Bills Committee on Companies (Amendment) Bill 2003

Summary of submissions in response to Administration's Consultation Paper on Statutory Derivative Action (SDA) and the Administration's response

(as at 20 May 2004)

I. Requirement to obtain leave to bring SDA and the conditions for granting leave

Name of organizations/individuals	Major views	Administration's response
Securities and Futures Commission (SFC)	In our view, the CSAs to proposed section 168BB(3) could end up producing a "trial within a trial". Given that the purpose of the SDA is to enable greater access to justice for minority shareholders, we remain of the view that there are enough disincentives militating against minority shareholders exercising the SDA without adding a leave requirement. However, if a leave requirement is imposed, this should be as low as possible. SFC suggests, that the leave requirement do no more than track the normal rules for striking out any action e.g. proceedings have not been brought in good faith as in proposed section 168BD(2)(b).	Having regard to the views of various organizations on this issue, we agree to introduce, as proposed by the Bills Committee, a leave requirement, and to lower the thresholds for granting leave as follows – (a) it appears to be prima facie in the interests of the specified corporation that the proceedings be brought, continued, discontinued or defended; (b) the applicant is acting in good faith; (c) if the applicant is applying for leave to bring proceedings on behalf of the specified corporation, there is a serious question to be tried and the specified corporation does not bring the proceedings; (d) if the applicant is applying for leave to intervene in proceedings on behalf of the specified corporation, the specified corporation does not diligently continue, discontinue or defend the proceedings;

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
Securities and Futures Commission (SFC) *(Cont'd)*		(e) except where leave is granted by the court, the member has served a written notice on the specified corporation. We consider that the above thresholds should be able to strike a balance between preventing frivolous actions and not discouraging the use of the derivative action.
The Hong Kong Institute of Company Secretaries (HKICS)	HKICS takes the view that a member should not be required to obtain leave before being entitled to commence an action. With the leave requirement, a member will have to demonstrate that the board's decision was not in fact arrived at bona fide, because that decision will not otherwise be questioned by the court. This will require him to demonstrate knowledge of the board's deliberations and previous correspondence to which he may very well not have access, making his task of seeking leave quite impossible in practice, particularly if he is required under the proposed section 168BB(3)(a) to meet a "best interests of the company" test, a far higher burden than a "prima facie in the interests of the company" test, as in the case of section 216(3)(c) of the Singapore Act. On the other hand, if the company wishes to argue that the action is not in the best interests of the company, all it will need to show is that the board's decision was reached bona fide. Where this is in fact the case, that will be the end of the matter, regardless of whether the decision was commercially sound. HKICS urges the Bills Committee not to introduce its proposed amendment, otherwise the proposed reform will, in HKICS's view, prove a pointless exercise.	See above responses to the SFC's submission. We do not consider that the above revised thresholds would require the member to demonstrate that the board's decision is not in fact arrived at bona fide.

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
Standing Committee on Company Law Reform (SCCLR)	The proposal to put in a leave requirement for the commencement of a SDA would in effect be a "trial within a trial". SCCLR is of the unanimous view that if a leave requirement is considered necessary, the threshold must be set at a meaningfully low level. The thresholds presently set out in section 168BB(3)(a) to (e) should be reviewed, especially the following two requirements - (i) that it is in the best interests of the specified corporation that the applicant be granted leave; and (ii) that the applicant is acting in good faith, which may force the court to enter into the merits of the claims, in cases where there are conflicting evidence and serious dispute of facts.	See above responses to the SFC's submission. As a matter of principle, if a member is not acting in good faith, he should not be allowed to commence an action on behalf of the specified corporation. The problem of conflicting evidence happens in nearly all court cases. The court would be in the same position under the proposed statutory derivative action as it is under any other kinds of action. It would not be in any way worse off.
Mr David Webb	The CSA to introduce a requirement to seek leave to bring proceedings and its several criteria is tantamount to reintroducing the "trial within a trial". If the member bringing the proceedings has to show that the proceedings are brought "in good faith" and "in the best interests" of the company, and that the question is "serious", then that may provoke a detailed analysis of the case before the proceedings can even begin. The "struck out" mechanism in section 168BD is the most appropriate way to handle frivolous, vexatious or nuisance actions. The member should be entitled to the presumption that he is acting in good faith and in the interests of the company until proven otherwise, in line with the common presumption of innocence.	See above responses to the SFC's submission. It is worth noting that the "serious question to be tried" is a standard adopted by courts for assessing interlocutory injunction applications. The phrase means that the derivative claims by the shareholder are not frivolous or vexatious. By this standard, it is not necessary for the purposes of the applicant obtaining the court's leave to show any prima facie case; it is sufficient to show that the proceedings are not frivolous or vexatious.

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
Mr David Webb *(Cont'd)*	The word "best" in the phrase "in the best interests of the specified corporation" would introduce a requirement to show that the proceedings are the best possible course of action having examined all possible courses of action. That would be a time and resource-consuming barrier. There should be no need for the member to show that "it is probable that the specified corporation will not itself bring the proceedings". The fact that the corporation is not bringing such proceedings should be sufficient. As to the condition that there is a "serious question to be tried", it should be up to the defendant to show that the complaint is "not serious". The only criterion that seems to be appropriate if there is a requirement for leave to bring proceedings is to show that notice or such proceedings was given to the specified corporation (except where the court has dispensed with this)	
Mr John Brewer	The proposal that in seeking leave, a shareholder needs to show that the action is in the "best interests of the company" threatens to make life impossible: even if the shareholder could get hold of the evidence he needs, he will have to convince a court that the board of directors did not act bona fide in its decision - a harder task than succeeding with the action he wants the company to pursue. If a shareholder is able to commence an action without leave, the company is still able to apply to have the action struck out if it (i.e. the board) can show that the action is not in the best interests of the company; all it needs to do in order to meet that test is to show that it acted bona fide.	See above responses to the SFC's submission.

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
The Hong Kong Mortgage Corporation Limited (HKMCL)	HKMCL is supportive of the Administration's original arguments for not imposing a leave requirement. The Administration's paper does not elaborate the reasons for the change in instance at the suggestion of the Bills Committee. Hong Kong law and procedure, unlike the United Kingdom, does not contain a requirement for leave to be obtained before commencing a common law derivative action (CDA) (per Godfrey JA in Tan Eng Guan v. Southland Co. Ltd. [1996] 2 HKC 105G.) Accordingly, if the right to take a CDA is permitted to co-exist with the proposed SDA, it will actually be procedurally more onerous for a shareholder to bring SDA proceedings than CDA proceedings. This appears to be anomalous and might have the effect of inhibiting use of the statutory remedy when the intent of the legislation is to facilitate the institution of SDA in order to remedy the shortcomings of the CDA. The condition set out in **section 168BB(3)(d)**, would present a very high hurdle for an applicant to overcome since, not being party to the ongoing litigation, the applicant would no way to find out the progress of the litigation or how it was being (mis)handled. Moreover, it is not clear what standard is required of a company before it can be said to be "properly taking responsibility". It would be helpful if some guidance could be given on how to satisfy this new condition.	See above responses to the SFC's submission.

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
The Association of Chartered Certified Accountants (ACCA)	We concur with the approach that conditions need to be fulfilled in the application for leave of the court. It should be recognized that the question of what are the "best interests" of the company is traditionally a matter of the company's directors to determine. It may not be appropriate for the court to interfere in companies' internal affairs to make such a determination. ACCA recommends including specific conditions that the court should consider before granting the SDA.	See above responses to the SFC's submission. In view of the varying nature of the cases involved, we consider it appropriate to prescribe the general thresholds rather than specific conditions for the court to consider before granting leave for the statutory derivative action.
The Hong Kong Association of Banks (HKAB)	The proposed SDA provisions appear to be very widely drafted and allow a member to bring any proceedings, other than criminal proceedings. For this reason, it seems sensible to require that leave of the Court be granted for such proceedings in order prevent any abuse. However, it has to be recognized that this may also act as a disincentive to legitimate proceedings being taken. One suggestion, therefore, would be to consider limiting in some way the scope of proceedings which may be brought under the SDA (to matters such as fraud, breach of directors' fiduciary duties), and limiting (or removing) the requirements to seek leave from the Court to proceed with the action.	See above responses to the SFC's submission. See responses below to the SCCLR's submission.

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
The Law Society of Hong Kong (The Law Society)	The Law Society does not object to the requirement of obtaining leave from the court. There are, almost invariably, serious allegations contained in a derivative action, and the basis for permitting a derivative action to proceed should go beyond having "a serious question to be tried". There are other factors set out in the section, but, on balance, the reference to "a serious question to be tried" sets the threshold too low. The leading cases on derivative actions, being *Prudential v. Newman* and *Smith v. Croft*, explained why it would be necessary to go above that threshold and require the plaintiff to prove a *prima facie* case. It is acknowledged there are problems under common law and the decision of *Smith v. Croft* has been heavily criticized, but the Bill provides that ratification is not a bar to proceedings. It also appears that the court may well have a wider jurisdiction to order an indemnity of costs. With those enhanced features, it seems prudent to continue with the requirement that a plaintiff has to prove a *prima facie* case.	See above responses to the SFC's submission.
Consumer Council (CC)	CC sees a checking function to be served by the introduction of a leave requirement for a shareholder of a company to commence a SDA and agrees that the striking out mechanism originally proposed will thereby be rendered superfluous. CC shares the concern of the Bills Committee that the threshold "properly taking responsibility for proceedings" in section 168BD(3)(d) may be very difficult to prove. The condition that "there is a serious question to be tried" in proposed section 168BB(3)(c) should constitute a good ground to support granting of leave not just to commence but also to intervene in proceedings and invites the Bills Committee to consider the same, especially since the best interest requirement already in place in section 168BB(3)(a) may well cover the situation envisaged in section 168BB(3)(d).	See above responses to the SFC's submission. Given that the proceedings under the proposed section 168BB(3)(d) are ongoing proceedings, we do not consider it necessary to apply the "serious question to be tried" threshold to such proceedings.

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
The Society of Chinese Accountants & Auditors	The proposed statutory leave requirement of section 168BB subsection (1) will tighten the judicial control of the new statutory procedure. Indeed, uncontrolled access to the remedy could not only burden the company with the costs of bringing the action, at the behest of someone with a relatively minor investment in the company, it could also result in potential directors feeling so vulnerable to be sued that they decline such position. The new conditions in the proposed sections 168BB(3) would provide more guidance to courts as to the appropriate criteria for granting leave, otherwise a hearing to determine whether there was a prima facie case would be almost as long as a full trial.	See above responses to the SFC's submission.
Hong Kong Society of Accountants (HKSA)	HKSA agrees with the introduction of a leave requirement. HKSA does 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.	See above responses to the SFC's submission.
Federation of Hong Kong Industries	The proposed mechanism for avoiding abuse of the process by way of a leave application is considered by us as sensible and essential to the proper functioning of the system.	See above responses to the SFC's submission.

I. Requirement to obtain leave to bring SDA and the conditions for granting leave *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
CPA Australia	We understand the need to maintain a balance of interests and to prevent the institution of frivolous actions. However, the test for granting leave of the court will be very subjective (ref. "good faith", "best interest of the company") and that this test will be applied to a number of criteria which may be difficult to establish by claimants (ref. "probability that the company will not bring proceedings itself", "seriousness of the question to be tried"). It is unlikely that the proposed SDA will open a floodgate of cases. To the contrary, given the significant legal costs and evidentiary difficulties related to qualifying corporate abuse cases for trial under the proposed SDA, the existing drafting of the provisions might be insufficiently "investor-friendly" to encourage bona fide and serious cases of corporate abuse to be instituted.	See above responses to SFC's submission.

II. Scope of proceedings

Name of organizations/individuals	Major views	Administration's response
Standing Committee on Company Law Reform (SCCLR)	While there is a leave application requirement, it is also desirable to restrict the scope of SDA. SCCLR is unanimously of the view that the scope of proceedings actionable under the proposed SDA procedure should be expressly limited to grounds like those expressed in paragraph 15.26 of the Standing Committee's Consultation Paper, which include - • fraud • negligence • default in relation to any law or rules • breach of any duty whether fiduciary or statutory or as recommended by the UK Law Commission in its Report on Shareholder Remedies (No. 246, 1997) which states that the SDA should only be available if the cause of action arises as a result of an actual or threatened act or omission involving (a) negligence, default, breach of duty or breach of trust by a director of the company, or (b) a director putting himself in a position where his personal interests conflict with his duties to the company.	Having regard to the views of various organizations on this issue, we propose, as agreed by the Bills Committee, to restrict the scope of the statutory derivative actions to those proceedings in respect of any fraud, negligence, default in relation to any law or rules, breach of duty in relation to the specified corporation.
Securities and Futures Commission (SFC)	On the policy view of the Administration that "it is not necessary to restrict the types of action that could be brought as derivative actions", SFC points out that an unlimited scope for the SDA would enable a minority shareholder to take action against any third party for a wrong done against a company arising out of contract or tort. The focus should be upon wrongs committed against the company arising out of fraud, negligence, default in relation to any legislation and breach of fiduciary or statutory duty by those controlling the company as suggested by the SCCLR. If the scope is limited, the leave threshold can also be low.	See above responses to SCCLR’s submission.

II. Scope of proceedings *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
The Hong Kong Association of Banks (HKAB)	HKAB suggests limiting in some way the scope of proceedings for the SDA and limiting (or removing) the requirements to seek leave.	See above responses to SCCLR's submission.
The Hong Kong Mortgage Corporation Limited (HKMCL)	HKMCL has no comment on the Administration's decision not to restrict the types of wrongs in respect of which action may be brought under the SDA and considers that these are matters which can be dealt with by the trial judge.	See above responses to SCCLR's submission.
The Law Society of Hong Kong (The Law Society)	As the intention is to abolish the requirement that the plaintiff must prove himself within the exceptions of *Foss v Harbottle*, it would seem not necessary to restrict the types of corporate wrongs that may be the subject of a SDA. That said, the emphasis must be on corporate wrongs and a SDA should not be permitted where a member disagrees with the management's business judgment or decisions provided that such judgments or decisions are made in good faith.	See above responses to SCCLR's submission.
Consumer Council	The criteria to be satisfied for leave to be granted as set out in section 168BB(3) will have restricting effect and it is not necessary to restrict the types of action that could be brought as derivative actions.	See above responses to SCCLR's submission.
CPA Australia	The proposed SDA does not solve the key criticism that such shareholder suits take a long time and are costly. As the shareholder is required to finance the suit until the matter is finally decided, there are still few new incentives for claimants to take action under the proposed SDA.	Under the proposed section 168BG, the court may, at any time, make an order as to costs of the statutory derivative actions.

III. Co-existence of common law derivative action (CDA) and SDA

Name of organizations/individuals	Major views	Administration's response
The Hong Kong Mortgage Corporation Limited (HKMCL)	HKMCL agrees with the Administration's position that the right to commence a CDA should be preserved. There is no reason to deprive shareholders of non-Hong Kong companies of rights that might otherwise be available to them and there are already adequate remedies under the current civil procedure rules to deal with a duplicity or multiplicity of proceedings.	We remain the view that it appears unlikely that a member would take two derivative actions respectively under common law and the statute, given that the damages, if any, obtained in the derivative action would go to the specified corporation and the member may be exposed to two sets of costs. That said, having regard to the views of various organizations on this issue, we propose to empower the court to deal with the co-existence or duplicity of a statutory derivative action and a common law derivative action as follows - (a) Add a new section to empower the court to dismiss an application for leave to commence a statutory derivative action if a common law derivative action has been commenced by the same member in respect of the same subject matter; (b) Add a new section to empower the court to prevent a member from commencing a common law derivative action if leave has been granted to the same member to commence a statutory derivative action in respect of the same subject matter; and (c) Add a new section to empower the court to make any order and give any direction it considers appropriate in relation to items (a) and (b) above.

III. Co-existence of common law derivative action (CDA) and SDA *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
The Hong Kong Mortgage Corporation Limited (HKMCL) *(Cont'd)*		Under this proposal, the court will be given the necessary power on how the issue of co-existence or duplicity should be best dealt with in the interest of justice, having regard to the relevant circumstances of the case.
The Law Society of Hong Kong	The only reason given for allowing common law derivative action and statutory derivative action to co-exist is that "there may be different rules of internal management in the law of the place of incorporation compared with those applying to Hong Kong incorporated companies". The rationale is unclear bearing in mind the Bill applies to non-Hong Kong companies. The SDA is a procedural remedy for corporate wrongs done, and if corporate wrongs (including those about internal management) have been committed, why would an SDA-only approach take away common law rights and prejudice shareholders? Indeed, a SDA would assist by providing the member with a right of redress not otherwise available, as the member is no longer required to prove himself within the exceptions to the rule in *Foss v Harbottle* and ratification will no longer itself be a bar to commencing proceedings.	See above responses to submission from HKMCL. We agree that the statutory derivative action would provide the member with a right of redress not otherwise available as the member is no longer required to prove himself within the exceptions to the rule in Foss v Harbottle. That said, if we abolish the common law derivative action in Hong Kong, we would deprive a member of his right to bring a derivative action under common law in Hong Kong. In considering whether the common law derivative action should be abolished in Hong Kong with the introduction of the statutory derivative action, we would like to avoid possible scenarios when a member might be deprived of the opportunity to bring a common law derivative action in Hong Kong to enforce the rights which are available under the law of the place of its incorporation.

III. Co-existence of common law derivative action (CDA) and SDA *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
The Law Society of Hong Kong (The Law Society) *(Cont'd)*	*Konamaeni v Rolls-Royce* referred to in paragraph 8 of the Consultation Paper is not about a SDA. It may perhaps also be relevant to note that the Indian connection in that case (including the bribery charges etc.) were evidently significant as a result of which the proper forum was considered to be India rather than England. In contrast, foreign-incorporated companies that are listed in Hong Kong clearly have a strong Hong Kong connection but have basically no business activities in their place of incorporation. The same comment also applies to foreign companies (such as those incorporated in the BVI) used by private businesses. It is important for the Bill to set out clearly how a derivative action should be conducted. Allowing for SDA and SDA to continue concurrently is an unnecessary complication that is likely to result in derivative actions becoming more costly.	
Standing Committee on Company Law Reform (SCCLR)	The problems and concerns raised by the Administration in paragraph 8 of the Consultation Paper can be addressed by conferring jurisdiction on the Hong Kong court to deal with SDAs by members of unregistered companies, if those companies have substantial connection with Hong Kong. Under Part X, section 327 of the Companies Ordinance, the court has the power to wind-up unregistered companies if the companies have sufficient nexus with Hong Kong. The same should be applied to SDA cases. On the basis of SCCLR's other recommendation as set out above, SCCLR does not see the need for a co-existing CDA.	See above responses to submission from HKMCL. As in the case of section 168A on unfair prejudice remedies, we would need to consult relevant stakeholders before taking a decision on whether the statutory derivative action should also apply to unregistered companies and that this issue would be best dealt with in the next exercise of amending the Companies Ordinance.

III. Co-existence of common law derivative action (CDA) and SDA *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
W H Lam & Company	An amendment should be introduced to proposed section 168BB(4) to abolish a shareholder's common law right to commence a CDA if leave has been granted to the same shareholder to commence a SDA in respect of the same subject matter, vice versa. The suggestion for empowering the court to dismiss a shareholder's application for leave to commence a SDA if a CDA has been commenced by the same shareholder in respect of the same subject matter is rather time consuming and disputes may arise in finalizing the court decision.	See above responses to submission from HKMCL.
Consumer Council	A SDA subject to a leave requirement should serve to make available an additional option so that a shareholder can have the choice of whether to resort to SDA or bring a CDA. However, co-existence should be allowed only up to the point when the form of action is settled on. Thereafter measures should be in place to prevent duplicity of proceedings on the same subject matter. CC therefore supports the proposed amendments set out in paragraph 12 of the Consultation Paper.	See above responses to submission from HKMCL.
The Society of Chinese Accountants & Auditors	The term "same shareholder" in paragraph 12(a) and (b) of the consultation paper should be defined more clearly and concisely for this purpose, particularly when there is no provision made for a parent company to bring a derivation action on behalf of a subsidiary or associate within the group.	See above responses to submission from HKMCL. We would use the same “member” instead of the same “shareholder’ in the Bill. The term “member” is defined under section 28 of the Companies Ordinance to mean a shareholder whoses name is in the register of members.

III. Co-existence of common law derivative action (CDA) and SDA *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
Hong Kong Society of Accountants (HKSA)	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. 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 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. HKSA suggests that consideration be given to either of the following two approaches - <u>Option 1</u> (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 CD 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: (i) the court is satisfied that the SDA cannot adequately address the relevant grievance; or (ii) the shareholder who commenced the SDA has lost the action.	See above responses to submission from HKMCL. As a matter of principle, we do not see any basis in depriving a member's rights to commence a derivative action (whether it is taken under common law or statute) simply because another member has commenced the action or vice versa.

III. Co-existence of common law derivative action (CDA) and SDA *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
HKSA *(Cont'd)*	Option 2 (c) If 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.	

IV. Conduct of proceedings

Name of organizations/individuals	Major views	Administration's response
Standing Committee on Company Law Reform (SCCLR)	SCCLR agrees that the powers conferred on the court under proposed section 168BG(1)(c) should be wide enough to enable it to deal with any problem relating to discovery of documents. It may be even better, however, if there is a specific provision to that effect.	Having regard to the views of various organizations on this issue, we propose to amend the proposed section 168BF(1)(c) to make it clear that the court may make an order directing the specified corporation or its officers to provide information or assistance in relation to the statutory derivative action.
The Hong Kong Mortgage Corporation Limited (HKMCL)	HKMCL agrees that issues relating to discovery can be dealt with under the current framework for discovery.	See above responses to the SCCLR's submission.
Consumer Council	The powers proposed in the Bill should be sufficient to address the concerns with respect to the conduct of proceedings.	See above responses to the SCCLR's submission.
The Society of Chinese Accountants & Auditors	Section 168BF gives the court wide power to make whatever orders it thinks fit regarding the conduct of the proceedings, including matters such as the provision of information and assistance to the applicant by the company or its directors. Our only comment here is to hope the court will exercise such powers prudently to avoid the decision being overturned on appeal.	See above responses to the SCCLR's submission.

V. Others

Name of organizations/individuals	Major views	Administration's response
Office of the Privacy Commissioner for Personal Data, Hong Kong (PCO)	Proposed section 168BF(1)(c) is one of the channels through which information or documents which involves personal data may be discovered. Also, it is likely that information or documents containing personal data may be collected, retained or used by the independent person appointed by court pursuant to proposed section 168BF(1)(d) for the purpose of investigating and reporting on matters related to the specified corporation. From the perspective of personal data protection, due regard should be give to the requirements of the Personal Data (Privacy) Ordinance, Cap 486 ("the Ordinance") on the collection, holding, processing or use of the data. Whilst proposed sections 152FA to 152FE have clearly provided for the permitted purposes of use of these information and documents and the need to comply with the requirements of the Ordinance, such are not found in section 168BF(1)(c) and (d). In the interest of clarity, it may be appropriate to reconsider the drafting of section 168BC(1)(c) and (d).	We propose to add a new provision along the following lines to enhance the protection of the personal data obtained under the proposed section 168BF - "Nothing in sections 168BF(1)(c), (d) and (2) shall authorize the collection, retention or use of personal data in contravention of the Personal Data (Privacy) Ordinance (Cap. 486).". However, we do not consider it necessary to go so far as to prescribe the uses of the information and documents which should be best dealt with by the court.
The Hong Kong Association of Banks (HKAB)	As the SDA will have to be brought in the name of the company, and as the member must bear the risk of absorbing the costs of the action, we question to what extent such a provision will be used. The Bills Committee has already highlighted the difficulty, for example, of establishing that the company will not itself bring the proceedings or properly take responsibility for them when seeking the Court's leave to proceed, and we agreed with these concerns.	Noted.

V. Others *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
Standing Committee on Company Law Reform (SCCLR)	Research SCCLR considers that some research ought to be undertaken as to - (a) how the SDA has fared in Singapore and in Australia; and (b) whether information is available from the HK Judiciary as to the number of derivative actions in the past, and whether there is any basis for concern that the procedure would be abused.	Since the introduction of the statutory derivative action in Singapore and Australia in 1993 and 2000 respectively, there are only very few cases in which the action is invoked. Hence, there is not much information on how the action fares in Singapore and Australia save for the information that has been provided to the Bills Committee before. We are not aware of any concern about the abuse of common law derivative action. We have also checked with the Judiciary and they do not have any statistics on derivative actions.
W H Lam & Company	Section 168BC - Service of written notice The wording of section 168BC(2)(a) - "in the case of a company, its registered office;" be amended to read - "in the case of a Hong Kong incorporated company, its registered office;" to avoid any confusion in interpreting the meaning of "a company" in this section.	We do not consider that there is a need to replace "company" with "Hong Kong incorporated company" as the former has been defined under section 2 of the Companies Ordinance to mean a Hong Kong incorporated company.

V. Others

Name of organizations/individuals	Major views	Administration's response
Mr David Webb	<u>Members-only kills the Bill?</u> One thing you appear to have completely overlooked is the investor ownership system of companies listed in Hong Kong. This oversight results in a Bill which is of no real use to investors, but it can be rectified. <u>Members-only kills the Bill?</u> *(Cont'd)* The investing public including both institutional and retail investors, hold almost all their shares through banks, brokers and custodians, and it some cases through "investor participant" accounts, and in each case these banks, brokers, custodians and investor participants hold the shares in accounts with the Central Clearing and Automated Settlement System (CCASS) operated by Hong Kong Securities Clearing Company Limited (HKSCC), a wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited (HKEx). HKSCC in turn holds all of these shares through a single registered shareholder, HKSCC Nominees Limited (HKSCCN). So for most investors, they are not "members" of any listed company in the legal sense, because the registered holder of their shares is HKSCCN.	At common law, a derivative action is brought by a member rather than by someone who is beneficially interested in the shares. We do not consider it necessary to depart from the common law principle in this regard. If a person is beneficially interested in the shares and would like to bring a statutory derivative action, that person may request that the shares be transferred into his own name before any action is to be taken.

V. Others *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
Mr David Webb *(Cont'd)*	This gives rise to a practical problem. If an investor (institutional or retail) wishes to bring an action under the proposed SDA, then he has no standing to do so. Mr Webb strongly urges that the law should provide not just for a "member" to bring proceedings, but for "any member or person beneficially interested in the securities of the specified corporation at the time of the alleged wrong-doing". The SCCLR's July-01 consultation paper on SDAs spoke of "shareholders" rather than "members", leaving it unclear whether they meant to include beneficial shareholders, but the Bill's drafting speaks only of members, and that is a potentially fatal flaw. <u>Scripless</u> In view of the slow progress of the work on developing a scripless securities market in Hong Kong, Mr Webb envisages that within the next 5-10 years, there is no material chance of having a system in which CCASS Participants are recognized in law as "members" of a company holding scripless shares. They will remain as customers of a nominee, HKSCCN, which for most investors will be the only member with legal standing to bring SDAs.	As regards the concerns about the scripless, they would be dealt with separately as they fall outside the scope of the Bill.
Hong Kong Society of Accountants	<u>Proposed CSAs to delete section 168BF(1)(b)</u> 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.	In response to a submission made by Mr Winston Poon, SC and, as agreed by the Bills Committee, we agree that “mediation” in the proposed section 168BF(1)(b) can be deleted.

V. Others *(Cont'd)*

Name of organizations/individuals	Major views	Administration's response
Federation of Hong Kong Industries	We support the Government's proposed amendments to the Bill as laid down in the present form in the consultation paper, and trust that the introduction of SDA will help improve Hong Kong's corporate governance.	Noted.
CPA Australia	The proposed SDA will not be a remedy for minority shareholders seeking direct compensation. It will not solve the bulk of the needs for legal protection of minority shareholders in Hong Kong (e.g., does not allow the sharing the risk of litigation within other aggrieved parties, does not expedite legal proceedings, does not ease the proof of shareholder cases). The proposed SDA will not apply to companies incorporated outside Hong Kong. This is a serious limitation given the number of private and listed companies operating in Hong Kong which are incorporated in the British Virgin Islands (BVI) and other jurisdictions where there is no SDA.	Derivative actions are applicable to cases where a wrong has been done to a company and are thus, by their nature, not to be used for seeking direct compensation for shareholders. As regards other concerns such as case management, multi-party litigation, they should be dealt with in the context of the civil justice reform as they fall outside the scope of the Bill. The proposed statutory action will also apply to non-Hong Kong companies registered under Part XI of the Companies Ordinance. As regards other unregistered companies incorporated outside Hong Kong, we would need to consult relevant stakeholders, as in the case of section 168A on unfair prejudice remedies, before taking a decision on whether the statutory derivative action should also apply to unregistered companies and that this issue would be best dealt with in the next exercise of amending the Companies Ordinance.