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

Dear Mr Au,

Thank you for your e-mail and the attachments with a summary of comments, your responses, and your proposed redraft of the relevant sections.

My further comments are as follows:

Leave requirement and Scope Limitation

It seems that in relation to the imposition of a leave requirement, the FSTB has done very little to address the majority of views expressed in response to your consultation. The SFC, HKICS, SCCLR, HKMC, CPA Australia, Mr John Brewer and myself all responded to the effect that it would be wrong to reintroduce the "trial within a trial" by imposing the leave requirement.

Given that the SCCLR proposed the SDA in the first place, and that this received support in its public consultation, you would do well to listen more carefully to the advice of the SCCLR.

The HKMC points out that a common law derivative action does not contain a leave requirement, so it will be procedurally more onerous to bring an SDA than a CDA if you introduce the leave requirement. The HKAB suggested restricting the scope of the SDA **rather than** imposing a leave requirement.

Instead, the FSTB is now proposing not only to impose a leave requirement but also to restrict the scope of complaint - what might be termed a "belt and braces" approach. **I would be in favour of restricting the scope as proposed ONLY IF you drop the leave requirement.**

If, as you now propose, a plaintiff has to prove a *prima facie* case, before receiving leave to bring the action, then as the law society says (in supporting it), this requirement is a higher hurdle than showing that there is "a serious question to be tried". It will introduce the "trial within a trial" or more accurately, the "trial before the trial".

I reiterate that it was sufficient in the original draft to provide a mechanism for the action to be struck out by the court, and that the onus should be on the alleged wrong-doers to prove the applicant's bad faith, or to show that the action is frivolous or vexatious if they do not wish to face a trial. It is unreasonable to expect the applicant to prove a negative.

This is a question of form over substance. It is not enough for Hong Kong to be seen by the World to introduce a statutory right of derivative action - it will be a subject of ridicule if that right is in practice unusable, because vested interests succeed in building an impermeable barracade around the court. Even without the CSAs, an applicant is already subject to the difficulties that (1) he might have to run up huge costs unless the

court sees fit to make an order for costs while the trial is in progress (this cannot be depended upon at the outset); and (2) if the case is successful, the damages will be payable to the company, which may still be controlled by the proven wrong-doers.

Members-Only

Finally, you have dismissed by suggestion that beneficial owners of shares (who are not members) should have the right to bring an SDA, and you maintain that it should be members-only. You suggest in response that a beneficial owner could transfer shares into his own name in order to bring the action.

Question 1: Would you then please confirm that, as a matter of law, it does not matter if the member bringing the action was not a member of the company at the time of the alleged wrong-doing against the company?

If that is correct, then I accept your response. But if the applicant must have been a member at the time of the alleged wrongdoing then clearly your response is invalid, because it would be impossible for people who were (at the time of the wrong-doing) beneficial owners to travel back in time and instead become registered members at the time of the wrong-doing.

Furthermore, I note that at paragraph **15.25** of the SCCLR Phase 1 Consultation, it was proposed that the SDA be available to **"Shareholders, directors and officers of the company, past or present...Past shareholders may, however, only take the action insofar as the act complained of arose while they held shares in the company." (emphasis added)**

So **Question 2:** what happened to the idea that past or present directors and officers could also bring the action; and **Question 3:** does the SCCLR report imply that becoming a member after the alleged wrong in order to bring an action is not permitted?

Regards

David Webb

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