

Guidelines *for* *Directors*

(3rd Edition)

Organised and Published by



香港董事學會
The Hong Kong Institute of Directors

ABOUT THE PUBLISHER

The Hong Kong Institute of Directors (“HKIoD”) is Hong Kong’s premier body representing professional directors working together to promote good corporate governance and to contribute towards advancing the status of Hong Kong, both in China and internationally. A non-profit-distributing organisation with membership consisting of directors from listed and non-listed companies, HKIoD is committed to providing directors with educational programmes and information service and establishing an influential voice in representing directors. With international perspectives and a multi-cultural environment, HKIoD conducts business in biliteracy and trilingualism. Website: <http://www.hkiod.com>.

GUIDELINES FOR DIRECTORS (3rd Edition)

**This publication is created and published by
The Hong Kong Institute of Directors and funded by
Corporate Governance Development Foundation Fund.**



Published by
The Hong Kong Institute of Directors Limited
1008 World-Wide House, 19 Des Voeux Road Central, Hong Kong
Tel: (852) 2889 9986
Fax: (852) 2889 9982
E-mail: executive@hkiod.com
Website: www.hkiod.com

First published in Hong Kong 1995
Second edition 2005
Third edition 2009

ISBN 978-988-97441-7-5

Copyright © The Hong Kong Institute of Directors Limited 2009

All rights reserved. No part of this publication may be reproduced, stored in or introduced into a retrieval system, or transmitted, in any form or by any means (electronic, mechanical, photocopying, recording or otherwise), without the prior written permission of the copyright owner of this book. Quotation of short passages of the Guidelines for the purposes of review and education is allowed provided that it is made with explicit reference to the source and publisher.

Disclaimer

The Guidelines contain general information only and are based on experiences and research of The Hong Kong Institute of Directors. The Institute is not, by means of the Guidelines, rendering business, financial, investment, or other professional advices or services, nor should the Guidelines be used as a sole basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. The Hong Kong Institute of Directors shall not be responsible for any loss sustained by any person who relies on this publication.

FOREWORD: KEY MESSAGES

Good corporate governance is essential to companies as well as to Hong Kong as a whole. It enables companies to identify and protect against risk and helps Hong Kong to maintain its competitiveness as an International Financial Centre. In pursuit of good corporate governance, directors have a unique and significant role to play. I commend the Hong Kong Institute of Directors for updating the Guidelines for Directors and I encourage directors to make use of this valuable reference to keep abreast of the latest developments in corporate governance and put good practices into action.

Professor K C Chan

Secretary for Financial Services and the Treasury
Financial Services and the Treasury Bureau

It is important for Hong Kong to continuously enhance its corporate governance standards if it is to maintain its position as a leading international finance centre. Just as companies need to constantly develop their business strategies to maintain a competitive edge in the market, it is also vital for them to keep under review their corporate governance standards so as to achieve the companies' objectives and meet their shareholders' concerns and expectations. The Guidelines for Directors published by the Hong Kong Institute of Directors provides a very valuable tool to directors on the law and best practices relating to their daily work and can be read together with the Non-statutory Guidelines on Directors' Duties published by the Companies Registry.

Ada Chung

Registrar of Companies
Companies Registry

The importance of good corporate governance for all companies in gaining the trust of the market and investors is well recognised. Prime responsibility for good corporate governance of a company rests with directors who need to understand their responsibilities to their companies and their stakeholders. Compliance with the ever increasing rules and regulations is an essential element of every director's duties. This updated 3rd edition of Guidelines for Directors from the Hong Kong Institute of Directors provides clear and concise guidance for directors and will be an invaluable guide to all directors.

Eddy C Fong

Chairman
Securities and Futures Commission

Company directors of today face many challenges, including the need to remain up-to-date with relevant information to fulfill their duties. Published by The Hong Kong Institute of Directors, Guidelines for Directors is a well sought after book that facilitates references and guidelines for newly appointed directors as well as experienced directors of all companies, both listed and private. The Institute has put in meticulous efforts in offering this updated edition to readers.

Paul Chow

Chief Executive
Hong Kong Exchanges and Clearing

FOREWORD: FROM THE PUBLISHER

The Hong Kong Institute of Directors is Hong Kong’s premier body representing professional directors. We continually develop multi-prong strategies to nurture excellence in corporate governance. A wide variety of director professionalism programmes is organised on a regular basis to assist directors in fulfilling their duties. One of our major programmes is the publication of guidelines to enable directors to do a better job.

Guidelines for Directors is a “best-seller” of the Institute and a desk-top easy-to-carry reference book for both practising and newly appointed directors. This 3rd edition of the book updates the latest revisions on regulatory policies, summarises the law and recommends good practices in areas into which the law has not yet reached.

We wish to gratefully acknowledge the many parties who helped to publish this revised edition including Ms Julianne P Doe and Prof Alex Lau; and all those who have taken part in promoting and supporting this book.

Peter S H Wong

Chairman

The Hong Kong Institute of Directors

The Hong Kong Institute of Directors has organised numerous programmes in the promotion of continuing professional development for directors, including seminars, forums, publications and workshops. We are pleased to present this third edition of *Guidelines for Directors*, which complements our many other initiatives. These guidelines aim to remind and inspire directors to address various significant issues with state-of-the-art practices.

In compiling these guidelines, the Institute has had three distinct groups of readers in mind:–

- (1) Newly appointed directors, for whom it is hoped that the work will provide a reasonably brief outline of their new duties.
- (2) All those currently holding the office of director who need a general refresher as to the breadth and scope of their responsibilities.
- (3) All practising directors who need a brief initial guide to possible courses of action in a new situation.

We are grateful to all those who have helped in the publication of this book. We welcome feedback of comments from readers and users, in order to enable us to enhance our director development programmes for the Hong Kong community.

Dr Carlye W L Tsui

Chief Executive Officer

The Hong Kong Institute of Directors

PREFACE

This book attempts to summarise the law and, where possible, to recommend good practice in those areas into which the law has not yet reached, but it is difficult to make firm practice recommendations on many aspects of a company's work, given the complexity of the law, the wide diversity of activities that companies pursue, and the infinite variety of the combinations of human personalities that are responsible for directing them. These guidelines reflect the law of Hong Kong as at 31 December 2008.

On 30 January 2004, the Hong Kong Exchanges and Clearing Limited ("HKEx") released amendments to the Listing Rules (for Main Board and for Growth Enterprise Market listed companies) and also released drafts of a Code on Corporate Governance Practices ("CG Code") and Corporate Governance Report, to which listed companies must pay particular attention. Subsequently after consultation and further development, HKEx released its conclusions on Exposure of Draft Code on Corporate Governance Practices and Corporate Governance Report in November 2004. Readers who are dealing with any listed companies matters should however always be mindful of the importance of referring to the actual provisions of the Listing Rules amendments, the Code and Report themselves for a complete picture of the regulatory requirements.

Every effort has been made to ensure this work is as comprehensive as possible but it is not designed to be a substitute for professional advice tailored to meet the particular problems which may arise in a dynamic and complex business community such as Hong Kong. No responsibility for any loss arising as a consequence of any person relying upon the information or views contained in this publication is accepted by The Hong Kong Institute of Directors.

CONTENTS

	<i>Page</i>
FOREWORD: KEY MESSAGES	i
FOREWORD: FROM THE PUBLISHER	ii
PREFACE	iii
PART I – THE COMPANY AND ITS BOARD	
<i>INTRODUCTION</i>	5
<i>THE COMPANY</i>	
INCORPORATION AND LIMITED LIABILITY	5
DIRECTORS' LIABILITY IS UNLIMITED	5
PUBLIC AND PRIVATE COMPANIES	6
PROFIT, SURVIVAL AND GROWTH	6
<i>THE PARTIES ASSOCIATED WITH A COMPANY</i>	
CUSTOMERS	7
EMPLOYEES	8
CREDITORS	8
GOVERNMENT AND THE COMMUNITY	9
SHAREHOLDERS	10
<i>GENERAL MEETING, BOARD AND MANAGEMENT</i>	
GENERAL MEETINGS AND RESOLUTIONS	11
WRITTEN RESOLUTION PROCEDURE	12
RELATIONSHIP BETWEEN GENERAL MEETING, BOARD AND MANAGEMENT	12
<i>THE FUNCTIONS OF DIRECTION – DEFINITION</i>	13
<i>THE FUNCTIONS OF DIRECTION – APPLICATION TO DIFFERENT TYPES OF COMPANIES</i>	
PUBLIC COMPANIES	15
PRIVATE COMPANIES	15
SUBSIDIARIES	16
<i>HOW THE BOARD OPERATES</i>	
COLLECTIVE RESPONSIBILITY	17
NOTICE OF MEETINGS AND QUORUM	18
AGENDA	18
MINUTES	18

	<i>Page</i>
INFORMATION AND DOCUMENTATION	19
REQUIREMENTS FOR INFORMATION	19
WHO INITIATES POLICY – MANAGEMENT OR BOARD?	19
DISAGREEMENTS ON THE BOARD AND RESIGNATION	20
DELEGATION AND COMMITTEES	21
DISCLOSURE and ACCOUNTABILITY	23
<i>THE BOARD'S MEMBERS</i>	
CHAIRMAN	25
MANAGING DIRECTOR	25
CHAIRMAN AND MANAGING DIRECTOR?	26
NON-EXECUTIVE DIRECTORS	27
EXECUTIVE DIRECTORS	29
“QUASI DIRECTORS”	30
ALTERNATE DIRECTORS	30
THE COMPANY SECRETARY	31
<i>THE BOARD'S RELATIONS WITH ASSOCIATED PARTIES</i>	
SHAREHOLDERS	32
EMPLOYEES	33
CREDITORS AND SUPPLIERS	34
THE PUBLIC	34
PART II – DIRECTORS' LEGAL STATUS, POWERS AND DUTIES	
<i>INTRODUCTION</i>	35
<i>DIRECTORS' LEGAL STATUS</i>	
THE NATURE OF THE OFFICE	35
“DE FACTO” AND “SHADOW” DIRECTORS	35
PERSONS ASSOCIATED WITH A DIRECTOR	36
<i>POWERS</i>	
DIRECTORS' AUTHORITY TO ACT	37
CORPORATE CAPACITY – OBJECTS CLAUSE	37
WHO CAN COMMIT THE COMPANY?	37
CONTROL OF ABUSE OF POWERS	38
ACCESS TO INFORMATION	41

DUTIES – GENERAL

INTRODUCTION	41
THE DIRECTORS' FIDUCIARY DUTY TO THE COMPANY	41
HONESTLY, "FOR THE BENEFIT OF THE COMPANY"	42
"PROPER PURPOSE"	43
"CONFLICT OF INTEREST"	43

DUTIES – CONFLICTS AND DECLARATION OF INTEREST

SECRET PROFITS	43
CONFLICTS AND DECLARATIONS OF INTEREST	44
TRANSACTIONS BETWEEN DIRECTOR AND COMPANY	44
INSIDER DEALING	50

DUTIES ARISING FROM THE COMPANIES ORDINANCE AND ASSOCIATED LEGISLATION

51

DUTIES – DISCLOSURE, REPORTING AND ACCOUNTING

DISCLOSURE	52
LETTERHEAD AND PUBLICATION OF COMPANY NAME	52
RETURNS TO THE REGISTRAR	53
DOCUMENTS WHICH THE COMPANY MUST MAKE AVAILABLE FOR INSPECTION	54
THE COMPANY'S ACCOUNTS	54
AUDITORS	58
HONG KONG EXCHANGES AND CLEARING LIMITED DISCLOSURE REQUIREMENTS	60

DUTIES IN RESPECT OF SHARES AND SHAREHOLDERS

DISTRIBUTIONS AND DIVIDENDS	61
DUTIES TO SHAREHOLDERS	62
DIRECTORS' POWERS TO ISSUE SHARES	62
SHAREHOLDERS' PRE-EMPTION RIGHTS	63
TAKEOVERS AND MERGERS	63

DUTIES – CAPITAL AND THE MAINTENANCE OF CAPITAL

PAYMENT FOR SHARES IN LISTED COMPANIES	65
PURCHASE AND REDEMPTION OF A COMPANY'S OWN SHARES	65
FINANCIAL ASSISTANCE FOR THE ACQUISITION OF A COMPANY'S SHARES	66
OTHER WAYS TO REDUCE CAPITAL	67

<i>DUTIES IN RESPECT OF CREDITORS AND INSOLVENCY</i>	
DIRECTORS' LIABILITY TO CREDITORS	67
DUTIES IN THE COURSE OF WINDING UP	67
DEFRAUDING CREDITORS AND PREFERENCES	68
<i>DUTIES – HOW SHOULD THEY BE PERFORMED?</i>	
STANDARD OF SKILL AND CARE	69
“KNOWINGLY A PARTY” TO FRAUDULENT TRADING	71
UNDER A SERVICE CONTRACT	71
<i>INDEMNITY AND RELIEF FROM LIABILITY</i>	
INDEMNITY	71
RELIEF	72
<i>THE COMPANY'S GENERAL LEGAL OBLIGATIONS</i>	
GENERAL	72
IN TORT	73
CRIMINAL OFFENCES	73
PART III – THE DIRECTORS AS AN INDIVIDUAL	
<i>ELIGIBILITY</i>	75
<i>APPOINTMENT, REMOVAL, DISQUALIFICATION</i>	
APPOINTMENT	75
EMPLOYMENT	76
REMOVAL FROM OFFICE	77
RETIREMENT	77
DISQUALIFICATION	77
<i>REMUNERATION AND COMPENSATION</i>	
ENTITLEMENT TO REMUNERATION AND EXPENSES	80
COMPENSATION FOR LOSS OF OFFICE AND EX GRATIA PAYMENTS	81
PROFIT SHARING AND OTHER INCENTIVE ARRANGEMENTS	81