Submission to the Financial Services and Treasury Bureau of the Hong Kong SAR Government on the Rewrite of the Companies Ordinance

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Executive Summary

This is a submission by Oxfam Hong Kong (OHK) concerning the Rewrite of the Companies Ordinance ("CO") as outlined in *the Consultation Paper: Draft Companies Bill, Second Phase Consultation* issued during May 2010.

The rewrite of the CO by the Financial Services and Treasury Bureau of the Government of the HKSAR is intended to update and modernise it, to make it more user-friendly and facilitate the conduct of business to enhance Hong Kong's competitiveness and attractiveness as a major international business and financial centre.

As noted in the *Consultation Paper: Draft Companies Bill, First Phase Consultation* (December 2009), one of the fundamental ways to ensure these aims is through the enhancement of corporate governance.

Enhancing corporate governance is understood by the Financial Services and the Treasury Bureau as enhancing transparency and accountability with companies' operations, as well as providing greater opportunity for all shareholders to engage in company business in an informed way.[1]

The ways in which this could be achieved, with relevance to this submission, include the following:

- Codification of the standard of directors' duty of care, skill and diligence
- Improved disclosure of company information
- Enhancing shareholders' engagement in the decision-making process[2]

OHK supports the rewrite of the CO, and believes that many of the proposed new clauses advance the case for transparency of non-financial information and the necessity of companies to be responsible for their social and environmental performance. As the consultation paper highlighted, this is in line with international trends to promote CSR.

OHK believes strengthening corporate governance and corporate social responsibility will bring the framework under which the business sector operates in Hong Kong into line with maturing public and stakeholder expectations about the roles, responsibilities and conduct of business in society. It is also recognised that companies will only succeed in creating long-term shareholder value if they manage

[1] *Consultation Paper: Draft Companies Bill, First Phase Consultation*, p. 2.

[2] *Consultation Paper: Draft Companies Bill, First Phase Consultation*, p. 2.

their relationships with employees, suppliers, customers and others who have a legitimate interest in the company's activities.

As the Hong Kong SAR Government has already demonstrated in its rewrite of the Companies Ordinance, the UK Companies Act 2006 (UKCA) provides relevance for the Hong Kong context. For instance, the rewrite of the Companies Ordinance currently includes articles from section 417 of the UKCA on the contents of directors' reports. OHK endorses the view that the UKCA's support of CSR is a strong model for Hong Kong to adapt to local conditions. The UKCA provides excellent guidance on the enhancement of corporate governance, and by association non-financial disclosure and the broader issue of corporate social responsibility (CSR).

However, OHK notes that although the rewrite of the Companies Ordinance has drawn heavily from section 417 of the UKCA, it has done so by selectively deleting or altering significant portions of the UKCA pertaining to CSR. The most glaring case of this is the failure to include section 172 of the UKCA, which in the UKCA is a mutually reinforcing component of section 417.

OHK believes, therefore, that section 417 on the contents of directors' reports cannot be considered in isolation from the general duties of directors, as contained in section 172. OHK does not believe it makes sense to incorporate parts of section 417 of the UKCA into the draft Companies Bill whilst at the same time ignoring section 172. The two sections of the UKCA are mutually reinforcing. Enhanced reporting is good in any context, but more powerful in conjunction with appropriate directors' duties.

OHK believes, therefore, that the rewrite of the CO must include a statutory statement of directors' duties like section 172 of the UKCA. Section 172 clarifies that the issues that affect a company's operations and value, and which should therefore be taken into account by directors, are necessarily complex and must be weighted carefully against each other. This reflects reality, and to ignore that is to encourage a narrow view of directors' duties.

Section 172 clarifies the role of directors. It states that directors are expected to weigh up these factors in the best interests of the company, and that these factors be given proper consideration; that is, be given appropriate weight in the context. We strongly believe it is better to give clear instructions to directors to take account of the wider business factors than to leave it implicit or unclear.

A statutory statement of directors' duties will provide certainty for business by levelling the playing field so that socially and environmentally responsible companies are not disadvantaged in the market by competing against those for which such issues are only impediments.

For the reasons set out in this submission, OHK's recommendations are as follows:

- Directors duties (as outlined in section 172 of the UKCA) and company reporting (as outlined in section 417 of the UKCA and in Chapter 9 of the CO rewrite) are mutually reinforcing, and it is not sufficient to have one without the other.

- The CO must include clarifications requiring directors, as part of their duty to the company, to consider the company's social and environmental impacts (as, for example, is stipulated in section 172 of the UKCA).

- Stakeholders must have access to relevant information to be able to assess the fulfilment of this duty. The CO rewrite must include substantially more wording from section 417 of the UKCA to ensure improved transparency and disclosure on environmental and social issues.

- The disclosure of non-financial corporate data should be based on the Global Reporting Initiative's Reporting Framework and Sustainability Reporting Guidelines and made mandatory to include the impacts of the company operations on employees or the workplace, environment, supply chain, community and other diverse stakeholders.

- Apart from the CO rewrite, OHK has high expectations that the HK SAR Government will take the lead to promote CSR in Hong Kong in consultation with key stakeholders and the business community.

- The Government should adopt a long-term strategy on CSR and create incentives for companies to strengthen CSR, such as through organising promotional campaigns, reviewing internal and external government policies in favour of CSR, prioritising companies with good CSR in the tendering process for public projects, as well as providing funding and other support for CSR awareness-raising programmes, research and training for small and medium-sized companies.

Introduction

OHK supports the rewrite of the CO, and believes that many of the proposed new clauses advance the case for transparency of information and the necessity of companies to be responsible for their social and environmental performance. This is in line with international trends to promote CSR.[3]

OHK supports the enhancement of corporate governance as conceived in Chapter 9 of the *Consultation Paper: Draft Companies Bill, Second Phase Consultation* – specifically Clauses 9.29 and 9.31 – which stipulates:

> Companies (except for those qualified to apply the simplified accounting and reporting requirements) are required to prepare, as part of the directors' report, a business review which is more analytical and forward-looking than the information currently required. The proposed business review is similar to the business review which all companies (except small companies) in the UK have to include in their directors' reports under section 417 in the UKCA 2006.[4]

OHK believes all companies bear a moral and social responsibility and require a 'social licence to operate' in society. We actively encourage and engage with companies to be more transparent in matters relating to social and environmental performance, and promote international best practice in CSR matters for Hong Kong companies.[5] We understand that there is a clear link between how companies manage activities that have an impact on the community and the environment and OHK's belief that respect for the environment, equal opportunities and human rights will help lift people out of poverty (OHK's prime mission).

Currently, there is no mandatory requirement for companies to report on their CSR performance in Hong Kong, but an increasing number of companies voluntarily publish some form of CSR or sustainability report.[6]

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[3] The requirement for business reviews to include information relating to environmental and employee (social) matters – and the view that this is in line with international trends to promote CSR – is outlined in *Consultation Paper: Draft Companies Bill, Second Phase Consultation*, p. 105.

[4] *Consultation Paper: Draft Companies Bill, Second Phase Consultation*, pp. 104-5.

[5] See, for example, OHK's *Transparency Report* and *Transparency Report II* (related to the Hong Kong apparel industry), OHK's *Good Fashion: A Guide to Being an Ethical Clothing Company*, and OHK's *Survey of Hang Seng Index (HSI) Constituent Companies* (which rates HSI companies on their CSR performance).

[6] CSR reports are also called sustainability reports, CR reports, CSER reports, corporate citizenship reports, EHS reports, and so on. The names are interchangeable and refer to reporting on social and environmental issues.

CSR reporting did not meaningfully exist 20 years ago anywhere in the world. The first documents were published in 1990 and 1991 in the form of environment, health and safety reports. Reports on social and environmental performance began to be issued in the mid-1990s, and the first true CSR reports were issued at the end of the decade.

In 2010, it is likely that over 3,000 companies world-wide will issue CSR reports. In Asia, the numbers are low, but rising quickly. In ASEAN, over 120 companies are producing CSR reports.[7] In China, the number of reports has increased significantly after reaching a tipping point in 2006, when the number of reports published exceeded the total number from all years combined. In 2007, 77 companies in mainland China published CSR reports, over 120 published reports in 2008,[8] and 533 were published in 2009 (partly resulting from mandatory requirements for state-owned enterprises to issue CSR reports).[9] In Hong Kong, 57 per cent of Hang Seng Index Constituent Companies issued a stand-alone CSR report in 2009 and 40 per cent of companies are reporting according to the Global Reporting Initiative (GRI) guidelines.[10]

The rise in (mostly voluntary) CSR reporting has been accompanied by a greater enthusiasm for governments and regulators globally to issue guidelines encouraging companies to report or regulations making it mandatory. Some examples of this include:

- **China**: the State-owned Assets Supervision and Administration Commission of the State Council (SASAC) issued a directive in 2008 stating that state-owned enterprises must improve their CSR management systems and release CSR reports. The Shenzhen Stock Exchange issued CSR guidelines for listed companies in early 2006 and has followed this through with training programmes, whilst the Shanghai Stock Exchange introduced equivalent measures in mid-2008 in the form of the “Shanghai CSR Notice” and the “Shanghai Environmental Disclosure Guidelines. Both guidelines have opted for voluntary disclosure of environmental and social information. The China Banking Association issued guidelines for banking financial institutions in 2009, which encourages the submission of a CSR report every year.

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7 ACCA, *Sustainability Reporting: The Rise of the Report and the Regulator*, (Singapore: ACCA, 2010), p. 1.

8 Guo Peiyuan, *et. al.*, *A Journey to Discover Values 2008: Study of Sustainability Reporting in China*, (Beijing: SynTao, 2008), p. 6.

9 SynTao, *Jiazhi faxian zhilu zhongguo qiye kechi xufa zhan baogao yanjiu* [*A Journey To Discover Value: Research On Sustainability Reporting In Chinese Companies*],(Beijing: Syntao, 2010), p. III.

10 *Corporate Social Responsibility Survey of Hang Seng Index Constituent Companies 2009*, (Hong Kong, OHK, 2010), p. 14.

- **Taiwan:** regulators require all listed companies to include CSR reporting in the corporate governance statement of the annual report and prospectus, including information on the company's CSR system, measures adopted and related performance.
- **Denmark**: Since December 2008, the largest 1,100 companies must include information on CSR in their annual reports.
- **Sweden**: State-owned companies have been required to produce annual sustainability reports in accordance with Global Reporting Initiative guidelines since 2009.
- **France**: In 2001, France was the first country to make public company reporting on environmental and social issues mandatory. The new economic regulations (the "NER" Act) requires public companies to include information on a series of topics in their annual report: status of employees, mobility of staff, work hours, social relations, health and safety, training, health policy, profits distribution and the amount of outsourcing. They must also describe their behaviour when it comes to communities who are concerned by their activities in the countries where they have offices.
- **Japan**: Specified corporations have been required to publish an annual environment report since 2005 (currently standing at 700 reports, or around 40% of listed companies).
- **Malaysia**: Since 2008, Bursa Malaysia (the Malaysian stock exchange) has required all publicly listed companies to publish corporate social responsibility information in annual reports.

Perhaps the most significant legislative act occurred in the UK when the Government oversaw the rewriting and passing into law of the new UKCA, which has been referred as the biggest reform of UK company law for 150 years. Two of the revisions are of specific interest here: i) non-financial reporting and ii) directors' duties.

The proposed draft Companies Bill has included part of a section of the UKCA (section 417), but does not include anything from section 172 of the UKCA, which introduces directors' duties closely linked to non-financial reporting.

Therefore, changes to the CO that incorporate parts of section 417 but do not include key points from section 172 will address only partially the issue of transparency. The progress made in the rewrite of the CO should not be put at risk by a partial change that alone will not meet the objectives set by the Government.

Moreover, the partial selection from section 417 does not fully meet objectives aimed at facilitating the conduct of business to enhance Hong Kong's competitiveness and attractiveness as a major international business and financial centre.

OHK's position

1. The importance of taking a holistic approach to reform

The UKCA is the basis for requirements in the CO rewrite related to non-financial disclosure. It is therefore appropriate to examine the reasoning for including the two interlinked sections (417 and 172).

Many years of consultation were required in the UK to prepare the ground for changes to the Companies Act. A brief overview of that process is useful to underscore why section 417 and section 172 are mutually reinforcing.

The consultation process encompassed themes as wide ranging as 'enlightened shareholder value' and 'pluralism'. The *Strategic Framework Consultation Document* that resulted from the consultation process notes discussions related to key legal rules defining the functions, powers and obligations of shareholders and directors in the operation and control of companies. These discussions led – and were interpreted as "a fundamental step" – to examining the issue of 'scope (i.e., "for what purposes and in whose interests should companies be run?").

The issue of scope led to discussions about, among others, "the place of transparency – in particular what information must be made available in companies and more widely, if these roles are to be carried out effectively.[11]

Central to the issue of scope were – as described in the UK Government's *Company Law Review*:

> two central proposals on directors' duties and on transparency [i.e., sections 172 and 417]. **These two proposals support each other**. They are designed to embrace a wider range of interests than is currently typically recognised as being within the law with the aim of reflecting the needs of companies and new concepts of value in the modern economy – and thus securing competitiveness.[12]

The explicit link formed during the consultation process was between:

I. clarifying directors' duties to include responsibilities to understand the company's impact on social and environmental aspects and vice versa; and
II. giving them and other stakeholders relevant information to be able to assess their fulfilment of this duty

[11] *Company Law Review*, p. 7. Retrieved from: http://www.berr.gov.uk/files/file23248.pdf
[12] *Company Law Review*, p. 7. Retrieved from: http://www.berr.gov.uk/files/file23248.pdf

This is made clear in the following quote from the UK Government's *Company Law Review*:

> The key components are the inclusive duty and broader accountability, in particular the inclusive operating review in the case of companies with real economic power. These both highlight the need to have due regard to the company's business, and wider external, relationships. **They are mutually reinforcing**. The proposed statement of directors' duties requires directors to act in the collective best interests of shareholders, but recognises that this can only be achieved by taking due account of wider interests. The transparency element provides the information needed to underpin this approach to governance. Just as importantly, we believe that this wider reporting requirement – particularly for large companies – will be an important contribution to competitiveness. Companies are increasingly reliant on qualitative and intangible, or "soft", assets such as the skills and knowledge of their employees and their corporate reputation. The reporting framework must recognise this and ensure that companies provide the markets and other interests with the information they need to understand companies' business and assess performance.[13]

OHK is therefore concerned that these two 'mutually reinforcing' aspects may be considered in a segregated manner that will not lead to the outcomes for the CO rewrite as envisaged by the Government.

Of further concern is the selective usage of section 417. The CO rewrite has only utilised a portion of section 417, and OHK believes this detracts from the overall objective of enhancing business competitiveness through increased transparency and disclosure.

It is noted that although section 9.31 of the draft Companies Bill – "Contents of directors' report: business review" – is based on section 417 of the UKCA, it is significantly shorter than section 417. The shortening and editing of section 417 has altered its original intent. There are three key changes in which alterations should be particularly noted:

1. In the UKCA, the explicit link between section 417 and section 172 is made clear in section 417:

   > 417(2) The purpose of the business review is to inform members of the company and help them assess how the directors have performed their duty under section 172 (duty to promote the success of the company).

[13] *Company Law Review*, p. 15. Retrieved from: http://www.berr.gov.uk/files/file23248.pdf

However, section 9.31 of the draft Companies Bill deletes this crucial clause, thereby losing the fundamental objective of section 417.

2. One of the key objectives of the UKCA is that it explicitly requires companies to analyse their performance with reference to the main trends and factors likely to affect their business. The article in section 417 where this idea is most clearly articulated is as follows:

> 417(5) In the case of a quoted company the business review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include—
>
> (a) the main trends and factors likely to affect the future development, performance and position of the company's business; and
>
> (b) information about—
>
> (i) environmental matters (including the impact of the company's business on the environment),
>
> (ii) the company's employees, and
>
> (iii) social and community issues,
>
> including information about any policies of the company in relation to those matters and the effectiveness of those policies

The draft Companies Bill has taken a part of section 417 (5), but reworded it in such a way as to provide no explicit request that companies analyse their performance with reference to trends and factors likely to affect their business. That is, the business case for the collection and disclosure of information related to its impact on society and the environment has been completely discarded. Thus, section 9.31(3) of the draft Companies Bill (based on section 417(5)) currently stands as follows:

> 9.31(3) To the extent necessary for an understanding of the development, performance or position of the company's business, a business review must include –
>
> (a) an analysis using financial key performance indicators;
>
> (b) a discussion on –
>
> (i) the company's environmental policies and performance; and
>
> (ii) the company's compliance with the relevant laws and regulations that have a significant impact on the company; and
>
> (c) an account of the company's key relationships with its employees, customers and suppliers and others that have a significant impact on the company and on which the company's success depends.

OHK believes the change in wording is of concern. As shown above, the UKCA requires companies to review the main trends and factors likely to affect the future development, performance and position of the company's business and *provide information* about environmental matters (including the impact of the company's business on the environment), the company's employees, and social and community issues. However, the Hong Kong draft Companies Bill simply requires companies include a mere discussion (not *information*, as is required in the UKCA) on environmental policies and performance (and no requirement for information on impact), and 'an account' (once again, there is no requirement for *information*) of key relationships with stakeholders.

Section 9.31(3) of the draft Companies Bill does not make a case to business that reviewing trends and factors related to environmental and social issues is i) a growing requirement from stakeholders and ii) makes good business sense.

Finally, requiring companies to provide a discussion of their compliance with relevant laws (as indicated in section 9.31(3)(bii)) that have a significant impact on the company appears to set the bar for non-financial disclosure very low indeed.

3. Finally, the deletion of article 417(6)(b) once again prevents an explicit understanding that key performance indicators related to environmental and social performance are essential in a business review. The UKCA makes this explicit.

    417(6) The review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include—

        (b) where appropriate, analysis using other key performance indicators, including information relating to environmental matters and employee matters.

Without these three key sections, the need for business to report on environmental and social matters that have a bearing on the promotion of company success is far too limited.

Sections 417 and 172 are mutually reinforcing, and it is essential that more wording from section 417 is used if the Government's stated objectives are to be met.

2. A statutory statement of directors' duties would assist business competitiveness

OHK has noted a mostly unreceptive response to the concept of enlightened shareholder value as would be required by a statutory statement of directors' duties (many such responses can be found in submissions to the Government on previous consultation documents[14]). These responses mainly focus on a lack of clarity and difficulties of compliance. A close analysis of most comments finds they are general assertions that are unclear and difficult to uphold without extended explanations or proof.

OHK also notes that many negative responses assume outcomes that have not happened in the UK as a result of the UKCA passing into law. For instance, section 172 has not proved unworkable in the UK, has not led to significant litigation, and has been largely accepted.

OHK also notes that negative responses to the inclusion of a statutory statement of directors' duties in the CO rewrite have also sometimes significantly misunderstood (or been unaware of) two aspects that drove change to the UKCA. The inclusion of non-financial reporting and directors' duties in the UKCA was premised on:

I. Enhancing business competitiveness and value (not, as some in Hong Kong seemed to interpret, constraining market forces and imposing regulations designed to hinder business via an inflexible and rigid statute that imposes unrealistic expectations on directors)
II. Enhancing clarity over complex issues (not, as some believed, making things more difficult for directors, such as leading to greater conflict with stakeholders and resulting legal challenges)

Enhancing business competitiveness: Many of the companies globally and in Asia that enhance corporate governance and make substantial CSR reporting do so on the basis that they will only succeed in long-term shareholder value if they manage their relationships with employees, suppliers, customers and others whom have a legitimate interest in the company's activities.

As elsewhere, CSR will happen in Hong Kong because it makes good business sense. Statutory requirements backed up by meaningful guidance by regulators, should help to provide certainty as well as levelling the playing field so that socially

[14] These can mostly be found in responses to Question 4: (b) do you agree that the UK approach, including the duty to promote the success of the company for the benefit of its members as a whole having regard to such factors like the long-term consequences of a decision, the interests of employees, the impact of a company's operations on the community and the environment, etc., should be adopted?

and environmentally responsible companies are not disadvantaged in the market by competing against those companies that ignore such issues because they are focused on short-term gain.

CSR is good business sense, and it is good business sense for directors of a company to have regard for their stakeholders (suppliers, customers, the community, and so on). This is already perceived by well managed companies as part of risk management, such as limiting damage to the company's brand and bottom line (which could be inflicted by bad press, consumer boycotts and by legal action).

Non-financial disclosure and a statutory statement of directors' duties in the CO rewrite are the means by which business is able to meet society's fast changing expectations and thus enhance business competitiveness.

Enhancing clarity over complex issues: OHK notes that much of the confusion in Hong Kong over the inclusion of directors' duties in the UKCA centres on interpretations that a similar statutory statement of directors' duties in the CO rewrite would lead create a minefield for directors.

The following table includes the major issues raised and OHK's responses to these based on the situation in the UK following the passing of the UKCA into law.

	Objections raised to a statutory statement of directors' duties in the CO rewrite	**OHK's responses**
1	Directors who must have regard to a range of stakeholders (who may be in conflict) will ultimately be accountable to no one, that directors should have equal regard to all parties and their interests, or that they should be accountable to all stakeholders.	Section 172 clarifies that the issues that affect a company's operations and value, and which should therefore be taken into account by directors, are necessarily complex and must be weighted carefully against each other. This reflects reality, and to ignore that is to encourage and narrow view of directors' duties. It states that directors are expected to weigh up these factors in the best interests of the company, and does not require them to have equal regard or be accountable to all stakeholders.
2	It will lead to increase in litigation that will not enhance CSR.	Unfounded assertion: There has been no increase in litigation in the UK.
3	It will lead to an increase in bureaucracy to demonstrate compliance, which will result in more 'box ticking' to establish paper trails of evidence showing that all relevant factors have been taken into account to meet the duty to promote success of the company.	Unfounded assertion: There is no evidence that there has been an increase in 'box ticking'

4	Each factor (listed in section 172 of the UKCA) may become an absolute obligation in its own right rather than simply a matter to be considered.	Section 172 clarifies the role of directors. It states that directors are expected to weigh up these factors in the best interests of the company. This reflects economic reality. It does not require them to reach any particular conclusion.
5	Directors don't have a clear basis for making decisions when different stakeholders are in conflict.	Section 172 requires that directors "think about" and "give proper consideration" to issues that arise. It maintains the basic principle that directors are accountable to shareholders and indeed acting in the company's long term interests includes having consideration of a broad range of factors, including social and environmental issues.
6	It will lead to a loss of flexibility for directors (i.e., that a statutory statement of directors' duties would become rigid and restrictive).	Unfounded assertion: Directors in the UK have not indicated a loss of flexibility.
7	It will lead to a rise in shareholder activist groups that will be unreasonably obstructive.	Unfounded assertion: There has been no rise in shareholder activism, and there is no evidence to suggest that this is likely in future.
8	Stakeholder terms like 'the community' or 'the environment' are ambiguous and inconsistent with the aim of making the CO more user-friendly.	Concerns over definitions are unfounded; the directors' duty under the law is to have regard to relevant matters and to use their own judgement to make a decision. The key point is that decisions must be made having full regard for all consequences.
9	Independent non-executive directors may be driven away from accepting positions on the board for fear of increased risk.	Unfounded assertion: This has not occurred; there is no suggestion that this is likely to occur.
10	There is no need to codify directors duties because directors already consider the issues outlined in section 172.	If this is the case, then why not add certainty to directors' duties by codifying what competent directors already do?
11	It will lead to conflicts between a range of directors' duties.	Unfounded assertion: There is no indication that there has been any conflict in the range of directors' duties. Section 172 clarifies the role of directors. It states that directors are expected to weigh up these factors in the best interests of the company. This reflects economic reality. It does not require them to reach any particular conclusion.

Around half of all objections to the inclusion of directors' duties in the CO in HK are based on unfounded assertions. The evidence from the UK is that these have not arisen and are unlikely to do so.

It is worth remembering that the consultation process in the UK leading up to the new UKCA was conducted in the context of improving business competitiveness.

As David Chivers QC points out in an introductory paragraph in his *The Companies Act 2006: Directors' Duties Guidance*:

> The new law explicitly enables directors to take into regard [the environmental and social impacts of their companies' business], highlighting the important link between responsible business behaviour and business success.[15]

He goes on to note that the language previously used by the courts to describe directors' duties (that is, to act "bona fide in the best interests of the company") is in essence repeated in the new Act. The obligation of good faith remains.

What has changed in the UK is, as Chivers states:

> …the Act now prescribes not only the basic duty of the director, but how the director must go about discharging that duty. The director must have regard to the specific matters set out in section 172(1)(a)-(f). While competent directors have previously had regard to these matters, that process is now part of the directors' statutory obligation.[16]

The same fears were articulated in the UK during the consultation process as are now being articulated in Hong Kong (i.e., that it would lead to 'box ticking' and an increased administrative burden, and so on).

Just as in Hong Kong, business in the UK were worried that directors 'must have regard' to a range of stakeholders (as expressed in Hong Kong in the first point in the table above).

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[15] David Chivers, *The Companies Act 2006: Directors' Duties Guidance*, (London: The Corporate Responsibility (CORE) Coalition, October 2007), p. 6.

[16] David Chivers, *The Companies Act 2006: Directors' Duties Guidance*, (London: The Corporate Responsibility (CORE) Coalition, October 2007), p. 6.

To alleviate these concerns, the UK Government responded in the following manner:

> The words ‘have regard to’ mean ‘think about’; they are absolutely not about just ticking boxes. If ‘thinking about’ leads to a conclusion, as we believe it will in many cases, that the proper course is to act positively to achieve the objectives in the clause, that will be what the directors’ duty is. In other words ‘have regard to’ means ‘give proper consideration to’.[17]

Fears that directors will have to give all factors equal weight, for instance, are not valid. Section 172 does not require this. It requires that factors be given proper consideration to; that is, be given appropriate weight in the context.

Section 172 clarifies that directors should have a broad understanding of various matters that affect the value of the company in the real world, and not just an artificially narrow one based on the balance sheet alone. There is no requirement that they act in any particular way, but the law provides a statutory context in which they can make informed decisions.

Section 172 in the UKCA is intended to assist companies to operate successfully in the market. It maintains the basic principle that directors are accountable to shareholders but have to take into account other interests.

A statutory statement of directors’ duties in the CO rewrite should not be abandoned on the basis of confusion about its role. OHK believes that experiences in the UK since the UKCA was passed into law should allay many of the fears expressed in Hong Kong. OHK also notes that other criticisms are unfounded.

OHK supports the Government’s goal of enhancing competitiveness, and believes that a statutory statement of directors’ duties is not an option; it is a necessity.

[17] The Government response from is from DTI [since renamed Department for Business Innovation and Skills] (June 2007) Companies Act 2006: Duties of Company Directors: Ministerial Statement. Quoted in, David Chivers, *The Companies Act 2006: Directors’ Duties Guidance*, (London: The Corporate Responsibility (CORE) Coalition, October 2007), p. 6.

OHK's recommendations

OHK supports the rewrite of the CO by the Financial Services and Treasury Bureau of the HKSAR Government. It supports the intention to update and modernise it, to make it more user-friendly and facilitate the conduct of business to enhance Hong Kong's competitiveness and attractiveness as a major international business and financial centre. And OHK supports it to bring the framework under which business sector operates in Hong Kong into line with maturing public and stakeholder expectations about the roles, responsibilities and conduct of business in society.

To achieve these goals, OHK believes that:

- Both non-financial reporting (as outlined in section 417 of the UKCA and in Chapter 9 of the CO rewrite) and directors' duties (as included in the UKCA in section 172) are mutually reinforcing, and it is not sufficient to have one without the other in the CO rewrite.
- A statutory statement of directors' duties is essential to ensure a level playing field for all companies in Hong Kong.
- Competitiveness and value are enhanced by directors having proper regard for all consequences of their business operations on society and the environment.
- Stakeholders must have access to relevant information to be able to assess the fulfilment of this duty. This is only possible with transparent CSR reporting, preferably based on GRI's Reporting Framework and Sustainability Reporting Guidelines.[18]

OHK thus recommends that:

- The CO rewrite must include a statutory statement of directors' duties as found in the UKCA in section 172.

- The CO must include clarifications requiring directors, as part of their duty to the company, to consider the company's social and environmental impacts (as, for example, is stipulated in section 172 of the UKCA).

[18] The GRI is generally regarded as the 'gold standard' reporting framework. It is the result of over a decade of multi-stakeholder dialogue, and is accepted by the vast majority of companies and other stakeholders as the definitive framework. According to the organisation's own data, nearly 1,400 companies reported to GRI that they used the reporting framework. The real number would be significantly higher as many companies that use the report don't inform GRI.

- The CO rewrite must include substantially more wording from section 417 of the UKCA to ensure improved transparency and disclosure on environmental and social issues.

- The disclosure of non-financial corporate data should be based on the GRI's Reporting Framework and Sustainability Reporting Guidelines and made mandatory to include the impacts of the company operations on employees or the workplace, environment, supply chain, community and other diverse stakeholders.

- Apart from the CO rewrite, OHK has high expectations that the HK SAR Government will take the lead to promote CSR in Hong Kong in consultation with key stakeholders and the business community.

- The Government should adopt a long-term strategy on CSR and create incentives for companies to strengthen CSR, such as through organising promotional campaigns, reviewing internal and external government policies in favour of CSR, prioritising companies with good CSR in the tendering process for public projects, as well as providing funding and other support for CSR awareness-raising programmes, research and training for small and medium-sized companies.