BY FAX AND BY POST
(2528 3345)

Our Ref.: C/EPLM, M27470 14 May 2004

Ms. Shirley Lam,
Financial Services Branch,
Financial Services and the Treasury Bureau,
18th Floor, Admiralty Centre Tower 1,
18 Harcourt Road,
Hong Kong.

Dear Ms. Lam,

Consultation Paper on Statutory Derivative Action in the Companies (Amendment) Bill 2003

I am replying to your letter of 22 April 2004 to Ms. Winnie Cheung, the Society's Chief Executive & Registrar, requesting comments on the *Consultation Paper on Statutory Derivative Action in the Companies (Amendment) Bill 2003*.

The Society is generally supportive of the changes being proposed and has the additional views set out below on the specific Committee Stage Amendments and other issues raised in the consultation paper.

Committee Stage Amendments

Section 168BB

The Society agrees with the introduction of a leave requirement. We do not have any objection to the proposed requirement in section 168BB(3)(d) that, before granting leave to intervene in proceedings under subsection (1)(b), the court has to be satisfied that it is probable that the company will not itself properly take responsibility for those proceedings. If the company is properly dealing with the relevant litigation, or is likely to do so, there seems to be no reason to allow a member to intervene on the company's behalf.

Issues arising from the discussion by the Bills Committee

Co-existence of the common law and statutory derivative actions

There may be some confusion in having two types of derivative action co-existing – common law (CDA) and statutory (SDA) - without any indication in the Bill as to how they might interact where, for example, there are parallel actions by the same shareholder in relation to the same subject matter. It is possible that the co-existence of the CDA and SDA could lead to a multiplicity of suits. However, we also take the point that one of the principal reasons for

introducing an SDA in Hong Kong is because of the disadvantages and practical difficulties associated with the CDA procedure and, in principle, there would seem to be no reason why the CDA should find more favour amongst shareholders in future than it has in the past.

On balance, we believe that it would be useful to include specific provisions in the Bill to deal with the possibility of actions under an SDA and CDA on the same subject matter, but we would also suggest that the proposals in paragraph 12 of the consultation paper are not entirely satisfactory. The proposals in paragraph 12 relate only to the situation in which the same shareholder wishes commences a CDA and an SDA, whereas in practice any restriction imposed on this basis could be avoided by arranging to have the actions initiated by different shareholders: in most cases it is quite likely that there would be more than one shareholder backing a derivative action.

Under the circumstances, we would suggest that consideration be given to either of two possible approaches outlined below.

Option 1

(a) Empower the court to dismiss an SDA if a CDA has been commenced in respect of the same subject matter, regardless of whether the plaintiff in the CDA is the same person as the applicant for the SDA; and

(b) if leave has been granted by the court to commence an SDA, the right of any member to commence a CDA on the same subject should be suspended. That right could, however, be resumed with the leave of the court which granted leave to commence the SDA, where, for example:

- the court is satisfied that the SDA cannot adequately address the relevant grievance; or

- the shareholder who commenced the SDA has lost the action.

Option 2

(c) If, as suggested in the consultation paper, the main concern relates to the position of shareholders of foreign companies controlled by Hong Kong residents and their possible loss of rights, then another option would be to limit the use of CDAs in Hong Kong to actions in relation to foreign companies only.

Conduct of proceedings

With regard to the orders that the court may make or directions that it may give under s168BF, we are unclear why the reference to mediation has been deleted from subsection (1)(b).

In view of the growing international trend to handle commercial disputes through alternative means of dispute resolution, the court should not be precluded from ordering mediation, and we would suggest, therefore, that the reference to the possibility of a direction "requiring mediation" be reinstated.

If you have any questions regarding our comments, please do not hesitate to contact me on 2287 7084.

Yours sincerely,

PETER TISMAN
TECHNICAL DIRECTOR
(BUSINESS MEMBERS & SPECIALIST PRACTICES)

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c.c. Clerk to the Bills Committee on the Companies (Amendment) Bill 2003
(Attn. Ms. Anita Sit) (Fax no.: 2121 0420)