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Ethical governance

Keeping companies on track

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Sanctions compliance



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Beyond compliance

The guardian role of company secretaries in ethics and governance



The Hong Kong Business Ethics Development Centre at the Independent Commission Against Corruption regards the company secretary as a trusted partner to achieve better ethical and governance standards in Hong Kong companies.

As part of the senior management team, the company secretary of listed companies plays a crucial role by acting as the board's professional adviser on governance matters. While every board is different in terms of its composition and the nature of the business, company secretaries face some common challenges when discharging their guardian role as the conscience of the company.

Encouraging active contribution of company directors at board meetings

It is important that every board member brings independent judgement to issues relating to the company's strategies, development, performance and risk management through their contribution at board meetings. Even where high-calibre executives with diverse industry expertise and experience have been recruited to the board, company secretaries may find it difficult to motivate directors to make an active contribution to the issues being

discussed or to show sufficient interest in the company's affairs. This may be because directors lack specific knowledge in the areas under discussion, or because the board lacks a culture of constructive challenge and debate. Acting as the key conduit for the free exchange of dissenting views and challenges between the board and management is never an easy task.

Advising the board to adopt best practices beyond regulatory compliance

It is not uncommon for listed companies to be reluctant to go beyond the minimum regulatory requirements and to 'do the right thing' – the pursuit of profit and business growth are often the prime concerns. Having the key responsibility to promote good corporate governance, company secretaries should encourage the board to invest in and adopt best practices beyond regulatory compliance – this will benefit the company's performance, manage risk

Highlights

- company secretaries have professional and fiduciary duties to safeguard the interests of the company and its stakeholders
- even where company secretaries are not directly involved in illegal activities, they can still bear criminal and civil liabilities where they have not fulfilled their professional and fiduciary duties
- company secretaries can contact the ICAC for advice on anti-bribery, corruption and corporate governance issues

effectively and protect the interests of different stakeholders in the long run.

Motivating company directors to attend training

Even where company directors are highly knowledgeable and experienced in their respective fields, continuous development is imperative to maintain their alertness to regulatory requirements and risk management issues. In addition to evaluating the corporate governance levels of Hong Kong listed companies, the *Corporate Governance Scorecard 2016*, published by The Hong Kong Institute of Directors, promotes the need for company directors to keep abreast of developments in corporate governance and in their relevant industries to perform their roles effectively.

The Corporate Governance Code under Hong Kong's listing rules requires directors to participate in continuous professional development to develop and refresh their knowledge and skills (see Paragraph A.6.5). The challenge posed to company secretaries is therefore to

motivate busy directors to attend training for the sake of their own self development as well as the success of the enterprises they direct.

Handling irregularities, non-compliance or misconduct

In cases of regulatory non-compliance or misconduct, especially when senior managers are involved, company secretaries face an ethical dilemma. They have a clear professional and fiduciary duty to take appropriate action against such cases, but past cases handled by the ICAC reveal that some company secretaries have chosen to stay silent about the malpractice rather than speaking out against it. In some extreme cases, some were even beguiled into joining the scams of corruption, fraud or other malpractices and were prepared to compromise their ethical standards for their own personal gain.

A recent ICAC investigation demonstrated the dire consequences for company secretaries who fail to recognise their guardian role to protect the interests of

the company when ethical challenges arise. In the case, an entrepreneur, a certified accountant, together with an executive director/company secretary of a listed company were convicted of bribery and fraud in relation to the acquisition of a Mainland plantation project by the listed company. The entrepreneur and the accountant had, with the assistance of the company secretary, offered the chairman of the listed company bribes amounting to HK\$180 million for acquiring the chairman's shareholding. In return, the chairman arranged his listed company to acquire the Mainland plantation project at HK\$500 million from an offshore company owned by the entrepreneur.

Consequently, the constitution of the listed company's board of directors was changed and the entrepreneur secured control of the company. The offenders defrauded the Stock Exchange, the listed company's existing shareholders and potential investors by concealing the corrupt scheme in the course of the acquisition. The company secretary not only failed in his duty as a corporate guardian, but even facilitated the wrongdoings, which subsequently cost him six years' imprisonment. The other offenders were sentenced to jail terms ranging from four years to seven years and nine months.

In sentencing, the judge remarked that corruption is a serious offence. He reprimanded the defendants for undermining the reputation of Hong Kong's financial industry and its honest business environment. Highlighting the guardian role of the company secretary, the trial judge commented that the company secretary 'was loyal to [the chairman], perhaps too loyal, so he joined the dishonest scheme. However, loyalty

How is bribery defined in law?

Section 9(1) of Prevention of Bribery Ordinance (PBO) states that any agent (for example an employee or a director of a company) shall be guilty of an offence if, without the permission of his principal (for example the employer or the company) or without any reasonable excuse, he or she solicits or accepts any 'advantage' for doing or forbearing to do any act in relation to his principal's affairs or business. It is also an offence under Section 9(2) of the PBO for any person who offers an advantage to an agent for the above purpose.

An 'advantage' refers to anything that is of value such as money, a gift, commission, loan, employment, or service and favour. 'Entertainment' is generally excepted where it involves the provision of food or drink for consumption on the occasion when it is provided, and any other entertainment connected with such provisions. The maximum penalty for an offence under Section 9 of the PBO is seven years' imprisonment and a fine of HK\$500,000.

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can only go so far and the judge pointed out that there is always the choice for the defendant to say 'no, Mr chairman, this is wrong, I will not do it'.

Anti-corruption laws in Hong Kong

The above case demonstrates how bribery can facilitate massive financial fraud and damage stakeholders' interests as well as Hong Kong's market integrity. Bribery in the private sector is governed by Section 9 of the Prevention of Bribery Ordinance (PBO) which aims to maintain fair play in the business environment and proscribe acts breaching agents' fiduciary duties to their principals. Section 9(1) of the PBO prohibits the solicitation and acceptance of advantage by an agent in connection

with his principal's business. Section 9(2) of PBO prohibits the offering of such advantage to an agent.

While business operations have become increasingly globalised, if any act of bribery – including promising, agreeing, soliciting or accepting advantages without permission – takes place within Hong Kong, the case can be pursued under the PBO enforced by the ICAC.

Are you personally liable?

Even where company secretaries are not actively involved in corruption or fraud, they may be liable for breach of duty in the same way that board members and senior executives are if

they fail to discharge their duties to protect the interests of the company as a whole – including those of the minority shareholders.

This can be best illustrated by a recent ruling of the Market Misconduct Tribunal (MMT) against the chairman and senior executives, including the company secretary/group financial controller, of a company listed on the Growth Enterprise Market (GEM) of the Stock Exchange of Hong Kong for accounting fraud. The MMT found that these parties had grossly overstated the company's net asset value in the company's annual reports and result announcements. Among others, the MMT found the company

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secretary culpable of market misconduct by negligently providing materially false and misleading information to the public. Though the company secretary argued that he did not have access to the financial records of the subsidiaries of the company, nor had he been able to monitor the subsidiaries' compliance with the appropriate financial standards, the MMT found him negligent in performing his professional duties as a qualified accountant by accepting the irrational arrangement limiting his ability to fulfil his duties, thereby enabling the chairman and senior executives to defraud the investing public.

In fact, both the Main Board and GEM listing rules recognise the important role of company secretaries in advising the board through the chairman and/or the chief executive on governance matters. The company secretary's role as a promoter of corporate governance is also highlighted by The Hong Kong Institute of Chartered Secretaries (the Institute) in its guide for members, *The Essential*

Company Secretary. In particular, the guide stresses that 'company secretaries cannot afford to ignore any cases of non-compliance with legislation or regulation that come to their attention, even if the directors have purported to make someone else responsible for those matters (Paragraph 3.5). They should also ensure that the board is fully aware of its responsibility to avoid engaging in any market misconduct practices, including not putting out or allowing the release of misleading information, or by engaging in a course of conduct which could amount to market misconduct (Paragraph 5.1.15).'

Disclosure of anti-corruption policy

To further enhance the corporate governance standard of listed companies and to ensure an orderly, fair and informed financial market in Hong Kong, the environmental, social and governance reporting requirements set out by the Stock Exchange have been strengthened with effect from the 2016 financial year. Among the changes was

the upgrade of the level of obligation of the disclosure of a listed company's anti-corruption policy from voluntary to 'comply or explain'. Furthermore, the requirements for risk management and key internal control measures have also been strengthened in the Corporate Governance Code. Listed companies are required to adopt a structured approach to risk management and internal control, as well as to conduct an annual review of the effectiveness of these systems. The related disclosures in the corporate governance reports of listed companies have also been upgraded from recommended best practice to 'comply or explain'.

Company secretaries responsible for preparing the corporate governance reports of listed companies can contact the ICAC for advice on promoting corporate governance. The ICAC provides assistance to listed companies in developing and effectively implementing their own programmes to prevent corruption, thereby facilitating the

meeting of their reporting requirements in respect of anti-bribery policy and corruption risk management.

The Ethics Promotion Programme for Listed Companies

In 2015, the Hong Kong Business Ethics Development Centre (HKBEDC) of the ICAC launched a three-year 'Ethics Promotion Programme for Listed Companies' in collaboration with relevant government departments, regulators, chambers of commerce and professional bodies, including the Institute, with the aim of bringing out the important roles of company directors and professionals in sustaining an ethical culture in listed companies. Apart from providing tailor-made corruption prevention and education services to listed companies, the HKBEDC has also developed a training package on business ethics for listed companies under the programme. The package consists of case studies, training videos and lessons to learn, featuring the ethical challenges faced by the company directors, senior executives and professionals during the pre-listing, daily operations and takeovers and merger stages of listed companies.

One hypothetical case scenario in the training package highlights the possible criminal and civil liabilities of a company secretary who fails to take action against suspected fraud during the pre-listing process. A company secretary is tasked to assist a company to become listed on the Stock Exchange of Hong Kong. In the listing process, he learns from the sponsor's due diligence unit that there are irregularities with respect to the company's bank loans and its land transactions in the Mainland. When he seeks clarification from the executive director/general manager

of the company, he is brushed off and reminded that any slippage in meeting the listing deadline would disappoint the founder of the company, whom he highly respects. Realising that the deadline is approaching, the company secretary does not pursue the issue further.

Although the company secretary in this scenario was not directly involved in the irregularities or illegal activities, he still bears possible criminal and civil liabilities on the basis of the breach of his professional and fiduciary obligations to safeguard the interests of the company and its stakeholders.

The training package will be launched at the *Conference on Business Ethics for Listed Companies – Corporate Governance: Compliance and Beyond* on 1 September 2017. Company directors, senior executives and governance professionals including company secretaries are encouraged to join the conference in which distinguished speakers from the government, regulators and professional bodies will discuss the latest regulatory developments relating to the governance of listed companies, as well as sharing their experience and skills in practising ethical governance from practitioners' perspectives. Participants will also gain a better understanding of the risks and corruption pitfalls relating to different aspects of the management of listed companies.

Trusted partners in upholding market integrity

For 23 consecutive years, Hong Kong has been ranked the freest economy by the Index of Economic Freedom released by the Heritage Foundation. As a leading international financial centre in the world, a level-playing

field for businesses that fosters fair competitions is instrumental to its success. Over the years, the ICAC has been sparing no effort in eradicating bribery and related malpractices that may impede the efficient operation and integrity of the financial market. In fact, Hong Kong has been consistently ranked among the cleanest places in the world with very low levels of corruption. In the TRACE Matrix 2016, a global index tracking business bribery risk developed by TRACE International in collaboration with the RAND Corporation, Hong Kong was ranked the fourth least corrupt jurisdiction among 199 economies around the world, and the best jurisdiction in Asia.

While the index further affirms the clean business environment in Hong Kong, it cannot be sustained without collective efforts and unwavering support from relevant stakeholders in the business community. The ICAC will continue to join hands with the business community to uphold high ethical standards in our financial market. The company secretary, as the guardian of corporate governance and 'conscience of the company', will always be the ICAC's most trusted partner to achieve this goal.

Hong Kong Business Ethics Development Centre

Independent Commission Against Corruption

More information on the 'Ethics Promotion Programme for Listed Companies' and the upcoming 'Conference on Business Ethics for Listed Companies – Corporate Governance: Compliance and Beyond' are available at: www.hkbedc.icac.hk/ic.