions on directors' trading would not be in the best interest of the investing public.

10. H(LD)/HKEx advised that the concern about inclination towards short-term business strategies was less warranted in the case of Hong Kong compared with that in the US, as listed companies in the US had more decentralized ownership and hence the management would try to present good business performance in every result announcement to satisfy the shareholders in general. He nevertheless appreciated that this was a challenge for the management of the listed companies in devising their business strategies.

11. Mr Abraham SHEK and Mr Paul CHAN supported the modified proposal. Mr SHEK enquired how the public consultation on quarterly financial reporting would be conducted to ensure that views of the stakeholders on the issue would be gauged accurately and thoroughly. Mr CHAN supported the introduction of quarterly financial reporting to enhance corporate governance of listed companies and inspire investors' confidence in the market of Hong Kong. Mr CHAN nevertheless called on HKEx to study in detail the form of quarterly reporting to be introduced in Hong Kong, i.e. whether it should be in the form of management reports or financial reports, and conduct thorough consultation with stakeholders before finalizing the proposal. Mr Jeffrey LAM also expressed concern about the conduct of consultation on quarterly financial reporting.

12. H(LD)/HKEx advised that in conducting market consultations, HKEx would describe the regulatory issues in question, set out the possible options to address the issues with analysis on the pros and cons of these options, with a view to soliciting market feedback on the proposals and to understanding their impacts on the market. Taking into account views of respondents expressed during the consultation, the proposals would be presented to the Listing Committee for consideration. H(LD)/HKEx said that it might not always be possible to identify a consensus option during the process of consultation, given that consultations on regulatory proposals would not be welcome by those being regulated.

13. Dr Philip WONG commented that the proposed extension of the "black out" period had sent three wrong messages to the market, namely, the regulatory safeguards against insider trading were ineffective; the amount of dealings by directors were substantial which had created an uneven playing field in the market; and the fluctuations in share prices were mainly caused by the financial results of the companies concerned. Dr WONG said that as far as he knew, dealings by directors only constituted an insignificant portion of market transactions of the securities of their companies. Moreover, other than their financial results, share prices of listed companies would be affected by other factors such as the economic environment and reports published by financial analysts of large broker firms. Mr Jeffrey LAM also observed that

apart from timely disclosure of financial results and price sensitive information by listed issuers, the regulators should also take heed of the market impact of comments/analyses made by big investment banks on the business performance of listed companies and consider measures to monitor the impact of such information on the share prices of the companies concerned.

14. In response, H(LD)/HKEx said that the proposed extension of the "black out" period was not put forward for enhancing safeguards against insider trading. Insider trading was governed by provisions against market misconduct under SFO. The analysis conducted by the Listing Division of HKEx on dealings by directors, which would be published in due course, revealed that dealings by directors of some companies had exceeded 10% of the annual transactions of the shares of these companies. While it was legitimate for company directors to support the trading of their company's shares, H(LD)/HKEx advised that HKEx would publish information on the dealings by directors on a regular basis to facilitate the investing public in making informed investment decisions. As to Dr Philip WONG's comment about trading by financial analysts, H(LD)/HKEx pointed out that in accordance with the code of practice applicable to these analysts, they should not conduct dealings in shares of listed companies which they were providing services. There were also transparency requirements for these analysts to disclose the positions they held in the shares in their analyses.

15. Mr Jeffrey LAM and Mr Abraham SHEK pointed out that under the current financial crisis, any changes to the Listing Rules could have significant impact on the listed issuers and the market, and hence only duly examined proposals supported by the majority of the stakeholders should be taken forward. Mr LAM recalled that during the market consultation through the Combined Consultation Paper (CCP), the majority of the respondents giving views on the proposed extension of "black out" period opposed to the proposal. Mr SHEK appreciated that the debate over the extension of the "black out" period was not directly related to insider dealings regulations. Mr SHEK pointed out that the controversy should not be seen as a conflict of interests between majority and minority shareholders of listed companies, as the modified proposal was not only supported by major listed issuers but also many small investors.

16. Ms Starry LEE considered the modified proposal acceptable, noting the insignificant volume of transactions by company directors and the possibility that a prolonged "black out" period would create a window of opportunities for corporate snipers under a volatile market. She noted that professional organizations such as the Law Society of Hong Kong and the Hong Kong Institute of Certified Public Accountants also supported the modified proposal. Ms LEE nevertheless noted with concern the perception that the Listing Committee had been pressurized to modify the extension proposal. In this connection, she enquired about the measures HKEx would take to assess the

effect of the modified proposal, say, by monitoring dealings by directors on a continuous basis.

17. H(LD)/HKEx advised that the Listing Committee had directed the Listing Division to undertake an enhanced programme of monitoring dealings by directors which was intended to increase confidence that suspicious dealings were subject to close regulatory scrutiny. Mr Brian HO, Executive Director, Corporate Finance Division, SFC (ED(CF)/SFC) supplemented that the Listing Division would closely monitor dealings by directors during the period between year/period end and results announcement and report any suspicious dealings to SFC for investigation. To address concerns about the lead time required for enforcement actions against cases of market misconduct, ED(CF)/SFC advised that recently SFC had stepped up actions against criminal offences and had succeeded in convicting a few cases of insider dealings. Responding to Ms Starry LEE's further concern about enhancements to the disclosure regime, ED(CF)/SFC said that SFC would work with HKEx to consider refining the Listing Rules concerning price sensitive information to pave way for the proposal of a statutory obligation to disclose price sensitive information.

18. Mr Paul CHAN was of the view that if the extension of the "black out" period was proposed on grounds that the directors possessed proprietary information about their companies' performance before the announcement of the companies' results to the public, the directors should have been debarred from trading their companies' shares at all time as they should have received regular reports on their companies' performance.

19. Mrs Regina IP opined that it was not justifiable to extend the "black out" period simply for the sake of addressing the concern about investors' perception of an uneven playing field. Mrs IP also disagreed with HKEx's observation that the ownership structure of Hong Kong listed companies, with a large proportion of them being family owned and managed companies would contribute to the concern about investors' perception, given that many corporate governance problems had been detected in the professionally managed companies in overseas jurisdictions. Mrs IP commented that the arrangement of grouping over 40 proposals under 18 policy issues for consultation through CCP might have distracted the attention of listed issuers on the proposed extension of the "black out" period. She called on HKEx to improve the consultation arrangement so that respondents could easily focus on the proposals that had been put forward.

20. Mr CHIM Pui-chung supported the modified proposal, pointing out that there was no evidence on the adverse impact of dealings by directors on the interests of the investing public, as dealings by directors only represented a negligible percentage of the overall transactions of the securities of the companies and they had to report these transactions to HKEx. He opined that

SFC/HKEx should take heed of and respond to the views of the listed issuers, and there was room for improvement in its consultation process. Mr CHIM was of the view that under the three-tier regulatory structure, the Administration, SFC and HKEx should maintain close communication and work in collaboration in mapping out measures to ensure an orderly, informed and fair securities and futures market.

21. DS(FS)1 advised that there was clear division of roles and responsibilities under the “three-tier regulatory structure” of the securities and futures industry. The Administration was responsible for formulating policies and coordinating legislative exercises; SFC had the statutory powers and responsibilities to supervise and regulate the securities and futures markets; and HKEx was the market operator and frontline regulator responsible for administering the Listing Rules. The three parties had been performing their respective roles effectively all along.

22. The Deputy Chairman remarked that the backtracking of the Listing Committee on the original "black out" proposal and delayed introduction of quarterly financial reporting as a long term goal had reduced the integrity and credibility of the Hong Kong stock market. The Deputy Chairman recalled that, when explaining the background to the original "black out" extension proposal at the FA Panel meeting on 30 December 2008, HKEx advised that the proposal had received support from respondents and got the approval of SFC. In this regard, the Deputy Chairman doubted the propriety of the existing mechanism for making amendments to the Listing Rules and sought information on the formulation process of the original "black out" extension proposal, such as the party who had initiated the proposal.

23. H(LD)/HKEx advised that the idea of extending the "black out" period was first raised by the SFC Public Shareholders Group and then championed by the staff of SFC. The Listing Division of HKEx had presented three possible options to deal with the issue of "black out" period for the Listing Committee's consideration: to extend the "black out" period from the financial period end until publication of results; to adopt the United Kingdom (UK) approach which involved either a maximum 60 day period or the period from the financial period end until publication of the issuers' results; or to maintain the status quo. The Listing Committee had adopted the first option and the revised Listing Rules to implement the proposal were approved by the board of the HKEx and SFC.

24. The Deputy Chairman further questioned whether the Listing Committee had yielded to the pressure of SFC or the Government in modifying the "black out" proposal. In response, H(LD)/HKEx advised that he was not in a position to respond on behalf of members of the Listing Committee. H(LD)/HKEx pointed out that in light of media reports, market comments and concerns of LegCo Members, the Listing Committee had re-considered the

"black out" proposal, as a package with other measures to enhance the disclosure regime, such as quarterly financial reporting. The Listing Committee had also taken into account views of SFC and further analysis of dealings by directors during 2008 provided by the Listing Division of HKEx. The latest analysis revealed a reduction in the number as well as value of dealings by directors of Main Board issuers during the recent period. Such findings had indicated self-restraint on the part of directors and effectiveness of the insider trading regulations. In re-consideration of the "black out" proposal, the Listing Committee focused on reaching a consensus option to address the issues of enhanced disclosure and perception of a level playing field in the market. The modified proposal was a step forward which could address the issue of perception and at the same time enhanced the disclosure regime.

25. Noting the three possible options to deal with the issue of "black out" period presented to the Listing Committee for consideration, Miss Tanya CHAN queried why, in working out the modified proposal, the Listing Committee had not gone for the second option directly, i.e. the UK approach. In response, H(LD)/HKEx advised that HKEx had to obtain the approval of SFC for Listing Rules amendment to implement the modified proposal. The modified proposal was an option to make some progress in the disclosure regime based on "pragmatism".

26. Noting that the Listing Committee had invited SFC to provide further advice on the issue of "black out" period and H(LD)/HKEx's response on putting forward the modified proposal based on "pragmatism", Mr James TO was of the view that the Listing Committee had yielded to pressure of SFC and the Government in the decision to modify the "black out" proposal. Mr TO commented that the modified proposal would not enhance the disclosure regime, as it did not provide adequate incentive for listed issuers to announce their results as soon as possible after the year/period end. Mr TO sought information on SFC's advice to the Listing Committee.

27. In response, ED(CF)/SFC advised that during the consultation period of CCP, over 100 submissions were received from listed issuers and market practitioners, which was a record high in HKEx's market consultations. The views of respondents on the proposed extension of the "black out" period were rather divided, with about one third supporting, one third opposing and the remaining one third making no comments. SFC had approved the proposed Listing Rule amendment to implement the original extension proposal noting that there was no strong opposition from the market. If the objections raised by the some 200 listed issuers shortly before the implementation of the proposed extension of the "black out" period had been received earlier, SFC might have taken a different view on the proposal. SFC also noted that the opposing parties had put forward new arguments vindicated by the prevailing market situation, including the difficulty controlling shareholders faced during

hostile takeovers and impact from a court judgment on the tools available to listed issuers to counter hostile takeovers. In view of the latest market comments and views of the FA Panel, SFC had advised the Listing Committee to re-consider the proposed extension of "black out" period together with the proposed shortening of reporting deadlines and quarterly financial reporting as a package. ED(CF)/SFC pointed out that the Listing Committee's decision to put forward the modified proposal, an arrangement somewhat between the UK approach and the original proposal, was made independently rather than adopted in full the advice of SFC. ED(CF)/SFC stressed that it would be difficult for all concerned parties to reach a consensus on a regulatory issue like the extension of the "black out" period.

28. To address the concern of Mr James TO, SFC and HKEx were requested to provide further information in writing on: details of SFC's further advice to the Listing Committee on the issue of "black out" period; new arguments considered by the Listing Committee and new developments supporting these arguments; and findings of the Listing Division of HKEx's further analysis of dealings by directors during the year ended 31 December 2008.

(Post-meeting note: SFC and HKEx's response was circulated to members vide LC Paper No. CB(1)1173/08-09 on 31 March 2009.)

29. Mr Albert HO did not subscribe to H(LD)/HKEx's explanation on the reasons for modifying the "black out" proposal and pointed out that the decision to modify the proposal had given the public an impression that the Listing Committee/HKEx had succumbed to pressure from the major listed issuers objecting to the original "black out" proposal. Pointing out that the "black out" proposal had been finalized after a long market consultation process, during which the pros and cons of the proposal had been thoroughly examined, Mr HO queried the credibility of the Listing Committee in deciding to modify the proposal without conducting further consultation. Mr HO opined that the guiding principle for the proposed extension of the "black out" period was to ensure a level playing field in the stock market. It was unfair to allow company directors to deal with the securities of their companies whilst in possession of proprietary and/or price sensitive information which was not available to other investors before result announcement and hence the modified proposal was not in line with the guiding principle of fairness. Mr HO questioned how a quality market could be maintained in Hong Kong if rules and proposals to ensure fair play in the market could be withdrawn due to strong pressures from listed issuers.

30. DS(FS)1 advised that the Administration considered that in light of the divergent views in the market regarding the proposed extension of the "black out" period in late 2008, it was necessary for the Listing Committee to re-consider the proposal having full regard of the latest comments from listed issuers, LegCo Members and SFC, with a view to working out an option that

met the circumstances of the Hong Kong market and was accepted by the relevant stakeholders. The modified proposal was put forward after detailed consideration by the Listing Committee.

31. Referring to recent incidents including the disclosure of investment losses by Citic Pacific, the privatization proposal of PCCW and the modification of the extension of "black out" period, Mr KAM Nai-wai expressed disappointment about the Administration's work in investor protection. Mr KAM recalled that at the FA Panel meeting on 30 December 2008, HKEx had provided many figures to support the original "black out" proposal. Nevertheless, the Listing Committee had subsequently decided to modify the proposal by cutting down the maximum "black out" period. Miss Tanya CHAN expressed similar concern about the change in stance of the Listing Committee/HKEx. Mr KAM stressed that the interest of the investing public should not be ignored and asked whether HKEx would consult the public afresh, especially the small investors, on the modified proposal.

32. H(LD)/HKEx said that the proposed extension of the "black out" period was only one of the measures to enhance the disclosure regime, and the Listing Committee would pursue other enhancement measures, such as quarterly financial reporting. H(LD)/HKEx reiterated that it was always difficult to reach a consensus option in the consultation of regulatory issues, as stakeholders would have different views from their own perspectives. HKEx aimed to gauge the views of stakeholders through market consultations, in order to facilitate the Listing Committee in examining the possible options to address regulatory concerns and deciding on the way forward. In the process of market consultation on the proposed extension of the "black out" period, a large number of stakeholders had put forward their comments at a very late stage. In response to such comments and the comments of LegCo Members, the Listing Committee had re-considered the issue and decided to modify the "black out" proposal. DS(FS)1 added that the Administration supported measures to enhance the disclosure regime under SFO and the Listing Rules.

Motion by Mr Albert HO

33. Mr Albert HO proposed the following motion which was seconded by Mr KAM Nai-wai and Mr James TO:

"由於港交所上市委員會在2月12日修訂延長禁止買賣期引起公眾強烈反響，本委員會要求有關當局就有關問題全面再諮詢公眾意見。"

(Translation)

"That, as the 'black out' period extension modified by the Listing Committee of the HKEx on 12 February has aroused strong reaction in

the community, this Panel requests the authority concerned to conduct a comprehensive public consultation on this issue afresh."

34. The Chairman considered that the proposed motion was directly related to the agenda item under discussion and members agreed that the motion should be dealt with at the meeting. The Chairman put the motion to vote. Among the members present, five members voted for and seven members voted against the motion. The motion was negated.

V Budget of the Securities and Futures Commission for the financial year of 2009 – 2010

(LC Paper No. CB(1)854/08-09(04) Administration's paper on the Budget of the Securities and Futures Commission for the financial year of 2009 – 2010)

Declaration of interests

35. The Chairman declared that as he was a non-executive director of SFC, he would like to invite the Deputy Chairman to chair the meeting for this item on his behalf. At the invitation of the Chairman, the Deputy Chairman took over the chair.

Discussion

Manpower plan and staff remuneration

36. Noting the large number of complaints relating to the Lehman Brothers Minibonds and structured financial products, Mr James TO enquired whether SFC had provided for additional manpower resources in its estimated provision for the 2009-2010 financial year for complaint handling work. Mr TO was concerned whether the existing manpower resources of SFC could adequately cope with the increased workload and opined that SFC should engage additional staff for complaint handling, such as through employing more contract or temporary staff.

37. In response, Mr Paul KENNEDY, the Executive Director and Chief Operating Officer/SFC (ED&COO/SFC) said that as a matter of fact, the workload of the Enforcement Division of SFC had increased by about 40% in the past year and the manpower resources had been fully stretched to cope with such increase. He pointed out that SFC had worked out the manpower plan in the 2009-2010 budget based on the estimated requirements in the medium and longer-term. SFC would keep its manpower provision under review and arrange to seek provisions for additional manpower resources, where

necessary. As regards manpower resources required for the investigation of Lehman-related complaints, ED&COO/SFC advised that SFC had adopted a "top-down" approach in handling these complaints, which was more efficient than handling each and every case of complaint on an individual basis. He took note of Mr TO's concern about the possible need to engage additional manpower resources for dealing with the Lehman-related complaints and reiterated that SFC would request for additional provisions where necessary.

38. Ms Emily LAU also expressed concern about the manpower resources allocated for the investigation of Lehman-related complaints. Ms LAU stressed that SFC should make every effort to expedite the complaint handling and investigation process to meet public expectations. She therefore requested SFC to provide further information on the number of cases awaiting investigation and the number of existing and/or new staff deployed to investigate the complaints. In response, ED&COO/SFC said that he did not have the required information in hand and undertook to submit a written response to this request after the meeting.

(Post-meeting note: SFC 's response was circulated to members vide LC Paper No. CB(1)1173/08-09 on 31 March 2009.)

39. Ms Emily LAU noted that SFC would freeze the pay for its staff in 2009-2010 in view of the recessionary economic outlook. She enquired about details of this measure. In reply, ED&COO/SFC advised that the 2009-2010 budget of SFC was prepared on the basis that all staff at directorate level and above would receive no salary increment. A provision of approximately 1% of personnel costs had been included on the assumption that there would be a cost of living adjustment for middle and junior ranking staff. Responding to Ms LAU's further enquiry, ED&COO/SFC said that the pay packages of SFC staff comprised an annual fixed pay and a performance related variable pay. While SFC would freeze the fixed pay for the directorate staff in 2009-2010, staff would still be eligible for variable pay, the amount of which had yet to be determined but was expected to be lower than that of last year.

40. Given the current economic downturn and the Lehman Brothers Minibonds fiasco, Ms Emily LAU questioned the rationale behind offering variable pay to SFC directorate staff. Ms LAU was of the view that as the unemployment rate was on the rise, SFC should no longer face recruitment difficulties which necessitated the provision of competitive remuneration package to attract and retain talents. Mr Abraham SHEK shared Ms LAU's view. Mr SHEK said that unlike staff of financial institutions whose pay was linked to their profit-making ability, SFC staff were performing regulatory duties and should not be eligible for extra pay for doing their work in a diligent and effective manner. Mr SHEK was of the view that the same principle should apply to other statutory bodies and asked whether the Government

would consider requesting SFC and other statutory bodies to restructure their pay packages so that only fixed pay would be offered to their staff.

41. ED&COO/SFC advised that in working out the pay packages, SFC had to ensure that the pay offered would be adequate to attract and retain talents required for the discharge of its statutory duties. SFC commissioned independent consultants to conduct pay surveys before determining the remuneration levels and adjustments for the coming year. Findings of the surveys had revealed that the packages offered by SFC was appropriate or below market median compared with market rates. ED&COO/SFC pointed out that splitting the remuneration of SFC staff into two components, i.e. fixed pay and variable pay, was a human resources management tool to drive staff performance, as the variable pay component was performance related. ED&COO/SFC pointed out that while there was a drop in the staff turnover rate of SFC key staff in the past year, it was still not easy for SFC to find the right talents among the candidates in recruitments. DS(FS)1 supplemented that Members' concern about the variable pay component in the staff pay packages of SFC might be relayed to the Remuneration Committee of SFC for consideration.

42. Responding to Mr SHEK's further enquiry, the Chairman said that as far as he knew, a number of public bodies had included variable pay in their staff remuneration structures. The staff remuneration structure of SFC was determined on the basis of the advice of an independent consultant. The design of the pay packages actually involved splitting the total annual remuneration into fixed pay and variable pay, and the amount of variable pay offered to the staff concerned would hinge on his/her performance.

43. Noting that a total headcount of 36 was proposed for SFC's external relations function in 2009-2010, Mr James TO questioned whether this was proportional, as the proposed headcount for this function would constitute over 6% of the total establishment of SFC. Mr TO further asked the reasons for proposing additional manpower for the Licensing Department and the work on investment products in 2009-2010, amid the recent financial crisis leading to a shrinking financial market and drop in transactions.

44. In reply, ED&COO/SFC explained that the 36 staff under external relations were deployed for different areas of work which included dealings with the media and the press, handling complaints and investor education. On the workload relating to licensing, ED&COO/SFC advised that the headcount of the Licensing Department had remained stagnant despite the over 30% increase in the number of licensees in recent years. Moreover, additional manpower resources were required for conducting the process re-engineering project for all licensing related processes and systems, which SFC had commenced following a review of its operational effectiveness. As regards the work on investment products, ED&COO/SFC pointed out that additional

resources were also required to focus on the review of new applications for authorization of offering documents for retail products and surveillance of advertisements. The regulatory framework for investment products and product disclosure documents also required review to address concerns regarding its adequacy in the light of the current more challenging economic environment.

Amount of reserves and levy

45. Noting that SFC would have a reserve of \$4.98 billion by 31 March 2009, which was 6.4 times of its approved operating expenditure for the 2008-2009 financial year, Mr CHIM Pui-chung queried why SFC did not propose to reduce the rate or amount of levy. Mr CHIM pointed out that according to the prevailing arrangement, SFC should recommend to the Administration for reduction of levy if the reserves of SFC was more than twice its operating expenses for that financial year.

46. ED&COO/SFC responded that having regard to the volatile market performance and the expected increase in resources to address challenges in various regulatory issues, SFC considered that a reduction in levy should not be pursued for the time being. DS(FS)1 supplemented that the statutory provision on reduction of levy did not mean an automatic reduction in levy once the SFC's reserves was more than twice its operating expenses for that financial year. Instead, SFC might recommend for the Administration's consideration that the rate or amount of levy be reduced having regard to relevant factors such as its forecast revenue and expenses for the coming year. DS(FS)1 said that the Administration concurred with SFC that the levy rates should not be revised for the time being having regard to the volatile performance of the securities market.

VI Rewrite of the Companies Ordinance

(LC Paper No. CB(1)678/08-09(05) — Administration's paper on progress update on the Companies Ordinance rewrite exercise

LC Paper No. CB(1)677/08-09 — Updated Background Brief on the Companies Ordinance rewrite exercise prepared by the Legislative Council Secretariat)

(The Chairman took over the chair at this point.)

Briefing by the Administration

47. At the invitation of the Chairman, the Deputy Secretary for Financial Services and the Treasury (Financial Services)3 (DS(FS)3) highlighted salient points in the Administration's paper on the latest development of the exercise to rewrite the Companies Ordinance (the Ordinance) (Cap. 32). The Administration had conducted three topical public consultations in 2007 and 2008 to gauge views on certain complex issues. The Administration would take into account public feedback from the consultations in preparation of a draft Companies Bill for public consultation in the fourth quarter of 2009 before it was introduced into the Legislative Council (LegCo) around October in 2010. DS(FS)3 also highlighted the following new developments in relation to the rewrite exercise:

- (a) The Administration adopted the recommendation of the Task Force on Economic Challenges to re-consider the introduction of a corporate rescue procedure, ahead of the schedule of the Phase II rewrite exercise which would deal with the winding-up related provisions in the Ordinance. The legislative proposal for corporate rescue was last put forward to LegCo in 2001 but the relevant bill had not been enacted in that LegCo term. The Administration would advance the study on provisions of the Ordinance in relation to the introduction of corporate rescue procedure, having regard to practices and recent developments in other common law jurisdictions as well as the feedback from consultations with stakeholders, and might introduce a separate amendment bill for corporate rescue procedure if a consensus option could be identified.
- (b) The Administration would introduce another amendment bill around October/November 2009 for implementation of electronic company incorporation and other technical amendments. Legislative amendments were required to incorporate the electronic signature and certification involved in the incorporation procedure. Amendments would also be proposed through the bill to tackle the problem of "shadow companies", which had exploited the company name registration system in Hong Kong to facilitate their counterfeiting activities. The Administration planned to consult the Panel on the legislative proposal in June this year, with a view to introducing the amendment bill in the fourth quarter of 2009.

Discussion

Timeframe for introduction of the new Companies Bill

48. Ms Emily LAU expressed concern that if the new Companies Bill was introduced into LegCo around October in 2010, there might not be sufficient time for Members to complete scrutiny of the Bill before the end of the current LegCo term in 2012. Mr Albert HO and the Deputy Chairman expressed similar concern and opined that despite past reviews implemented through a number of amendment bills, the Ordinance which was enacted in 1948, remained largely outdated. The Deputy Chairman was of the view that the Ordinance should be modernized through a complete rewrite but not piecemeal amendments. The Deputy Chairman was concerned about the prolonged process of the rewrite exercise and the delay in the drafting of the new Companies Bill. He called on the Administration to expedite the drafting of the new Companies Bill and allow adequate time for LegCo's scrutiny work.

49. DS(FS)3 advised that the progress of the rewrite exercise was slightly behind schedule in that the draft Companies Bill would be issued for public consultation in the fourth quarter of 2009, instead of the original plan of mid-2009. He nevertheless assured members that the Administration would endeavour to introduce the new Companies Bill into LegCo in the fourth quarter of 2010, as it was aware that the scrutiny of such a complicated legislation would take considerable time and might span over one year. DS(FS)3 said that the Administration would try its best to facilitate Members in the scrutiny work, with a view to enacting the new Companies Ordinance before the end of the current LegCo term in 2012, failing which the Bill would lapse and have to be introduced afresh in the next term.

50. Mr Albert HO opined that the rewrite exercise could be conducted in a more efficient manner by making reference to the latest company legislation of overseas jurisdictions. Mr HO enquired whether the new Companies Bill would be modeled on the legislation of the United Kingdom (UK) or that of Australia. The Deputy Chairman remarked that the company regime in Australia was more advanced and should have higher reference value. He nevertheless opined that the Administration should develop a model that suited the unique circumstances of Hong Kong instead of adopt one directly from overseas jurisdiction.

51. DS(FS)3 responded that in preparing the draft Companies Bill, reference would be made to the latest developments of company law in other common law jurisdictions such as the UK, Australia and Singapore. For example, reference would be made to the UK Companies Act 2006 but not the earlier versions. He advised that the draft Bill would not be a direct adaptation of the UK Companies Act 2006 or other company laws. The Administration would benchmark the company regime of Hong Kong against those of other common law jurisdictions in general in the rewrite, taking into account Hong Kong's unique business environment.

Scope of the rewrite exercise

52. Ms Emily LAU referred to paragraph 13 of the Administration's paper about directors' duties. She noted that the Administration considered it premature at this stage to go down the route of comprehensive codification of directors' general duties in light of the controversies over the idea during the topical consultation. Ms LAU was concerned that despite controversies, the Administration should not give up the opportunity of enhancing corporate governance through codifying directors' general duties. She asked the Administration to make reference to the UK Companies Act 2006 in this regard.

53. DS(FS)3 advised that divergent views on directors' duties were expressed by respondents during the second topical consultation. Although directors' general duties were codified in the UK Companies Act 2006, dissenting views had been raised by stakeholders and professionals during the legislative process. The pros and cons of codifying directors' general duties were set out in the paper for the second topical consultation. Respondents who disagreed with the idea of codifying directors' general duties considered that detailed codification would reduce the flexibility that the court had for interpretation and development of the law. While reference would be made to practice in the UK, more time should be taken to observe the effect of the UK reform on directors' duties, as this had just come into operation in 2008 and had not been fully tested. Nevertheless, the Administration saw merits in codifying directors' standard of care, skill and diligence as this would clarify the law and enhance corporate governance. Responding to Ms Emily LAU's further enquiry, DS(FS)3 advised that the Administration would not rule out the possibility of re-visiting the idea of codifying directors' duties, subject to the experience of the UK reform on directors' duties as well as views of respondents during the upcoming public consultation of the draft Companies Bill.

54. The Deputy Chairman suggested that the scope of the rewrite exercise should cover issues of wide public interest, such as review of the provisions governing privatization of listed companies. He opined that the existing voting requirements imposed by law for approval of the scheme of arrangement for privatization might not adequately safeguard the interest of minority shareholders as intended. In reply, DS(FS)3 advised that the Administration would invite views on the draft provisions of the Companies Bill, including provisions governing privatization, during the upcoming public consultation later this year.

55. While not opposing to the Administration's proposal of introducing corporate rescue procedure through a separate amendment bill, Ms Emily LAU doubted whether the legislative exercise could be completed within a short timeframe as to rescue enterprises hard-hit by the current financial tsunami,

given the divergent views of stakeholders on the procedure. Mr Albert HO recalled that the failure to reach a consensus for enactment of the bill on corporate rescue back in 2001 was mainly attributable to problems relating to labour issues. Mr HO hoped that the Administration would take note of these issues when preparing the legislative proposal for corporate rescue.

Statutory derivative action

56. Mr Albert HO expressed concern that the statutory derivative action regime under the Ordinance did not provide for multiple derivative actions. Mr HO enquired whether amendments would be made to rectify the problem. In reply, DS(FS)3 advised that the Administration noted the recent recommendation of the Court of Final Appeal for legislative amendments to allow for multiple derivative actions, and planned to incorporate relevant technical amendments in the Companies amendment bill to be introduced into LegCo in the fourth quarter of 2009.

Company names

57. The Chairman noted that the Administration aimed to introduce, ahead of the rewrite exercise, necessary legislative amendments to tackle possible abuses of company name registration regime by "shadow companies". He opined that given the increasing economic integration between Hong Kong and the Mainland, it would be helpful if the Administration could make reference to the relevant Mainland regulations and requirements in preparation of the legislative amendments.

58. DS(FS)3 advised that the Registrar of Companies (the Registrar) had received many complaints from owners of trademarks or trade names regarding "shadow companies". Authorities in the Mainland, Japan, the European Union and the United States had also expressed concerns that such "shadow companies" exploited the company name registration system in Hong Kong to facilitate their counterfeiting activities in the Mainland. The Administration was of the view that the problem of abuse would be alleviated with legislative amendments to give effect to the proposal of empowering the Registrar to act upon a court order directing a defendant company to change its infringing name, and substituting with its registration number if the company failed to comply with the Registrar's direction to change its infringing name. While direct reference had not been made to Mainland regulations in working out the proposal, DS(FS)3 said that there had been informal discussions with the Mainland authorities on the subject. The Administration had invited public views on the proposal during the second topical consultation and received overwhelming support from the respondents.

VII Any other business

59. There being no other business, the meeting ended at 6:48 pm.

Council Business Division 1
Legislative Council Secretariat
23 April 2009