Hong Kong

Summary of Current Shareowner Rights

Percentages cited reflect information gathered by GMI about 79 companies in Hong Kong as of 15 May 2008.

Shareowners in the Hong Kong market generally have strong rights that allow engagement and activism. Such engagement is limited and unusual, however, because the market is relatively passive; institutional investors are generally not active and often do not vote their shares. Shareowner rights are also somewhat weakened by the fact that boards often have a majority of non-independent board members and that many companies are controlled by founding families. Shareowner proposals are allowed at annual general meetings but are rare.

Issue	Current Standard or Usual Practice	Level of Practice Adoption, Exceptions to Usual Practice, and Trends (if any)
What is the average percentage of independent board members on public company boards (% independent board members)?	36%	
What percentage of companies report significant related-party transactions (1% of revenue or more) within the last three years?	38%[8]	Related-party transactions are prevalent in the Hong Kong market, but shareowners have some rights in this regard because they must approve significant related-party transactions by a resolution; and interested parties are not entitled to vote on the approval of these transactions. These resolutions almost invariably pass, however, because shareowners have traditionally supported management with little dissent.
What percentage of publicly traded companies have a controlling shareowner (e.g., family, government, majority block holder)?	56%	
Is voting by proxy permitted?	Yes	
Must shares be deposited or blocked from trading in order to vote?	No	
Are there share ownership limitations in this market?	Mostly, no	Share ownership limitations are not common but may apply to a specific company, such as Hong Kong Exchanges and Clearing Limited, the operator of the Hong Kong Stock Exchange, which has a 5% ownership restriction unless approved by the Securities and Futures Commission.

[8]For more on related-party transactions in Hong Kong, please see *Related-Party Transactions: Cautionary Tales for Investors in Asia* (www.cfainstitute.org/centre/topics/governance/relatedparty.html).

Issue	Current Standard or Usual Practice	Level of Practice Adoption, Exceptions to Usual Practice, and Trends (if any)
Are there [other] common restrictions on the rights of shareowners to vote in person or by proxy?	Mostly, no	Resolutions are often declared by meeting chairs by a show of hands (i.e., one vote per person), which tends to negate the value of proxies unless a poll (one vote per share) is called. This approach by meeting chairs is common. Certain votes are required by law to be by poll, including votes on related-party transactions, transactions that are subject to independent shareowners' approval, and transactions in which an interested shareowner will be required to abstain from voting.
Do companies adhere to a majority voting standard in the election of board members?	Yes	
Do companies allow for cumulative voting in the election of board members?	No	
Are shareowners able to affect a company's remuneration policy through shareowner approval (binding or nonbinding) of the remuneration committee report, the proxy's Compensation Discussion and Analysis section, or otherwise?	No	At each annual general meeting, shareowners vote on a proposal to authorize the board of directors to fix the board members' remuneration (but not the remuneration of executives).
Are shareowners able to affect remuneration policy through binding shareowner approval of specific equity-based incentive plans or otherwise?	Yes	Equity-based incentive plans require shareowner approval.
Are shareowners permitted to introduce dissident resolutions (binding or nonbinding) at an annual meeting?	Yes	
Do shareowners have a right to convene a general meeting of shareowners outside the annual meeting process (e.g., an extraordinary general meeting or special meeting) if only 10% or less of the shares are represented in the group requesting the meeting?	Yes	
What percentage of companies include golden shares in their capital structure?	0%	Golden shares do not exist in Hong Kong.
Are shareholder rights plans (poison pills) allowed in this market?	No	The Takeovers Code expressly prohibits actions by the board designed to frustrate an offer; such acts may be implemented only through a shareowners resolution in a general meeting.
If shareholder rights plans are in use, do they have to be approved by shareowners?	NA	

Issue	Current Standard or Usual Practice	Level of Practice Adoption, Exceptions to Usual Practice, and Trends (if any)
Do all shareowners have the right to approve significant company transactions, such as mergers and acquisitions?	Yes	
Do companies require a supermajority vote to approve a merger?	No	Majority vote is required.
Are companies subject to a fair price provision, either under applicable law or as stated in company documents (such as the charter or bylaws)?	Yes	
Are class action suits commonly used in this market?	No	
Are derivative suits commonly used in this market?	Yes	

Current Engagement Practices and Shareowner Rights Developments

In Hong Kong, shareowner engagement and activism is limited. The most prominent body in corporate engagement is the Asian Corporate Governance Association (ACGA), which collaborates with leading pension and investment funds, financial institutions, listed companies, multinational corporations, and educational institutions seeking implementation of effective corporate governance practices throughout Asia. The ACGA has identified a number of concerns with Hong Kong–listed companies. Of particular note are the following: Companies are not required to report annual results within two months of fiscal year-end, quarterly reporting is not mandatory, and class action is not permitted. The ACGA has also raised concerns about institutional shareowners, in that they typically do not attend shareowner meetings, often do not exercise their votes, and rarely nominate independent board members to boards.

Nevertheless, even though shareowner activism is limited in Hong Kong, one individual, David Webb, a former independent non-executive board member at Hong Kong Exchanges and Clearing, has emerged as a prominent proactive investor who engages in activist campaigns with his own funds.

Some practices impede engagement in the Hong Kong market. Hong Kong companies have a single-tier board structure with no size limit, and the average level of board independence stands at 36 percent, which is low compared with that of other developed markets. This percentage indicates that companies tend to comply with the one-third board independence requirement but generally choose not to meet the higher standards of international best practice. The family-controlled capital structure still common in Hong Kong raises conflict-of-interest concerns. The large number of controlling shareowners in Hong Kong generally weakens minority shareowners' capacity to exercise their rights. Fifty-six percent of the Hong Kong companies researched for this manual have controlling shareowners. Furthermore, most votes at Hong Kong general meetings are conducted by a show of hands, which means that a vote can be largely determined by how many people are in the room rather than how many votes are cast. Observers of corporate governance in Hong Kong have long criticized this practice.

Hostile takeovers in Hong Kong are rare, mainly because most public companies are closely controlled, either by the founding families or by parent companies, but also because shareowners traditionally either support the local managers or remain passive. Poison pills are not permitted in Hong Kong, and although fair price provisions support general fairness in takeovers, in many companies, a controlling shareowner can weaken the role of minority shareowners where takeovers are concerned.

A significant right Hong Kong shareowners have, which is aligned with international best practice, is the ability to approve or disapprove by vote substantial related-party transactions. Related-party transactions are common in Hong Kong, particularly in controlled companies, so the right to approve them is important. Detailed information on both the nature of such transactions and the method of determining the "arms length" price has been quite variable, however, and the subject of considerable criticism.

In May 2008, Railways Pension Trustee Company, one of the largest U.K. occupational pension funds, published a statement about Hong Kong corporate governance policy. Regarding shareowner rights, this report states that the Trustee Company expects companies listed on the Hong Kong Stock Exchange (HKEx) to have at least one-third independent board members on the board, to separate the role of chair and CEO or to nominate a lead independent director, and to adopt voting by poll rather than by a show of hands at the annual general meeting.

Legal and Regulatory Framework

Many key shareowner rights are delineated in the corporate governance standards in the listing rules for companies listed on the main board of the HKEx or Growth Enterprise Market.[9] These rules include regulations for the supervision of board members, operation of boards, composition of committees, and shareowner rights. Companies must state in their half-year and annual reports whether they have complied with the rules. These rules are administered by Hong Kong Exchanges and Clearing, the stock exchange operator in Hong Kong.

The Hong Kong Securities and Futures Commission, an independent statutory body, is the main authority for and supervisor of the securities market in Hong Kong. To strengthen public confidence in the market, investor awareness, and investor protection, the commission regulates investment products offered to the public, listed companies, the HKEx, share registration approval, and those entities that participate in trading activities. The Takeovers and Mergers Panel and the Takeovers Appeal Committee is overseen by the Securities and Futures Commission. The Takeovers and Mergers Panel is charged with administering the Takeovers Code. The Takeovers Appeal Committee is charged with reviewing disciplinary rulings of the Takeovers and Mergers Panel at the request of an aggrieved party to determine whether any sanction imposed by the panel is unfair or excessive.

A number of mechanisms are presently in place in Hong Kong to facilitate shareowner engagement. The Hong Kong Companies Ordinance mandates the practice of one share, one vote for listed companies. It also states that shareowners are allowed to bring lawsuits against board members and major shareowners on behalf of the company but that shareowners need to acquire judicial approval before launching the derivative actions. Class action suits are not allowed in Hong Kong, which makes lawsuits difficult to undertake. An extraordinary general meeting of shareowners may be called, however, by shareowners representing 5 percent of the issued share capital. Additionally, board members can be removed without cause by a simple majority vote at a shareowners' meeting. Board members are subject to election on a periodic basis by a majority vote. A supermajority vote of shareowners is required to amend a company's articles of association.

Voting in general meetings in Hong Kong is by a show of hands, or one vote per person attending the meeting, regardless of the number of shares the shareowner may hold or present, unless a poll is demanded. Thus, many votes have been approved only on a show of hands, which may not reflect the balance of proxies. Since 31 March 2004, voting by poll (one vote per share) has been required for related-party transactions, transactions that are subject to independent shareowners' approval, and transactions in which an interested shareowner will be required to abstain from voting.

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[9]The Growth Enterprise Market is a stock market set up by the Hong Kong Stock Exchange specifically for growth companies that do not yet meet the requirements of profitability or track record that would allow them to be listed on the main board of the HKEx.

Key organizations with information relevant to shareowner rights in Hong Kong include the following:

Hong Kong Exchanges and Clearing Ltd (www.hkex.com.hk)
Securities and Futures Commission (SFC) (www.sfc.hk)
Companies Registry—Hong Kong Companies Ordinance (www.cr.gov.hk)
Hong Kong Institute of Chartered Secretaries (www.hkics.org.hk)
Hong Kong Retirement Schemes Association (www.hkrsa.org.hk)
Hong Kong Securities Institute (www.hksi.org)
Hong Kong Investment Funds Association (www.hkifa.org.hk)
Hong Kong Institute of Directors (www.hkiod.com)
Hong Kong Institute of Certified Public Accountants (www.hkicpa.org.hk)
Asia Corporate Governance Association (www.acga-asia.org)
Webb-site (www.webb-site.com)