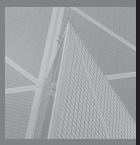

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A GUIDE FOR THE EFFECTIVE BOARD

A GUIDE FOR THE EFFECTIVE BOARD

Charltons' Hong Kong adaptation of Abbott Stillman & Wilson's "Seeing Beyond Compliance" - an Australian guide to Corporate Governance

Foreword

A Guide for the Effective Board is designed for government authorities, and for profit and not for profit organisations. Good governance and effectiveness of the governing body are critical to an organisation's success.

The issue of corporate governance has been simmering away for years. The collapse of the VEDC, Pyramid, and the Bond and Skase empires readily come to mind. Recent collapses, including ENRON and WorldCom in the USA, Vivendi in France, Marconi in Britain, Parmalat in Italy and, in Australia, the high profile crashes of Ansett, HIH and One.Tel, have brought the issue to the boil. Board members have been charged, or found wanting, and in some cases Directors & Officers' Liability insurance has not been forthcoming.

Regulators continue to set rules and processes under the mantle of compliance. This will not prevent collapses in the future. It is people on the board working effectively as a board, and with senior management, which will make organisations successful.

We see the effective governance recipe as:

The Ideal Board Member + The Effective Board Member + Compliance + Social Responsibility + Whistleblower Protection.

This publication demonstrates how to make the board effective; thus enabling the board members collectively to fulfil their role.

It outlines a program for the board, which can be tailored effectively to meet the needs of any substantial business. The following topics are discussed:-

1. What does corporate governance mean?
2. Creating and developing the board as an effective governance body
3. Necessary legislative requirements for governance
4. The board's role and relationship with the community

Many of the regulatory requirements relate to public companies or listed entities. The principles in this booklet apply to any organisation (including private company, not for profit, government authority, partnership etc). Adherence to these principles should lead to more effective entities, with resultant increased profits, better risk management and creation of an improved working environment.

As with all publications of this nature, this guide is not intended to constitute advice on any specific issue. Its purpose is to draw attention to the overall concept of good governance. Advice should be sought in respect of any specific concern.

We wish to thank Andrew Marty, Managing Director of SACS Executive Solutions, Geoffrey Williams, Management Consultant and Executive Coach, and R (Bob) Falconer, Chairman of STOPline Pty Ltd (see contact details in Appendix E), for their assistance in putting together this booklet and permitting us to quote them.

The contents of this guide have not been reviewed or endorsed by the Stock Exchange of Hong Kong Ltd. or by the Hong Kong Companies Registry.

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ABOUT CHARLTONS

Charltons was founded in October 1998 as a focused corporate finance firm. The focal point of the firm is to provide a first class legal service on Hong Kong and PRC-related corporate finance matters, to both international and local clients from Hong Kong and mainland China. Its aim is to give practical, creative and commercial solutions that match the business objectives and priorities of our clients. The firm was awarded the "Boutique Law Firm of the Year Award" by Asian Legal Business in both 2002 and 2003.

Charltons has considerable experience in offering advice to multinational and local companies operating in Hong Kong and China. Its regulatory work involves frequent communications with the Hong Kong Stock Exchange and Securities and Futures Commission regarding regulatory and corporate finance issues relevant to our clients' projects.

The partners of Charltons have given legal and strategic advice on governance and effectiveness to governing bodies in all spheres of activity. They have served and still serve on the boards of companies, both listed and unlisted.

Charltons has quite deliberately taken a broad yet integrated approach to the production of effective governance information to assist boards in a practical way. A combination of legal and strategic business issues needs to be integrated into this model. Charltons believes that with its management and public board experience and legal knowledge, it can offer boards help and guidance in tailoring their governance model and procedures to meet each organisation's specific business requirements.

We hope that in reading this guide, you will see we believe in clear communication. There is one point we want to make clearly and unashamedly - we have prepared this guide to assist you and in the hope that we can provide advice and assistance to you in our professional capacity. We have set out in the section entitled "Where to From Here?" some of the ways we believe we may be able to assist you to achieve your governance objectives.

We invite you to visit our website www.charltonslaw.com

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PART I

GOVERNANCE

In this section we shall deal with:

- What is Corporate Governance?
- Is Good Governance Restricted to Corporations?
- The Board's Governance Roles
- Establishing an Effective Governance Charter

What is Corporate Governance?

"Corporate governance has succeeded in attracting a good deal of public interest because of its apparent importance for the economic health of corporations and society in general. However, the concept of corporate governance is poorly defined because it potentially covers a large number of distinct economic phenomenon. As a result different people have come up with different definitions that basically reflect their special interest in the field." [1]

One of the definitions that we like is: "*Corporate governance is about promoting corporate fairness, transparency and accountability.*" [2]

A number of important corporate governance initiatives have been implemented recently or are under implementation in Hong Kong. Firstly, the Stock Exchange of Hong Kong Ltd. (the "SEHK") amended the Main Board and Growth Enterprise Market (the "GEM") Listing Rules to introduce comprehensive changes relating to corporate governance. The new Listing Rules came into effect on 31 March 2004 subject to certain transitional arrangements.

The SEHK has now introduced a new Code on Corporate Governance Practices (the "Code") for listed companies and Listing Rules on the Corporate Governance Report which listed companies are required to include in their summary annual and annual reports. The bulk of the Code's provisions and the disclosure requirements in the Corporate Governance Report are effective for accounting periods commencing on or after 1 January 2005. The requirements of the Code and the Corporate Governance Report relating to "internal controls" will take effect for accounting periods commencing on or after 1 July 2005.

The Code and Corporate Governance Report are the same for Main Board and GEM issuers, except that while quarterly reporting is a recommended best practice for Main Board issuers under the Code, it remains a mandatory requirement under the GEM Listing Rules.

The Code and the Listing Rules on the Corporate Governance Report are set out in full in Appendices A and B, respectively. Certain other consequential amendments have been made to the Listing Rules in connection with the introduction of the Code and the Rules on the Corporate Governance Report. These amendments are set out in Appendix C.

Please note that copyright ownership in the Listing Rules, of which the Code and the Rules relating to the Corporate Governance Report form part, belongs to the SEHK.

The Code on Corporate Governance Practices

The Code represents a considerable enhancement of the Main Board's Code of Best Practice in Appendix 14 of the Main Board Rules and the corresponding requirements of GEM Rules 5.35 to 5.45, which it replaces. In the GEM Rules, the Code is set out in a new Appendix 15.

The Code contains 2 tiers of recommended board practices. The first tier contains the "Code provisions" which are the minimum standards of board practices with which listed companies are expected to comply. Compliance is not however mandatory. Instead, the Code has adopted the "comply or explain" approach adopted in the UK Combined Code. Listed companies must state whether they have complied with the Code provisions and, if they have chosen to deviate from them, must give considered reasons for each deviation in their preliminary half-year and annual results announcements and in their half-year and annual reports (and summary half-year and annual reports, if any).

In the case of half-year and summary half-year reports, companies must either give considered reasons for each deviation or may refer to the Corporate Governance Report in the previous annual report and include details of any changes and considered reasons for any deviation not previously reported.

In the case of preliminary half-year and annual results announcements, companies may give the required information by reference to the Corporate Governance Report in the previous annual report, or in the case of preliminary annual results announcements, to the previous half-year report together, in either case, with a summary of changes since the relevant report.

Transitional arrangements will also apply so that:

- companies will not be required to disclose and give considered reasons for every deviation from the Code provisions in their first preliminary annual and half-year results announcements published in respect of an accounting period commencing on or after 1 January 2005. Instead, it will be sufficient to include a summary of the major areas of deviation. Considered reasons will not be required; and
- in the case of half-year reports for periods commencing on or after 1 January 2005 where the company has not previously issued an annual report for a full financial year commencing after that date, companies will not be required to give considered reasons for each deviation from the Code. Instead a company will be required to disclose the deviations and, in respect of each deviation, to either give considered reasons as to why it does not propose to comply with the relevant Code provision in the future or to set out the steps it has taken or proposes to take in order to comply with the relevant Code provision in future.

Companies may also adopt their own codes on corporate governance practices on such terms as they may consider appropriate. They will however be required to give considered reasons for any deviation from the SEHK's Code provisions in their relevant financial reporting documents.

The second tier of recommended board practices comprises recommended best practices which listed companies are encouraged to adopt. They are based largely on certain UK Combined Code provisions and other UK guidelines. Listed companies are encouraged, but not required, to include a statement as to compliance with the recommended best practices and considered reasons for any deviation from them in their half-year and annual reports (and summary half-year and annual reports, if any).

The Code covers 5 principal areas: Directors; Remuneration of Directors and Senior Management; Accountability and Audit; Delegation by the Board; and Communication with Shareholders. Under each heading, the Code sets out a general principle, the Code provisions and Recommended Best Practices.

A number of the provisions of the UK Combined Code have been omitted from the Code, at least for the time being. These include a requirement for boards to formally evaluate their own performance and provisions relating to institutional shareholders' responsibilities, the appointment of a senior independent director and enhanced responsibilities for company secretaries.

The Corporate Governance Report

Listed companies are required to include a separate report on their corporate governance practices in their annual and summary annual reports for accounting periods commencing on or after 1 January 2005. The Corporate Governance Report included in a company's summary annual report may be a summary of that contained in its annual report and may incorporate information by reference to its annual report. The summary must contain, as a minimum, a narrative statement indicating overall compliance with, and highlighting any deviation from, the Code provisions.

The Corporate Governance Report consists of 2 levels of disclosure requirements. The first level comprises mandatory disclosure requirements. Failure to meet any of the mandatory disclosure requirements constitutes a breach of the Listing Rules. The mandatory disclosure requirements include, among others:

- a narrative statement of how the listed company has applied the principles of the Code, providing an explanation enabling its shareholders to evaluate how the principles have been applied; a statement as to whether the company meets the provisions of the Code; and details of, including considered reasons for, any deviation from the Code provisions;
- whether the company has adopted a code of conduct for securities transactions by directors on terms no less exacting than the minimum standard required by the Model Code for Directors' Dealings (Appendix 10 of the Main Board Rules) and by GEM Rules 5.48 to 5.67; confirmation of compliance with the required standard and, in the event of any non-compliance, details of the non-compliance and an explanation of the remedial steps taken;
- information about the company's directors (including composition of the board, number of meetings held and details of non-compliance with certain of the Listing Rules' requirements relating to independent non-executive directors ("INEDs")); and
- an analysis of auditors' remuneration and information about the audit committee (including its role and composition, a report on work performed by the committee and details of any non-compliance with the Listing Rules' requirements as to the establishment and constitution of an audit committee).

Certain Code provisions also expect listed companies to make specified disclosures in their Corporate Governance Reports. Where companies choose not to make any expected disclosure, they must give considered reasons for the deviation. The expected disclosures under the Code provisions include a statement that the directors have conducted a review of internal controls and an explanation by the audit committee of its recommendation and the reasons for any different view taken by the board in relation to the selection, appointment, resignation or dismissal of the external auditors.

The second level consists of recommended disclosures which are set out at paragraph 3 of the Corporate Governance Report. Companies are encouraged to make these disclosures. As an alternative to disclosure of detailed and lengthy information relating to the recommended disclosures in their Corporate Governance Reports, companies may choose to include all or part of such information on their websites, if they highlight to investors where they can access the soft copy of the information by giving a hyper-link directly to the relevant webpage and/or collect a hard copy of the information free of charge. Alternatively, if the relevant information is publicly available, companies may state where the information can be found. Any hyperlink must be directly to the relevant webpage.

With the demise of a number of high profile corporations worldwide this is a further attempt to restore public and investor confidence in Hong Kong corporate leadership.

Non-statutory Guidelines on Directors' Duties

The Hong Kong Companies Registry also published Non-statutory Guidelines on Directors' Duties (the "Guidelines") in January 2004 which are reproduced with the permission of the Companies Registry at Appendix D. All rights reserved. The latest version of the Guidelines is available for downloading from the "List of Circular" section of the Companies Registry's homepage on the internet (website: http://www.info.gov.hk/cr/) or at the enquiry counters of the Companies Registry on the 13th and 14th floors of the Queensway Government Offices.

The Guidelines outline the general principles for directors in the performance of their duties which are largely derived from case law. They are intended for directors of all companies irrespective of whether they are public or private, listed or unlisted. It is important to note that the Guidelines constitute principles only and not an exhaustive statement of the law, their intended purpose being to assist directors in understanding their responsibilities by making the principles of law and equity more accessible. Copies of the Guidelines should be given to all directors.

Other Corporate Governance Initiatives

Other important initiatives introduced by the Hong Kong government and regulatory authorities to improve corporate governance include the implementation of the Securities and Futures Ordinance[3] in April 2003 which, in relation to listed companies, introduced an enhanced regime for the disclosure of interests in their securities, significantly extended the market misconduct regime and the possible sanctions and increased the investigatory powers of the SFC. The SEHK has also introduced further amendments to the Listing Rules tightening the regulation of sponsors of

listing applicants and independent financial advisers to listed issuers which came into force on 1 January 2005. The government of Hong Kong also proposes to amend the Securities and Futures Ordinance to extend the market misconduct regime to cover breaches of the more important Listing Rules (e.g. the requirements relating to financial reporting, disclosure of price-sensitive information and obtaining shareholders' approval for certain notifiable transactions) and to provide sanctions for such breaches, so giving "statutory teeth" to the Listing Rules. Increased remedies for shareholders of listed and unlisted companies (including a right to bring a derivative action on behalf of a company) have been included in the Companies (Amendment) Ordinance 2004. The relevant provisions are expected to come into force in 2005.

The Companies Ordinance[4] clearly holds directors of companies responsible for the company that they govern. This role includes a significant mandate for improving the performance of a company through strategic planning and monitoring of senior management action. Boards are also directly responsible for their own conduct.

Is Good Governance Restricted to Corporations?

In popular language, "governance" and "corporate governance" have become synonymous.

We believe that they are not. We believe that the J. Wolfensohn definition applies to any governing body. Although the Code applies only to listed public companies, the effective management of boards in all organisations, including private companies, not for profits, government bodies and partnerships, is essential to the development of the business. The information in this booklet applies to this range of organisations.

Much of the literature focuses on the regulatory, legal and accounting aspects of corporate governance. These are extremely important and should not be underrated. Unfortunately this focus and some of the courts' decisions over the last 10 – 15 years have made many directors risk-averse. This attitude negates the very reason that limited liability companies were developed in the first place. Board members must balance business growth and development and the concomitant risk-taking with risk management. The realisation that a risk-averse mentality could frustrate corporate enterprise led to changes in jurisdictions such as Australia, though not yet seen in Hong Kong, to the law encapsulated in the so-called Business Judgment Rule.[5]

At the same time, if boards are to be truly effective, there is a need to go beyond the statutory requirements and look at the effectiveness of the governing body.

The Board's Governance Roles

Kiel[6] lists the dual roles of the board to be:-

1. ensuring compliance (through monitoring of the company) and self regulation of the conduct of board members individually and collectively as the board; and
2. improving the performance of the organisation it is charged with overseeing through strategy formulation and policy making

Recent Australian court decisions have emphasised that directors should bring "an informed and independent judgment" to bear on the various matters that come to the board for decision.[7] It is likely that Hong Kong courts will adopt a similar attitude.

In our view, in order to fulfil its governance roles the board is responsible for:

1. Strategic direction - setting major goals, policy, framework and strategies
2. Selection, remuneration and performance review of the CEO
3. Monitoring adherence to governance compliance and risk management policies and practices
4. Advocacy and network on behalf of the organisation to assist in achieving its strategic goals, including communication with key stakeholder groups
5. Monitoring organisational performance

Establishing a Corporate Governance Charter

Each organisation needs to establish a charter based on a philosophy which is appropriate to that organisation. Issues include:

- How "hands-on" will the board be in relation to the management and oversight of the company?
- What will come to the board and what will be delegated?
- The board's role in strategic planning processes including the important relationship it has with all stakeholders
- The relationship with the broader community

A survey conducted by SACS Executive Solutions in Australia comments on the importance of the board having a philosophy with which it approaches governance issues which transform into various style and values issues. The most important criteria for board members were ethics, openness, honesty, trustworthiness and transparency with high levels of integrity (100%). This was immediately followed

by an 80% figure for courage to challenge the status quo and have an independent mind, whilst at the same time being a team player.

Also important was being attuned to the community's value system. "How would this look on the front page of the newspaper?" is only one element. Ethical governance and social responsibility are pivotal areas for an effective board.

Various authors on governance have put together sample charters on governance.[8] Whilst they are useful, each requires tailoring to meet the specific needs of the organisation. There is no sense in taking a pro forma and thinking it will apply in all cases. Indeed, to do so in some circumstances could lead to a major diminution in effectiveness of the board. Each board needs to develop its own charter.

THE IDEAL BOARD MEMBER

In this section we shall cover:

- Selection, Retention & Succession Planning
- Essential Skills
- Roles & Responsibilities

Selection, Retention & Succession Planning

Selection

For a board to be effective, there needs to be appointment of people with the requisite skills and values. As such, there needs to be a skill matrix produced and maintained for each organisation. For example, a board may find that it needs members with skills and experience in the legal, financial, marketing and strategic and business-planning fields in addition to industry based experience. Recruitment must also be aligned to correspond with gaps in skill base from time to time.

SACS Executive Solutions interviewed thirty prominent directors, whose experience covers public, private and voluntary sectors. Managing Director, Andrew Marty, titled this research the "Human Resources Aspects of Governance."[9]

The survey found that board members should possess strong general knowledge and experience of the industry sector in which the business is involved as well as high levels of education and a grasp of legal and statutory issues associated with the entity in the business sector.

In addition, broad business experience and a personal understanding of the role of boards were considered to be very important. Interestingly, a knowledge of the board member's own limitations was in the top six knowledge and experience factors mentioned, which may reflect a response to some of the high profile mistakes and omissions made by board members in recent times.

Interestingly, it was seen as being less important, whilst not unimportant, that the person have specific experience within the industry sector in which the business is involved. In general, broad levels of experience in business, life experience and general technical knowledge associated with legal and statutory issues seem to be the most important issues mentioned.

The above provide challenges for most organisations, even though there are well developed human resources policies within such organisations as a whole. Often such policies are not applied to the board.

Letters of appointment which make it clear to board members what the corporation expects of them are useful. Letters of appointment should contain the following matters:

- Terms of appointment
- Time commitment envisaged
- Powers and duties of directors
- Any special duties or arrangements attaching to the position
- Circumstances in which the office of director becomes vacant
- Expectations in regard to committee work
- Remuneration and expenses
- Superannuation arrangements
- Disclosure of interests and independence
- Fellow board members
- Policy governing dealing in securities
- Induction training and continuing education
- Access to independent professional advice
- Indemnity and insurance arrangements
- Confidentiality and rights of access to information
- A copy of the constitution

Retention

Having recruited a board, it is important to retain good people. Here the chairman plays an important role in effectively communicating with each board member, encouraging and challenging them to provide a real contribution. Board members also need to be supported by provision of quality and timely information by management.

Succession Planning

A level of stability for board membership assists in taking a longer-term perspective on organisational strategic issues.

The same skills matrix established to admit board members can assist in planning succession to ensure that an appropriate level of expertise is maintained.

Progressive turnover of board members is desirable for continuity.

Special attention needs to be paid to succession planning for key board positions such as the chairman, deputy chairman and heads of each major committee.

Essential Skills

It is interesting to compare in Table A Pease & McMillan's[10] views on the skills essential to make for an effective director with those core competencies identified in the SACS survey (the percentages shown against each equate to the percentage of the thirty directors responding to the survey):

Table A

Pease & McMillan *Essential Skills*	**SACS** *Core Competencies*
Communication and people skills	Strong communications skills (93%) Ability to establish quality relationship/people skills (67%) Sound written communication (30%) Good public speaking skills (17%)
Analytical and critical thinking ability	Strong analytical and problem solving skills (60%)
Long-term vision	Ability to think strategically (50%)
An understanding of broad economic issues	Basic financial analytical abilities (43%)
Leadership skills	Ability to influence and persuade others (23%)
Sensitivity and the willingness to listen to the needs of interested parties	Ability to listen meaningfully (20%) Ability to gain respect and act as a mentor to management (10%)

The ability to function well in meetings and in small groups	Ability to relate to a wide range of people (10%)
Objectivity and the ability to take a broad view	Clear thinker and strong critical reasoning skills (13%)
Responsibility and a willingness to be accountable	Ability to understand and relate to stakeholders (10%)
A broad knowledge of business	Basic economic skills, i.e. an understanding of the broader environmental economic factors, which affect commercial business success (10%)
Creativity and lateral thinking ability	

In summary, the conclusion one draws from the above table reinforces the view that board members must be leaders who have good communication, business and financial skills. They must have empathy and possess high moral standards.

Roles & Responsibilities

SACS research identified the following key result areas for boards. In order of importance, they are as follows:-

1. Preserve and advantage the investment entrusted into their care by shareholders and stakeholders – measured by success of the company (83%).
2. Challenge, approve and monitor strategies set by management and the CEO (70%).
3. Protect the legal entity by ensuring an effective risk management strategy is in place, and deliver a culture of compliance with the legislation (60%).
4. Act responsibly and be accountable to shareholders, and communicate with the stock exchange (33%).
5. Create a clear and explicit vision for the future of the entity, and have that underpinned by aims, strategies and processes which achieve the organisation's strategies and aims and, ultimately, vision (33%).
6. Achieve points of the strategic plan which have been set for that year (17%).
7. Deliver transparent reports to shareholders and the community (ask yourself "how is this going to look on the front page of the newspaper?") (10%).

Individual Board Member's Key Results Areas

The SACS survey also identified four key result areas for individual board members:

1. Demonstrate a good understanding of the business. The board member needs to have an interest in the business being conducted by the entity and become familiar enough with this business to advantage decision making on strategic issues (27%).
2. Diligently engage with issues brought to the board and offer constructive input. Board members should be active, positive, and engaged participants (20%).
3. Effectively manage their particular portfolio. The comment relates to the fact that many board members are appointed to boards due to a portfolio specialisation – law, finance, engineering etc. The individual must ensure that his/her specialist expertise is brought to bear on any decisions taken by the board (13%).
4. Contribute to the setting of strategic directions of the organisation. Each board member should have an active involvement in the development of strategy. The capacity to contribute in this way is a key success factor of board membership (13%).

The Role and Effectiveness of the Chairman

In addition to skills, experience and values as a board member, in common practice the chairman of a board has additional responsibilities. In a recent Australian case[11] relating to the collapse of One-Tel, a large Australian telecommunication company, the Australian Securities and Investments Commission contended that a chairman has a higher duty of care than ordinary directors. The chairman, Greaves, made an interlocutory application to strike out the allegation. The Court ruled that ASIC had a "reasonably arguable cause of action against the chairman" and therefore declined to strike out the cause of action as it related to Greaves. The question of whether or not a chairman does indeed have greater responsibility in law, at least in Australia, will be determined by the outcome of that case. Even though any outcome reached by an Australian court would not be legally binding on a Hong Kong court, it may prove to be persuasive when this question does come up before a Hong Kong court.

The additional responsibilities which relate to the effective operation of the board include:

1. Choosing the right people for appointment to the board in conjunction with a Nomination Committee
2. Effectively leading the board and acting as a facilitator of relationships within the board and ensuring there is a corporate culture within the board itself in keeping with achieving objectives

3. Ensuring board members achieve key result areas
4. Ensuring that the board provides shareholders with sufficient information to allow them to make informed decisions about issues
5. Acting as a conduit between the board and the CEO
6. Promoting and facilitating constructive, debated Board meetings by effectively managing different views and opinions
7. Making use of his/her special skills such as:-
   (a) meeting management skills
   (b) time management skills
   (c) ability to demonstrate quality leadership
   (d) ability to bring the board and management together to work as a team
   (e) ability to construct and manage agendas

THE EFFECTIVE BOARD MEMBER

In this section we will deal with:

- Performance Management
- Relationship Management
- Support Services
- Making Meetings Work

Performance Management

In order to ensure that board members, including the chairman, operate effectively requires some form of evaluation system. The research points to the need for effective people management at board level. Indeed, better management of such issues can be a differentiator and provide competitive advantage.

A clear distinction needs to be made between performance on the one hand and conformation/compliance on the other. Board members can readily discharge their compliance obligations by adhering to the minimum legal requirements; for example, by attending the requisite number of meetings. Compliance is necessary – but it is not sufficient for effectiveness.

A board performance management process needs to start with a list of specific goals and targets relevant to each board member. Some will be general for all board members and others will need to be specific, based upon the expertise that individuals bring to the board. The board needs to ensure that part of its governance planning includes the setting of goals and performance management of each of its members, including the chairman.

Once goals are established, there are a number of ways in which performance can be assessed. For example:

1. Goals are produced and annually the chairman consults each board member about their view on each other board member. The chairman then combines this with his or her own perspective and has a one to one performance review with each board member. For the chairman, two nominated board members obtain information from their fellow board members and have a private discussion with the chairman.

2. The board undertakes a separate meeting in camera to discuss board member and the chairman's performance. This should be against a pre-determined set of criteria.

3. An independent consultant is engaged by the board to collect information from within and outside the board and a report is generated.

Each of the above may be suitable in various environments. However, perhaps option 1 is the most useful starting point as it has the advantages of confidentiality and the most potential for frank, open discussion.

Options 2 and 3 may produce more clinical rather than effective outcomes.

It is important to note that in relation to voluntary boards, all board members need to be totally committed to an appraisal program. As these are unpaid positions, there is a risk that board members may just leave rather than subject themselves to a formal appraisal process. The whole issue of performance management for board members needs to be very carefully and sensitively handled so it is seen as constructive, rather than destructive.

Relationship Management

The Chairman and the Board Members

The chairman is the leader of the board, and leadership skills (refer page 16) are essential for an effective board.

The chairman may or may not be an executive director. In practical terms, each organisation needs to determine this matter based on its:

- Size
- Shareholder profile
- Board member skills

We offer the following few points of advice:

1. The chairman needs to be well informed, and act as a sounding board for other board members so they have confidence in the chairman.
2. The chairman should solicit board members' comments and the board members should actively seek out the chairman, providing their ideas, feedback and views.
3. New board members should be supported and mentored by the Chairman to ensure they are properly inducted and participate in ongoing professional development.
4. The chairman should, when necessary, counsel board members. All should participate in an agreed board performance evaluation mechanism and process.

5. For new board members, the chairman should lead the Board Nomination Committee in a process to select. Selection should be based on the existing and desired skills matrix of the board itself. The Nomination Committee will identify perceived gaps, and hopefully select to encourage:

   (a) Diversity

   (b) Constructive teamwork

6. The Chairman be non-executive.

The Chairman and the CEO

The new Code for listed companies requires segregation of the roles of chairman and chief executive and the division of their responsibilities to be clearly set out in writing.

Effective governance necessitates a working relationship between the chairman and the CEO which is characterised by:-

- Openness
- Honesty
- Consultation and communication
- Trust

This is perhaps the most important relationship in any organisation.

Here are a few tips.

For both:

Don't play games with each other. The stakes are too high.

For the chairman:

1. Build an effective relationship with your CEO.
2. Be a sounding board for the CEO, on behalf of the board members, to advise likely board opinion on particular issues and the time they should come before the board.
3. Be honest and constructive with the CEO on issues to be addressed. When an issue comes up, discuss it constructively and how it might be dealt with.
4. Engage in an ongoing and constructive process of performance feedback for the CEO. Adopt a "no surprises" approach. Establish clear expectations. Do not leave it for the annual review. Ensure that annual reviews are a balance of positive and constructive feedback for improvement.

5. Through regular briefings from the CEO, be on top of major management and strategic issues, but stay out of managing, in detail, the issues themselves. This will enable you to answer other board members' queries and promote confidence within the board.
6. Solicit information on the way in which the organisation is running overall, how board members and senior management are performing, and constructively advise the CEO. Advice can be obtained both from within and external to the organisation.
7. Defend the CEO from unfair or unreasonable criticism from within the board, particularly at meetings. Ensure, however, that valid issues are properly raised and dealt with constructively.
8. Actively participate in the selection of any new CEO and, where possible, involve your successor. It is important that the chair be confident of being able to develop an effective and trusting relationship with the new appointee. Issues such as personality, value system, organisational fit and the chair's personal level of comfort with a new CEO are very important in determining how effective a relationship with a new person will be.

For the CEO:

1. Build an effective relationship with your chairman.
2. Meet and brief your chairman regularly, being careful not to burden the chairman unnecessarily with levels of administrative detail. Focus on:-
   - Strategic/emerging issues
   - Current and projected performance highlights
   - Any shareholder feedback or comments
   - Any issue likely to have an effect on the organisation internally or in the public eye
3. Work on, and thoroughly brief, the chairman on the detail of the board agenda; the issues, potential reactions and desired outcomes. The chairman can't help, or be effective in dealing with business, unless well briefed.
4. Expose the chairman (and board members) to the organisation's operations through tours, briefings etc as part of a defined board member education/ development program. An understanding of the business by the board will dramatically increase its effectiveness.
5. Actively seek your chairman's advice on major issues. Use your chairman as a sounding board. As the CEO would like to have no surprises from the chairman, the same applies to the CEO. Keep the chairman informed.
6. Wherever possible, participate in the appointment of a new chairman. Regrettably, few CEOs do. Remember relationships are two way, and it is just as important that a CEO be able to work with a new chairman as vice versa.

It is recognised that the CEO will not select the new chairman, but it is highly desirable they should be involved and make comment on their ability to establish an effective working relationship with a new person.

Support Services

The SACS survey identified that the directors consulted believed attending formal training in the area of governance was essential.

Under the new Code for listed companies, all directors are required to receive a comprehensive and tailored induction on appointment and continuous professional development thereafter. In this regard boards would be well advised to take advantage of the many excellent courses that are conducted on the roles and responsibilities of board members by various bodies. The Hong Kong Institute of Directors conducts a number of them on a regular basis.

It is also a minimum requirement under the new Code for listed companies that a board member should be entitled to seek independent professional advice at the listed company's expense in appropriate circumstances.

Board members should also be protected by suitable Deeds of Access, Insurance and Indemnity and should be offered the opportunity to seek professional advice in regard to such matters. The provision of indemnities and insurance for directors is governed by section 165 Companies Ordinance which is discussed in Part III under "Indemnities and Insurance".

It is worth noting that some organisations are now re-engineering their board support services – including pre and post-meeting processes – to more effectively service the needs of their board members. Charltons is able to arrange further advice on these best practices.

Making Meetings Work

Meetings must be carefully planned, and nothing should be left to chance. The chairman plays a key role in this regard. The first matter to consider is the agenda for the meeting. This should be settled between the chairman and CEO/managing director. They should agree on what they are hoping that the meeting will achieve.

Once the agenda is settled, the chairman and CEO should decide whether the normal venue is suitable or not. This will depend upon the nature of the business to be conducted at the meeting. It may be important that the board be briefed by an outside specialist. If this is so and the matter is sensitive, it may well be that the board should meet at a discreet venue. At the very least, consideration should be given to this point.

It is essential that all board members be given board papers within a reasonable time for the meeting to enable them to properly prepare themselves for discussion. It should only be in emergencies that board members are given papers at the boardroom table. Listed companies must send board papers for regular board meetings to directors at least 3 days before the meeting (Code provision A.6.1). The chairman must be "on top" of every item on the agenda so that he can control the meeting effectively. What management says or introduces at the meeting should not surprise the chairman.

The chairman should allow full and constructive debate but should always be in control. For instance, the chairman should not allow board members who are endeavouring to push a particular point of view to be repetitive, nor should he/she allow personal remarks or argumentative behaviour. All board members should constructively contribute during the board meeting. The chairman should run the meetings effectively and encourage participation and discussion by all board members and not allow particular dominant members to overshadow others and quash discussion.

If the subject matter requires decision or is introduced to gauge the board's attitude only, the chairman should indicate this at the outset.

COMPLIANCE

In this section we shall cover:

- The Board's Role
- Compliance Reviews
- Appropriate Committees

The Board's Role in Ensuring Compliance with Board Members' Duties

We have touched upon the role of the board in ensuring compliance with statutory and regulatory obligations. The legal obligations imposed upon board members as set out in Part II are the obligations and duties of individual board members. It is imperative, however, in order to be effective that the board develop procedures to ensure that each board member and all of them collectively fulfil their duties both to the letter and the spirit of the law.

The board can do this by establishing:

- Regular compliance reviews
- Appropriate committees

Regular Compliance Reviews

An effective board should establish a board Compliance Manual and have a Compliance Plan which is monitored by the board of the responsible entity (if it has a majority of independent directors) or by a Compliance Committee. Regular compliance reviews should be conducted to ensure that there has been no breach of the legal or Listing Rules' obligations set out in Part II. The suggested Governance Committee should conduct this review.

Establishing Appropriate Committees

Some of these board committees may seem like overkill to smaller entities. Depending upon the size of the organisation, it may not be necessary to establish each as a separate committee, but all of the areas should be covered by one or more board committees.

Governance/Compliance

This committee's duty should be to conduct a regular audit to gauge the effectiveness of the board and its operations. This committee should ensure that there is a Compliance Manual and should monitor compliance with common law, statutory and other regulatory requirements. It should comprise some board members and independent third parties. The chairman should be one of the independent third parties.

In smaller organisations this committee could be combined with the Audit Committee.

Audit

The establishment of an audit committee is mandatory under both the Main Board and GEM Listing Rules. The committee must be made up of non-executive directors ("NEDs") only, the majority of whom must be INEDs of the company. The committee must have a minimum of 3 members, at least one of whom must be an INED with appropriate professional qualifications or accounting or related financial management expertise. The committee must be chaired by an INED.

A detailed list of the duties and responsibilities of audit committees has been included as minimum standards and recommended best practices in the new Code to give further guidance to listed companies.

The overall responsibility of the audit committee should be to review the integrity of the company's financial reporting. It should have direct access to management and oversee the independence and performance of the external auditors and review the relationship with external auditors.

The Hong Kong Society of Accountants has also produced "A Guide for Effective Audit Committees", which contains a detailed list of the responsibilities of an Audit Committee. The website of the Hong Kong Society of Accountants can be found in Appendix E.

Even those organisations that are not compelled by the Listing Rules to have an audit committee should seriously consider establishing one. Audit committees "can be a more efficient mechanism than the full board for focussing the company on particular issues relevant to verifying and safeguarding the integrity of the company's financial reporting"[12].

IT Compliance Committee

If the company depends upon information technology, and very few do not do so, it should establish an IT Compliance Committee. This could be part of the Risk Management Committee, but if the size and critical nature of the company's IT warrants it, a separate committee should be established. The committee's function should be to ensure that:

- The company's IT delivers value to stakeholders
- It controls and minimises IT risk
- Privacy legislation is adhered to
- The Telecommunications Ordinance[13] which deals with unauthorised access to computers and interference with telecommunications installation, and the Interception of Communications Ordinance[14] which deals with the interception of e-mails, are not breached

Remuneration

The establishment of a remuneration committee comprising a majority of INEDs is a minimum requirement under the new Code for listed companies (Code provision B.1.1). The committee is required to have written terms of reference dealing clearly with its authority and duties. Its responsibilities include making recommendations to the board on the company's remuneration policy, determination of remuneration packages of executive directors and senior management, pension rights, compensation payments and incentive policies. It should also make recommendations to the board on the remuneration of NEDs.

Nomination

It is a recommended best practice under the new Code that listed companies should establish a nomination committee comprising a majority of INEDs (Code provision A.4.4). The committee's role is to ensure the appropriate size and composition (including the skills, knowledge and experience) of the board, to identify individuals suitably qualified to become board members and to assess the independence of non-executive board members.

Risk Management

This committee should comprise a suitable mix of executive (preferably CEO) and independent board members. Its role is to devise the mechanism for establishing a risk profile for the company which embraces both financial and non-financial risk. It must monitor the profile and recommend actions to minimise risk. It must ensure that board members have adequate resources and evaluate the exercise of directors' duties in making business judgments.

SOCIAL RESPONSIBILITY

Social Responsibility and being a good and ethical business is not only "feel good", it is "good business". It is a key responsibility of the board and senior management.

Internally, there is a strong connection between the organisation's social responsibility as perceived by staff, and the ability for the organisation to recruit and retain motivated people. Externally, the argument is equally pervasive, as community perception will directly impact sales and revenue.

Corporate businesses do not operate in a vacuum. Each is part of a community – local, national and often international. A corporation's reputation for social responsibility, or being a good and ethical business, has a direct bearing on its:-

- Level of sales and revenue. The buying community will have a view on the social contribution made, or the harm done, by a corporation as part of its decision to purchase.
- The level of shareholder interest in investment. Increasingly investors are asking for "ethical" investments.
- Recruitment and retention of talented and motivated people. Surveys have shown staff want to be part of an organisation which operates ethically in the community.
- Bottom line profitability.

For larger organisations in particular, social responsibility is not a "feel good" thing, but good business.

Business is run by board members, CEOs and senior management. It is this group which must take on the mantle of strategic leadership in philanthropy.

It is not only cash from corporations which support community organisations. A number of overseas companies allow staff-paid time to undertake work for voluntary organisations to motivate staff and provide good corporate citizen images within the community.

More recently, literature has been produced on the importance of being strategic in relation to community philanthropy. Professor Michael Porter in the Harvard Business Review in December 2002 clearly demonstrates the link between effective strategic philanthropy and growth in bottom line profitability.[15]

Porter suggests that most organisations focus their philanthropic giving on:-

- Communal obligation; support for civic, educational and welfare organisations,

motivated by a desire to be a good citizen

- Goodwill building; support for staff, suppliers, clients or government/community leaders, often necessitated by the quid pro quo of business and the desire to improve the organisation's relationships[16]

He has highlighted the importance of moving towards more strategic philanthropy which contributes to bottom line profitability. Porter argues that where corporate expenditure produces simultaneous social and economic gains, shareholders and corporate philanthropy merges. This means that the organisation should spend money on philanthropy where it can produce economic gain to that organisation in the short, medium or long term.

Understanding a corporation's community and strategically identifying where convergences of goals exist requires a real leadership in philanthropy from boards, CEOs and senior management.

On the planning drawing board, corporations now need an additional section – "Strategic Philanthropy and Social Responsibility". It is only by taking a strategic approach that a real benefit will come in the form of bottom line profitability, not merely PR. This focus is a move away from the more traditional avenues of giving, namely a desire to be a good corporate citizen or building goodwill between clients, suppliers and others. By carefully analysing the elements of competitive context, a company can identify the areas of overlap between social and economic value that will best enhance its own competitiveness.[17]

The task is not easy, yet significant progress can be made where there is commitment by the board, CEO and senior management to constructive thought leadership and the allocation of resources.

Porter goes on to say that understanding the link between philanthropy and competitiveness can help companies identify where they should focus their corporate giving. Understanding the way in which philanthropy creates value highlights how they can achieve the greater social and economic impact through their contribution. The where and how are mutually reinforcing.[18]

The broad sector of philanthropy, social responsibility and not for profit organisations is going through a period of growth and change. It is important to recognise that it is a complex and specialised area where getting the best advice is as important as becoming strategic. There are a number of emerging bodies which may assist with independent advice on available philanthropic options and effective social investment. These organisations are not the traditional trusts that allocate funds from a pool. Rather, they are facilitators that can assist corporations in identifying their preferred area for social investment, then introduce them to credible organisations or projects in their areas of interest.

Having decided upon what to invest on a strategic basis, there is a need for vigorous tracking and evaluation of results. Effective boards will ensure that these criteria are built in to their board monitoring reports.

By adopting a strategic approach to giving, an organisation is truly investing in the community. In the process, the board is demonstrating within its own organisation and to the broader community a genuine leadership in philanthropy in a way which does not reduce shareholders' long term imperatives. The board is fulfilling elements of its effectiveness charter by demonstrating it is fulfilling its social responsibilities and benefiting the organisation by doing so.

WHISTLEBLOWERS

Bob Falconer, in his paper "Whistleblowers and Corporative Governance" raises important questions when he asks:

> *Would the collapse of Enron and WorldCom have reached the proportions that it did if the concerns of Sherron Watkins and Cynthia Cooper had been heard and acted upon earlier?"*

At the time of their disclosures, neither Watkins nor Cooper had legal protection. It is only since the US Sarbanes – Oxley Act that there is a mandatory provision for a confidential anonymous whistleblower's hotline for use by all company personnel.

In the interests of protecting people who wish to express concerns about improper behaviour, the UK has the Public Interest Disclosure Act (1998). Also in Australia, several Australian States have legislation impacting upon the public sector.[19]

Although this legislation pertains to the public sector, the private sector is increasingly regarding whistleblower protection as essential to good governance. Whether the motivation for doing so is driven by ethics or pragmatism does not matter. "It is now a clear corporative imperative."[20]

To be effective, boards need to ensure that whistleblowers are protected by anonymity and that they are not victimized. We do have a tendency to wish to "kill the messenger". Boards must ensure that we do not do so. We are all aware of the anonymous quote "confession might be good for the soul but it's bad for the career prospects". The following matters need to be addressed:

- establish a whistleblower protection policy
- facilitate whistleblowers through an independent hotline
- provide staff education and training
- communicate the entities' commitment to addressing reportable conduct

Boards should remember that:

> *"In all the known celebrated corporate collapses loyal and committed employees tried to alert management to their suspicions and concerns without success."*[21]

Effective boards will ensure this does not happen.

WHERE TO FROM HERE?

Every board should conduct a due diligence examination of itself as measured against the matters outlined in this guide. We suggest that the best way to do this is to conduct an effective governance audit.

We do not profess to be able to provide every solution to your governance requirements. We do believe, however, that because of the background of some of our people in:

- management;
- service on public company boards; and
- the conduct of thorough due diligence investigations of corporations

we are able to identify areas that may need improvement.

Charltons can help by:

- preparing a governance charter for the board or assisting the board in this process
- tailoring this booklet and our effective governance audit checklist to meet the specific needs of your organisation
- preparing a resource guide that is specific to your organisation's requirements
- making personal presentations to individual board members, Compliance Committees or boards with question and answer opportunities
- conducting a full audit to establish the effectiveness of a board and to identify and recommend changes, if necessary, to make the board more effective
- conducting an audit limited to legal compliance issues
- helping with discrete aspects of effective governance by advising on any of the individual matters that are dealt with in this booklet
- providing written responses to specific board or other company officers' concerns
- providing you with checklist material to enable you to undertake your own audit
- working with your auditors to establish a compliance audit, both presently and on an ongoing basis
- devising and preparing a Compliance Manual for use by your Governance/ Compliance Committee

- providing an independent "sounding board" to the board or other company officers for compliance or other issues on an agreed or as required basis

More information about us, our people, and our capabilities can be found by visiting our website www.charltonslaw.com

PART II

THE LEGAL AND LISTING RULES OBLIGATIONS

Mandatory for Listed Companies[22]

The following are some of the more important requirements for companies listed on the Main Board and the GEM:

Continuing Disclosure

Main Board Rule 13.09 and GEM Rule 17.10

Generally and apart from compliance with all the specific requirements of the Listing Rules, a company listed on the Main Board or GEM must keep the SEHK, members of the company and other holders of its listed securities informed as soon as reasonably practicable of any information relating to the group (including information on any major new developments in the group's sphere of activity which is not public knowledge) which:-

(i) is necessary to enable them and the public to appraise the position of the group; or

(ii) is necessary to avoid the establishment of a false market in its securities; or

(iii) might be reasonably expected materially to affect market activity in and the price of its securities.

Financial Reporting

(1) Main Board

Rules 13.46 and 13.48

Main Board companies are required to distribute their annual reports and accounts or summary annual reports within 4 months after the end of each financial year. Full or summary half-year reports must be distributed within 3 months after the end of each 6 month period. Main Board companies are not required to include a comparison of actual business progress with the business objectives contained in the listing document in their annual or half-year reports.

(2) GEM

Chapter 18

Companies listed on the GEM are required to distribute their annual reports and accounts or summary financial reports within 3 months after the end of each financial year. Full or summary half-year reports and quarterly reports must be published within 45 days after the end of each relevant period. Moreover, for the period comprising the remaining financial year or half-year during which listing occurs and the 2 financial years thereafter, the annual and half-year reports must include a comparison of actual business progress with the business objectives contained in the listing document, together with an explanation of any material differences.

Audit Committee

Main Board Rule 3.21 and GEM Rule 5.28

The establishment of an audit committee is compulsory for both Main Board and GEM listed companies. If a company fails to establish an audit committee or fails to meet the requirements as to its constitution, it must immediately notify the SEHK and publish an announcement containing the relevant details and reasons and rectify the situation within 3 months.

Corporate governance

Main Board and GEM

The Listing Rules require:

- every board of directors of a Main Board or GEM listed company to include at least 3 INEDs, at least one of whom must have appropriate professional qualifications or accounting or related financial management expertise (Main Board Rule 3.10 and GEM Rule 5.05);
- each INED to provide annual confirmation of his independence to the listed company, receipt of which must be confirmed by the company in its annual reports;
- listed companies to employ a full-time qualified accountant to oversee their accounting and financial reporting procedures and internal controls (Main Board Rule 3.24 and GEM Rule 5.15);
- all listed companies to have an audit committee (see above);

- listed companies are required to adopt a code of conduct for securities transactions by directors on terms no less exacting than the minimum standard of conduct for such transactions set out in Appendix 10 of the Main Board Rules and GEM Rules 5.48 to 5.67;
- GEM listed companies to designate one executive director as their compliance officer (Rule 5.19);
- shareholders' approval for directors' service contracts exceeding 3 years or providing for more than one year's notice or payment of more than one year's remuneration on termination; and
- disclosure of individual directors' emoluments on a named basis in a company's financial statements.

Persons to liaise with the SEHK

Every Main Board (Rule 3.05) and GEM (Rule 5.24) listed company must appoint 2 authorised representatives who will act at all times as the company's principal channel of communication with the SEHK. These authorised representatives must be either two directors or a director and the company's secretary, unless in exceptional circumstances agreed by the SEHK.

Directors' Disclosure

Main Board and GEM

Section 341 of the Securities and Futures Ordinance (Cap. 571) of the Laws of Hong Kong applies to directors of listed companies. It requires such a director to disclose any of the following events to the SEHK:

(i) when he becomes interested in the shares or debentures of a listed company or any associated company;

(ii) when he ceases to be interested in such shares or debentures;

(iii) when he enters into a contract to sell any such shares or debentures;

(iv) when he assigns any right granted to him by the listed company to subscribe for shares or debentures of the listed company;

(v) when an associated company grants him rights to subscribe for shares or debentures of that associated company, or if he exercises or assigns such rights;

(vi) when the nature of his interest in the shares or debentures of the listed company or any associated company changes; and

(vii) when he comes to have or ceases to have a short position in the shares of a listed company or any associated company.

The notification time limit allowed is 3 business days.

Mandatory for all Companies

Disclosure of Material Personal Interests

Section 162 of the Companies Ordinance (Cap. 32) of the Laws of Hong Kong requires a director of a company who is in any way, directly or indirectly, interested in a contract or proposed contract with the company to declare the nature of his interest, if it is material, at the earliest meeting of directors at which it is practicable for him to do so. Section 161 requires certain directors' emoluments, pensions and compensations to be included in the company's accounts to be laid before the company in its general meetings.

Section 155B of the Companies Ordinance provides that where a proposed resolution affects the interests of any director differently from the interests of any other member, details of such interests must be disclosed in the notice of the resolution. If a meeting is summoned to approve any alteration of the company's articles of association to provide or improve directors' emoluments, the notice convening the meeting must include an explanation of the proposal and the provision must be approved by a resolution which does not relate to any other matters (Section 116A of the Companies Ordinance).

Prohibition on Loans to Directors

Subject to certain exceptions provided by section 157HA of the Companies Ordinance, Section 157H provides that a company cannot directly or indirectly:

- make a loan or quasi-loan to a director of the company or of its holding company;
- enter into any guarantee or provide any security in connection with a loan or quasi-loan made by any person to a director of the company or of its holding company; or

- if any director of the company holds a controlling interest in another company, make a loan or quasi-loan to that controlled company, or enter into any guarantee or provide security in connection with a loan or quasi-loan made by any person to that controlled company.

The above prohibitions relating to "quasi-loans" apply only to "relevant companies", being companies other than private companies unless the private company is part of a group of which another member is listed. The section also prohibits a "relevant company" from entering into a credit transaction as creditor for a director of the company or of its holding company or a company in which a director has a controlling interest and from providing a guarantee or security in connection with any such credit transaction.

Section 157I provides that where a transaction is entered into in breach of section 157H:

- the transaction itself is not invalidated, but the person receiving payment is liable to repay it to the company immediately unless he is not a director of the company and he shows that, at the time the transaction was entered into, he did not know the relevant circumstances; and
- any guarantee or security given is not enforceable against the company unless the guarantee or security is provided in connection with a loan or quasi-loan to, or a credit transaction entered as creditor for, a person who is not a director of the company or of its holding company and the person to whom the guarantee was given or the security provided did not know the relevant circumstances at the time.

Section 157I also states that a director of a company which has breached section 157H is liable:

- to account to the company for any gain made directly or indirectly by the transaction; and
- jointly and severally with any other director so liable, to indemnify the company for any loss or damage resulting from the transaction if:
  - (i) he knowingly and wilfully authorised or permitted the transaction; or
  - (ii) the transaction consists of either a loan or quasi-loan to, or the entering into of a credit transaction as creditor for, him or a person connected with him; or
  - (iii) the transaction consists of giving a guarantee or providing security in connection with a loan or quasi-loan made by any person to, or a credit transaction entered into by any person as creditor for, him or a person connected with him.

In addition to the above civil consequences of a breach of section 157H, as imposed by section 157I, the following persons are guilty of an offence pursuant to section 157J:

- the company;
- any director who wilfully authorised or permitted the transaction to be entered into; and
- any person who knowingly procured the company to enter into the transaction.

A person is not guilty of an offence if he shows that at the time the transaction was entered into, he did not know the relevant circumstances.

Fraudulent Trading

If in the course of winding up the company it appears that any of its business has been carried on with the intent to defraud creditors or for any fraudulent purpose, the court may declare that persons who were knowingly parties to carrying on business with such fraudulent intent are personally liable for all debts and other liabilities of the company (section 275 of the Companies Ordinance).

PART III

THE ROLE OF THE COMPANY DIRECTOR

POWERS, DUTIES, OBLIGATIONS, CONFLICTS OF INTEREST AND CONSEQUENCES OF BREACH

Powers, Duties and Obligations

Directors are agents of the company appointed by the members to carry on the business of the company. They are not per se shareholders or employees, although they may also fill either or both of those roles in a separate and completely distinct capacity.

A director is defined in section 2 of the Companies Ordinance as including "any person occupying the position of director by whatever name called".

Powers of Directors

Directors derive their power from the common law and from the articles of association of the company.

Once appointed, directors have the power to do anything on behalf of the company that the company can do (Table A, article 82). As companies are now vested with the power to do anything a natural person can do (section 5A of the Companies Ordinance, which effectively abolished the ultra vires rule except in the case where companies continue to have specific objects), the powers of directors are obviously very wide.

At common law, directors are obliged to act as a board and exercise their powers collectively passing resolutions at properly convened meetings.

Acting as a board may not be practical at all times, therefore it is common for the articles to grant powers to delegate the collective powers of the board to individual directors or to committees of directors (Table A, article 104) and to a managing director (Table A, article 111).

It is not always convenient for directors of a company to meet to consider business as required by common law. This is why it is now usual for most modern articles to contain a power to pass written resolutions, which means physical meetings are no longer necessary (Table A, article 108). Some articles even allow directors to sign separate sheets of paper containing the same resolution, rather than one circular letter, and allow business to be conducted by facsimile.

Duties of Directors

Duties of directors are generally owed to the company. They act in a fiduciary capacity.

Common law duties

As noted above, the Companies Registry issued its Non-statutory Guidelines on Directors' Duties in January 2004 which are reproduced at Appendix D and are available on the website of the Companies Registry.

Fiduciary duties of honesty and bona fides

- requirements of absolute good faith;
- duty to exercise powers for their proper purpose;
- not to allow conflict between duties to the company and personal interests;
- not to make a secret profit (see also statutory prohibition on insider dealing).

Non-fiduciary duties of care, diligence and skill

- subjective obligation dependant on actual knowledge and experience;
- no requirement of continuous attention to the affairs of the company;
- no liability for poor judgment (provided acted bona fide).

Statutory duties imposed by:

Companies Ordinance

- duty to maintain registered office (section 92) and publish accurate company name (section 93);
- duty to call and hold meetings (section 111 for AGMs and section 113 for EGMs);
- duty to prepare and maintain accounts (sections 121 to 129);
- duty to maintain registers and minute books and file returns (section 95 for members and section 158 for directors and secretary);
- duty to issue and allot shares in accordance with section 57B;
- duty not to trade fraudulently (section 275).

Securities and Futures Ordinance

- applies to listed companies only;
- requires directors to disclose interests and dealings in shares or debentures of the company or its associated companies (section 341);

- requirement to maintain registers of interests and short positions (sections 336 and 352);
- prohibits a "person connected with a corporation" (as defined in sections 247 and 287) (including a director) from dealing in listed securities of that corporation or any related corporation (sections 270 and 290), if he possesses "relevant information" (as defined in section 245) about the corporation or the related corporation.

Listing Rules

- investors and the SEHK must be kept fully informed with immediate disclosure of any information which might reasonably be expected to have a material effect on market activity in and the price of its securities;
- all holders of listed securities must be treated fairly and equally;
- Chapter 3 of the Main Board Listing Rules and Chapter 5 of the GEM Listing Rules impose fiduciary duties and duties of skill, care and diligence and a duty on directors to accept full responsibility for compliance with the Listing Rules;
- The Code on Corporate Governance Practices (Appendix 14 of the Main Board Listing Rules and Appendix 15 of the GEM Listing Rules)

Obligations of Disclosure

Companies Ordinance

Directors are obliged to disclose to the board of directors any material interest, whether direct or indirect, in any contract or proposed contract with the company. Such disclosure should be made at the earliest meeting of the directors (section 162 of the Companies Ordinance).

It is possible to make a general disclosure to the board, but this must be prior to the first time the contract or proposed contract is considered by the board (section 162(2) of the Companies Ordinance).

Failure to disclose exposes the director to a potential fine.

Disclosure does not validate the contract. It simply removes the possibility of the director being fined under the Companies Ordinance.

Securities and Futures Ordinance - Disclosure of Interests

- applies to listed companies only;
- requires directors to disclose interests and dealings (including those of their spouse, children under 18 and companies under their control) in shares or debentures of the company or its associated companies;

- Section 341 requires directors of listed companies to disclose any of the following events:

  (i) when he becomes interested in the shares or debentures of a listed company or any associated company;

  (ii) when he ceases to be interested in such shares or debentures;

  (iii) when he enters into a contract to sell any such shares or debentures;

  (iv) when he assigns any right granted to him by the listed company to subscribe for shares or debentures of the listed company;

  (v) when an associated company grants him rights to subscribe for shares or debentures of that associated company, or if he exercises or assigns such rights;

  (vi) when the nature of his interest in the shares or debentures of the listed company or any associated company changes; and

  (vii) when he comes to have or ceases to have a short position in the shares of a listed company or any associated company.

- The notification time limit allowed is 3 business days.

  The duty of disclosure is to the company and the SEHK. Failure to make disclosure within the time limits required by the SFO or the making of a statement which is false or misleading in any material particular constitutes a criminal offence carrying a maximum fine of HK$100,000 or maximum prison sentence of 2 years for each offence. Members and officers of a company can also be personally liable for the offences of a company.

Listing Rules

- Obligations of declaration and undertaking given on listing under Appendix 5 of the Main Board and GEM Listing Rules;
- Continuing obligations under Chapter 13 of the Main Board Listing Rules and Chapter 17 of the GEM Listing Rules, including a prohibition on directors voting on any board resolution relating to a matter in which they or any of their associates have a material interest (subject to specified exceptions);
- Obligations of disclosure of notifiable and connected transactions under Chapters 14 and 14A of the Main Board Listing Rules and Chapters 19 and 20 of the GEM Listing Rules.

Conflicts of Duty and Interest

Conflicts arise where a director's duties to the Company conflict with the personal interests of a director.

The obligation on directors to account for any profit does not depend on fraud or lack of good faith.

The director can genuinely believe he is acting in the best interest of the company and only making an incidental personal gain. Nevertheless, without approval he will be obliged to account for profit.

Furthermore, the directors are liable even if they have caused no loss to the company.

Contracts with the Company

At common law there is a general prohibition on directors contracting with a company of which they are a director, either directly or indirectly, even if the contract is fair and reasonable and negotiated at arms length. The principle behind the law is that if any director is interested in any contract into which the company intends to enter, he may be tempted to put his own personal interests before those of the company.

Exceptions

Subject to disclosure, the contract will be binding and valid provided there is either:-

- a general power in the Articles for directors to contract with the company; or
- specific approval of the members in general meeting.

Specific contracts

There are certain types of contract which require specific approval from the company in general meeting. General approval in the articles will not suffice. These are:

- Payment of compensation for loss of office (section 163 of the Companies Ordinance)
- Payment of compensation for loss of office in connection with the transfer of company property (section 163A of the Companies Ordinance)
- Payment of compensation for loss of office in connection with the transfer of shares in the company (section 163B of the Companies Ordinance)
- Payment of damages or pension to a director (section 163C of the Companies Ordinance)

Secret Profits

We mentioned above that directors have a duty not to make a secret profit from the company. Even where a director acting bona fide and in the best interest of the company enters into a contract on behalf of the company, which is extremely beneficial to the company, he will be in breach of fiduciary duty if he makes an undisclosed profit from that deal.

Diversion of Contracts

Where a director uses the company's assets or his position as director to generate a business opportunity which the company is capable of exploiting but which is then diverted to himself or a company owned by him, there is a clear breach of fiduciary duty and a glaring conflict of interest.

Loans to Directors

The very concept of directors making loans of company money to themselves raises potential for conflict of interests. For this reason, there is a general prohibition contained in section 157H(2) of the Companies Ordinance on a company either directly or indirectly:

- granting a loan to a director of the company or of its holding company or to a company controlled by such a director; or
- entering into any guarantee or providing any security in connection with any loan made by any person to such a director or a company controlled by such a director.

Sections 157H(3) and (4) contain further prohibitions on companies other than private companies (except a private company which is part of a group of which another member is listed) from making quasi-loans to, or entering into credit transactions as creditor for, a director of the company or of its holding company or a company controlled by such a director. The giving of any guarantee or security for such loans or credit transactions is also prohibited.

There are several exceptions to these prohibitions, which are set out in section 157HA eg. where the transaction entered into by a private company (not being part of a group of which another member is listed) is approved in general meeting (section 157HA(2)) or where the director requires funds to meet expenditure incurred for the purposes of the company or to enable the director properly to perform his duties as an officer of the company (section 157HA(3)(a)).

Where a valid transaction is entered into with a director or a connected party there is a requirement for the details of the transaction to be disclosed in the accounts of the company (section 161B).

For more details, please see Part II.

Insider Dealing and Other Market Misconduct

Insider dealing is a clear example of a director potentially making a secret profit. Insider dealing was a big problem in Hong Kong in the 1980's, so much so that in 1991 the Securities (Insider Dealing) Ordinance was brought into force and subsequently replaced by the Securities and Futures Ordinance which came into force on 1 April 2003. Sections 270 and 290 prohibit a director from making an unjustifiable profit by using confidential, price-sensitive information in dealing in the shares of a listed company.

This Ordinance established dual civil and criminal regimes (under Parts XIII and XIV) in respect of all types of market misconduct. "Market misconduct" as regulated under Parts XIII and XIV comprises of 6 offences: insider dealing, false trading, price rigging, disclosure of information about prohibited transactions, disclosure of false and misleading information inducing transactions and market manipulation.

Consequences of and Remedies for Breach of Duty

- **Injunction**

  If a breach is anticipated but has not yet occurred, an injunction may be appropriate to prevent the breach. If the directors propose to use their powers for an improper purpose, an injunction may prevent their so acting.

- **Rescission**

  Where the directors have failed to disclose their personal interest in a contract which they have entered into on behalf of the company, that contract may be avoided at the option of the company.

  Rescission is an equitable remedy. A contract cannot be rescinded if it is impossible to do so, if the company has gone into liquidation or if the contract has been adopted by the company.

- **Damages**

  All directors who are found to have acted in breach are jointly and severally liable to the company. Damages are the appropriate remedy where the directors are in breach of the common law duty of care.

- **Account of profits**

  The misapplication of the company's property renders the directors liable to account to the company in equity on the same basis as governs a misapplication of trust funds by trustees.

- **Personal Liability**

  Personal liability may be incurred where in the course of winding up a company it appears that any business of the company has been carried on with intent to defraud creditors or for any other fraudulent purpose. There is no limitation on the amount of liability which may be imposed (section 275 of the Companies Ordinance).

- **Disqualification**

  Please see below under the heading "Disqualification".

- **Ratification**

  A breach of duty leading to a conflict situation does not render a contract void but merely voidable at the option of the company, and the company in general meeting may ratify the transaction.

  Ratification by the shareholders in general meeting is not possible in the case of a fraud on the minority.

  If the director is also a member, he may vote on the transaction, provided there is no fraud on the minority.

- **Power of the Court to Grant Relief for Breach**

  Section 358 of the Companies Ordinance provides that if in any proceedings for negligence, default, breach of duty, or breach of trust against a director (inter alia) it appears to the court that he has acted honestly and reasonably, and that having regard to all the circumstances of the case he ought fairly to be excused, the court may relieve him, either wholly or in part, from liability on such terms as it thinks fit (section 358(1)).

  A director who anticipates that such a claim will or might be made against him may also apply to the court for relief (section 358(2)).

- **Indemnities and Insurance**

  Directors cannot absolve themselves from liability owed to the company or a related company by taking an indemnity from the company. Any such clause included in a company's Articles of Association has no effect. The law provides that any provision contained in the company's articles, or in any contract with the company or otherwise, for exempting a director from, or indemnifying him against, any liability to the company or a related company for negligence, default, breach of duty, or breach of trust, is void (section 165(1) of the Companies Ordinance).

A company is not, however, prohibited from indemnifying its directors against liabilities owed to third parties, such as shareholders and creditors. Companies are also entitled to indemnify their directors against the costs incurred by them in defending any proceedings, civil or criminal, in which judgment is given in their favour or in which they are acquitted, or where relief is granted under section 358 (section 165(2)). Table A, article 137 of the Companies Ordinance makes provision for such an indemnity.

In addition, companies are allowed to take out and maintain insurance policies for directors against liability to the company, a related company or third parties for negligence, default, breach of duty or trust (save for fraud) and also against any liability incurred in defending any proceedings for negligence, default, breach of duty or trust (including fraud) (section 165(3)).

Disqualification of Directors

Disqualification of directors is governed by:

- **Articles of Association** of the company;
- **Part IVA** of the Companies Ordinance; and
- **Securities and Futures Ordinance** - for breaches of this ordinance.

Part IVA of the Companies Ordinance provides four principal grounds on which a court may make a disqualification order against a director:

1. conviction of an indictable offence in connection with the promotion, formation, management, receivership or liquidation of a company or any other indictable offence which involves a finding that the director acted fraudulently or dishonestly (section 168E);
2. persistent default of the provisions of the Companies Ordinance requiring any return, account or other documents to be delivered to the companies registrar (section 168F);
3. if in the course of winding up the company, it appears that the director has been guilty of fraud in relation to the company or that the director has been guilty of fraudulent trading under section 275 of the Companies Ordinance (section 168G); and
4. if the court considers that the conduct of the director at any time the company is insolvent makes him unfit to be concerned in the management of a company (section 168H).

The last two grounds of disqualification also apply to a shadow director. A "shadow director" is defined in section 2 of the Companies Ordinance as "a person in accordance with whose directions or instructions the directors or a majority of a company's directors are accustomed to act". The definition excludes persons advising directors in a professional capacity.

Penalties for breach of disqualification order

Breach of a disqualification order renders a person liable to:

- a fine and imprisonment (section 168M of the Companies Ordinance);
- personal responsibility for the debts of a company incurred whilst disqualified (section 168O of the Companies Ordinance).

APPENDIX A
CODE ON CORPORATE GOVERNANCE PRACTICES

Copyright ownership in the Listing Rules, of which the Code on Corporate Governance Practices forms part, belongs to the Stock Exchange of Hong Kong Ltd.

MAIN BOARD

APPENDIX 14 OF THE MAIN BOARD LISTING RULES
CODE ON CORPORATE GOVERNANCE PRACTICES

This Code on Corporate Governance Practices sets out the principles of good corporate governance, and two levels of recommendations: (a) code provisions; and (b) recommended best practices.

Issuers are expected to comply with, but may choose to deviate from, the code provisions. The recommended best practices are for guidance only. Issuers may also devise their own code on corporate governance practices on such terms as they may consider appropriate.

Issuers must state whether they have complied with the code provisions set out in this Code for the relevant accounting period in their interim reports (and summary interim reports, if any) and annual reports (and summary financial reports, if any).

Every issuer must carefully review each code provision set out in this Code and, where the issuer deviates from any of the code provisions, the issuer must give considered reasons:

(a) in the case of annual reports (and summary financial reports), in the Corporate Governance Report which must be issued in accordance with Appendix 23; and

(b) in the case of interim reports (and summary interim reports), either:

(i) by giving considered reasons for each deviation; or

(ii) to the extent that it is reasonable and appropriate, by referring to the Corporate Governance Report in the immediately preceding annual report, and providing details of any changes together with considered reasons for any deviation not reported in that annual report. Such references must be clear and unambiguous and the interim report (or summary interim report) must not only contain a cross-reference without any discussion of the matter.

In the case of the recommended best practices, issuers are encouraged, but are not required, to state whether they have complied with them and give considered reasons for any deviation.

PRINCIPLES OF GOOD GOVERNANCE, CODE PROVISIONS AND RECOMMENDED BEST PRACTICES

A. DIRECTORS

A.I The Board

Principle

An issuer should be headed by an effective board which should assume responsibility for leadership and control of the issuer and be collectively responsible for promoting the success of the issuer by directing and supervising the issuer's affairs. Directors should take decisions objectively in the interests of the issuer.

Code Provisions

A.1.1 The board should meet regularly and board meetings should be held at least four times a year at approximately quarterly intervals. It is expected that such regular board meetings will normally involve the active participation, either in person or through other electronic means of communication, of a majority of directors entitled to be present. Accordingly, a regular meeting does not include the practice of obtaining board consent through the circulation of written resolutions.

A.1.2 Arrangements should be in place to ensure that, all directors are given an opportunity to include matters in the agenda for regular board meetings.

A.1.3 Notice of at least 14 days should be given of a regular board meeting to give all directors an opportunity to attend. For all other board meetings, reasonable notice should be given.

A.1.4 All directors should have access to the advice and services of the company secretary with a view to ensuring that board procedures, and all applicable rules and regulations, are followed.

A.1.5 Minutes of board meetings and meetings of board committees should be kept by a duly appointed secretary of the meeting and such minutes should be open for inspection at any reasonable time on reasonable notice by any director.

A.1.6 Minutes of board meetings and meetings of board committees should record in sufficient detail the matters considered by the board and decisions reached, including any concerns raised by directors or dissenting views expressed. Draft and final versions of minutes of board meetings should be sent to all directors for their comment and records respectively, in both cases within a reasonable time after the board meeting is held.

A.1.7 There should be a procedure agreed by the board to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the issuer's expense. The board should resolve to provide separate independent professional advice to directors to assist the relevant director or directors to discharge his/their duties to the issuer.

A.1.8 If a substantial shareholder or a director has a conflict of interest in a matter to be considered by the board which the board has determined to be material, the matter should not be dealt with by way of circulation or by a committee (except an appropriate board committee set up for that purpose pursuant to a resolution passed in a board meeting) but a board meeting should be held. Independent non-executive directors who, and whose associates, have no material interest in the transaction should be present at such board meeting.

Notes: 1 Directors are reminded of the requirement under rule 13.44 that they must abstain from voting on any board resolution in which they or any of their associates have a material interest and that they shall not be counted in the quorum present at the board meeting. The existing exceptions to the general voting prohibition are currently set out in note 1 to Appendix 3.

2 Such exceptions to the general voting prohibition should also be taken into account when considering whether a substantial shareholder or a director has a conflict of interest in a matter to be considered by the board. If the relevant exceptions apply, a regular board meeting need not be held. For this purpose, please refer to A.1.1 for the meaning of a regular board meeting.

Recommended Best Practices

A.1.9 An issuer should arrange appropriate insurance cover in respect of legal action against its directors.

A.1.10 Board committees should adopt, so far as practicable, the principles, procedures and arrangements set out in A.1.1 to A.1.8.

A.2 Chairman and Chief Executive Officer

Principle

There are two key aspects of the management of every issuer - the management of the board and the day-to-day management of the issuer's business. There should be a clear division of these responsibilities at the board level to ensure a balance of power and authority, so that power is not concentrated in any one individual.

Code Provisions

A.2.1 The roles of chairman and chief executive officer should be separate and should not be performed by the same individual. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing.

Note: Under paragraphs 2(c)(vii) and 2(d) of Appendix 23, issuers must disclose in their Corporate Governance Report the identity of the chairman and the chief executive officer and whether these two roles are segregated and the nature of any relationship (including financial, business, family or other material/relevant relationship(s)), if any, among members of the board and in particular, between the chairman and the chief executive officer.

A.2.2 The chairman should ensure that all directors are properly briefed on issues arising at board meetings.

A.2.3 The chairman should be responsible for ensuring that directors receive adequate information, which must be complete and reliable, in a timely manner.

Recommended Best Practices

A.2.4 One of the important roles of the chairman is to provide leadership for the board. The chairman should ensure that the board works effectively and discharges its responsibilities, and that all key and appropriate issues are discussed by the board in a timely manner. The chairman should be primarily responsible for drawing up and approving the agenda for each board meeting taking into account, where appropriate, any matters proposed by the other directors for inclusion in the agenda. The chairman may delegate such responsibility to a designated director or the company secretary.

A.2.5 The chairman should take responsibility for ensuring that good corporate governance practices and procedures are established.

A.2.6 The chairman should encourage all directors to make a full and active contribution to the board's affairs and take the lead to ensure that the board acts in the best interests of the issuer.

A.2.7 The chairman should at least annually hold meetings with the non-executive directors (including independent non-executive directors) without the executive directors present.

A.2.8 The chairman should ensure that appropriate steps are taken to provide effective communication with shareholders and that views of shareholders are communicated to the board as a whole.

A.2.9 The chairman should facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.

A.3 Board composition

Principle

The board should have a balance of skills and experience appropriate for the requirements of the business of the issuer. The board should ensure that changes to its composition can be managed without undue disruption. The board should include a balanced composition of executive and non-executive directors (including independent non-executive directors) so that there is a strong independent element on the board, which can effectively exercise independent judgement. Non-executive directors should be of sufficient calibre and number for their views to carry weight.

Notes: 1 Under rule 3.10, every board of directors of a listed issuer must include at least three independent non-executive directors.

2 Guidelines on independence of independent non-executive directors are set out in rule 3.13.

Code Provisions

A.3.1 The independent non-executive directors should be expressly identified as such in all corporate communications that disclose the names of directors of the issuer.

Note: Under paragraph 2(c)(i) of Appendix 23, issuers must disclose the composition of the board, by category of directors, including names of chairman, executive directors, non-executive directors and independent non-executive directors in the Corporate Governance Report.

Recommended Best Practices

A.3.2 An issuer should appoint independent non-executive directors representing at least one-third of the board.

A.3.3 An issuer should maintain on its website an updated list of its directors identifying their role and function and whether they are independent non-executive directors.

A.4 Appointments, re-election and removal

Principle

There should be a formal, considered and transparent procedure for the appointment of new directors to the board. There should be plans in place for orderly succession for appointments to the board. All directors should be subject to re-election at regular intervals. An issuer must explain the reasons for the resignation or removal of any director.

Code Provisions

A.4.1 Non-executive directors should be appointed for a specific term, subject to re-election.

Note: Under paragraph 2(e) of Appendix 23, issuers must disclose the term of appointment of non-executive directors in the Corporate Governance Report.

A.4.2 All directors appointed to fill a casual vacancy should be subject to election by shareholders at the first general meeting after their appointment. Every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years.

Notes: 1 The names of all directors submitted for election or re-election must be accompanied by the same biographical details as required for newly appointed directors set out in rule 13.51(2) (including other directorships held in listed public companies in the last three years and other major appointments) to enable shareholders to make an informed decision on their election.

2 If a director resigns or is removed from office, an issuer must comply with the disclosure requirements in rule 13.51(2) and include in its announcement about the director's resignation or removal the reasons given by the director for his resignation (including but not limited to information relating to a relevant director's disagreement with the issuer, if any, and a statement

confirming whether or not there are any matters that need to be brought to the attention of shareholders).

Recommended Best Practices

A.4.3 Serving more than nine years could be relevant to the determination of a non-executive director's independence. If an independent non-executive director serves more than 9 years, any further appointment of such independent non-executive director should be subject to a separate resolution to be approved by shareholders. The board should set out to shareholders in the papers accompanying a resolution to elect such an independent non-executive director the reasons they believe that the individual continues to be independent and why he should be re-elected.

A.4.4 Issuers should establish a nomination committee. A majority of the members of the nomination committee should be independent non-executive directors.

A.4.5 The nomination committee should be established with specific written terms of reference which deal clearly with the committee's authority and duties. It is recommended that the nomination committee should discharge the following duties:

(a) review the structure, size and composition (including the skills, knowledge and experience) of the board on a regular basis and make recommendations to the board regarding any proposed changes;

(b) identify individuals suitably qualified to become board members and select or make recommendations to the board on the selection of, individuals nominated for directorships;

(c) assess the independence of independent non-executive directors; and

(d) make recommendations to the board on relevant matters relating to the appointment or re-appointment of directors and succession planning for directors in particular the chairman and the chief executive officer.

A.4.6 The nomination committee should make available its terms of reference, explaining its role and the authority delegated to it by the board.

Notes: 1 This requirement could be met by making it available on request and by including the information on the issuer's website.

2 Under paragraph 2(g)(i) of Appendix 23, issuers must explain the role of the nomination committee (if any) in the Corporate Governance Report.

A.4.7 The nomination committee should be provided with sufficient resources to discharge its duties.

A.4.8 Where the board proposes a resolution to elect an individual as an independent non-executive director at the general meeting, it should set out in the circular to shareholders and/or explanatory statement accompanying the notice of the relevant general meeting why they believe the individual should be elected and the reasons why they consider the individual to be independent.

A.5 Responsibilities of directors

Principle

Every director is required to keep abreast of his responsibilities as a director of an issuer and of the conduct, business activities and development of that issuer. Given the essential unitary nature of the board, non-executive directors have the same duties of care and skill and fiduciary duties as executive directors.

Note: These duties are summarised in "the Non-statutory Guidelines of Directors' Duties" issued by the Companies Registry in January 2004. In determining whether a director has met the requisite standard of care, skill and diligence expected of him, courts will generally have regard to a number of factors. These include the functions that are to be performed by the director concerned, whether the director is a full-time executive director or a part-time non-executive director and the professional skills and knowledge of the director concerned.

Code Provisions

A.5.1 Every newly appointed director of an issuer should receive a comprehensive, formal and tailored induction on the first occasion of his appointment, and subsequently such briefing and professional development as is necessary, to ensure that he has a proper understanding of the operations and business of the issuer and that he is fully aware of his responsibilities under statute and common law, the Exchange Listing Rules, applicable legal requirements and other regulatory requirements and the business and governance policies of the issuer.

A.5.2 The functions of non-executive directors should include but should not be limited to the following:

(a) participating in board meetings of the issuer to bring an independent judgement to bear on issues of strategy, policy, performance, accountability, resources, key appointments and standards of conduct;

(b) taking the lead where potential conflicts of interests arise;

(c) serving on the audit, remuneration, nomination and other governance committees, if invited; and

(d) scrutinising the issuer's performance in achieving agreed corporate goals and objectives, and monitoring the reporting of performance.

A.5.3 Every director should ensure that he can give sufficient time and attention to the affairs of the issuer and should not accept the appointment if he cannot do so.

A.5.4 Directors must comply with their obligations under the Model Code set out in Appendix 10 and, in addition, the board should establish written guidelines on no less exacting terms than the Model Code for relevant employees in respect of their dealings in the securities of the issuer. For this purpose, "relevant employee" includes any employee of the issuer or a director or employee of a subsidiary or holding company of the issuer who, because of such office or employment, is likely to be in possession of unpublished price sensitive information in relation to the issuer or its securities.

Recommended Best Practices

A.5.5 All directors should participate in a programme of continuous professional development to develop and refresh their knowledge and skills to help ensure that their contribution to the board remains informed and relevant. The issuer should be responsible for arranging and funding a suitable development programme.

A.5.6 Each director should disclose to the issuer at the time of his appointment, and on a periodic basis, the number and nature of offices held in public companies or organisations and other significant commitments, with the identity of the public companies or organisations and an indication of the time involved. The board should determine for itself how frequently such disclosure should be made.

A.5.7 Non-executive directors, as equal board members, should give the board and any committees on which they serve such as the audit, remuneration or nomination committees the benefit of their skills, expertise and varied backgrounds and qualifications through regular attendance and active participation. They should also attend general meetings and develop a balanced understanding of the views of shareholders.

A.5.8 Non-executive directors should make a positive contribution to the development of the issuer's strategy and polices through independent, constructive and informed comments.

A.6 Supply of and access to information

Principle

Directors should be provided in a timely manner with appropriate information in such form and of such quality as will enable them to make an informed decision and to discharge their duties and responsibilities as directors of an issuer.

Code Provisions

A.6.1 In respect of regular board meetings, and so far as practicable in all other cases, an agenda and accompanying board papers should be sent in full to all directors in a timely manner and at least 3 days before the intended date of a board or board committee meeting (or such other period as agreed).

A.6.2 Management has an obligation to supply the board and its committees with adequate information in a timely manner to enable it to make informed decisions. The information supplied must be complete and reliable. To fulfil his duties properly a director may not in all circumstances be able to rely purely on what is volunteered by management and further enquiries may be required. Where any director requires more information than is volunteered by management, he should make further enquiries where necessary. The board and each director should have separate and independent access to the issuer's senior management.

Notes: 1 The information provided should include background or explanatory information relating to matters to be brought before the board, copies of disclosure documents, budgets, forecasts and monthly and other relevant internal financial statements. In respect of budgets, any material variance between the projections and actual results must also be disclosed and explained.

2 For the purpose of this Code, "senior management" should refer to the same category of persons as referred to in the issuer's annual report and is required to be disclosed under paragraph 12 of Appendix 16.

A.6.3 All directors are entitled to have access to board papers and related materials. Such papers and related materials should be prepared in such form and quality as will enable the board to make an informed decision on matters placed before it. Where queries are raised by directors, steps must be taken to respond as promptly and fully as possible.

B. REMUNERATION OF DIRECTORS AND SENIOR MANAGEMENT

B.1 The level and make-up of remuneration and disclosure

Principle

An issuer should disclose information relating to its directors' remuneration policy and other remuneration related matters. There should be a formal and transparent procedure for setting policy on executive directors' remuneration and for fixing the remuneration packages for all directors. Levels of remuneration should be sufficient to attract and retain the directors needed to run the company successfully, but companies should avoid paying more than is necessary for this purpose. No director should be involved in deciding his own remuneration.

Notes: 1 Under paragraph 24B of Appendix 16, issuers are required to give a general description of the emolument policy and long-term incentive schemes of the group as well as the basis of determining the emolument payable to their directors.

2 Under paragraph 24 of Appendix 16, directors' fees and any other reimbursement or emolument payable to a director must be disclosed in full in the annual reports and accounts of the issuer on an individual and named basis.

Code Provisions

B.1.1 Issuers should establish a remuneration committee with specific written terms of reference which deal clearly with its authority and duties. A majority of the members of the remuneration committee should be independent non-executive directors.

B.1.2 The remuneration committee should consult the chairman and/or chief executive officer about their proposals relating to the remuneration of other executive directors and have access to professional advice if considered necessary.

B.1.3 The terms of reference of the remuneration committee should include, as a minimum, the following specific duties:-

(a) to make recommendations to the board on the issuer's policy and structure for all remuneration of directors and senior management and on the establishment of a formal and transparent procedure for developing policy on such remuneration;

Note: For the purpose of this Code, "senior management" should refer to the same category of persons as referred to in the issuer's annual report and is required to be disclosed under paragraph 12 of Appendix 16.

(b) to have the delegated responsibility to determine the specific remuneration packages of all executive directors and senior management, including benefits in kind, pension rights and compensation payments, including any compensation payable for loss or termination of their office or appointment, and make recommendations to the board of the remuneration of non-executive directors. The remuneration committee should consider factors such as salaries paid by comparable companies, time commitment and responsibilities of the directors, employment conditions elsewhere in the group and desirability of performance-based remuneration;

Note: Please refer to the Note to B.1.3(a) of this Code for the definition of "senior management".

(c) to review and approve performance-based remuneration by reference to corporate goals and objectives resolved by the board from time to time;

(d) to review and approve the compensation payable to executive directors and senior management in connection with any loss or termination of their office or appointment to ensure that such compensation is determined in accordance with relevant contractual terms and that such compensation is otherwise fair and not excessive for the issuer;

Note: Please refer to the Note to B.1.3(a) of this Code for the definition of "senior management".

(e) to review and approve compensation arrangements relating to dismissal or removal of directors for misconduct to ensure that such arrangements are determined in accordance with relevant contractual terms and that any compensation payment is otherwise reasonable and appropriate; and

(f) to ensure that no director or any of his associates is involved in deciding his own remuneration.

Note: The remuneration committee shall advise shareholders on how to vote with respect to any service contracts of directors that require shareholders' approval under rule 13.68.

B.1.4 The remuneration committee should make available its terms of reference, explaining its role and the authority delegated to it by the board.

Notes: 1 This requirement could be met by making it available on request and by including the information on the issuer's website.

2 Under paragraph 2(f)(i) of Appendix 23, issuers must explain the role of the remuneration committee (if any) in the Corporate Governance Report.

B.1.5 The remuneration committee should be provided with sufficient resources to discharge its duties.

Recommended Best Practices

B.1.6 A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance.

B.1.7 Issuers should disclose details of any remuneration payable to members of senior management, on an individual and named basis, in their annual reports and accounts.

Notes: 1 Issuers should disclose details of any remuneration payable to members of senior management. Such disclosure should be to the same standard as that required for directors of issuers under paragraph 24 of Appendix 16.

2 For the purpose of this Code, "senior management" should refer to the same category of persons as referred to in the issuer's annual report and is required to be disclosed under paragraph 12 of Appendix 16.

B.1.8 Where the board resolves to approve any remuneration or compensation arrangements which the remuneration committee has previously resolved not to approve, the board must disclose the reasons for its resolution in its next annual report.

C. ACCOUNTABILITY AND AUDIT

C.1 Financial reporting

Principle

The board should present a balanced, clear and comprehensible assessment of the company's performance, position and prospects.

Code Provisions

C. 1.1 Management should provide such explanation and information to the board as will enable the board to make an informed assessment of the financial and other information put before the board for approval.

Note: Issuers are reminded of their obligation to comply with the financial reporting and disclosure requirements set out in the Exchange Listing Rules. Failure to comply with such requirements constitutes a breach of the Exchange Listing Rules.

C.1.2 The directors should acknowledge in the Corporate Governance Report their responsibility for preparing the accounts, and there should be a statement by the auditors about their reporting responsibilities in the auditors' report on the financial statements. Unless it is inappropriate to assume that the company will continue in business, the directors should prepare the accounts on a going concern basis, with supporting assumptions or qualifications as necessary. When the directors are aware of material uncertainties relating to events or conditions that may cast significant doubt upon the issuer's ability to continue as a going concern, such uncertainties should be clearly and prominently set out and discussed at length in the Corporate Governance Report. The Corporate Governance Report should contain sufficient information so as to enable investors to understand the severity and significance of the matters at hand. To the extent that it is reasonable and appropriate, the issuer may refer to the other relevant parts of the annual report. Any such references should be clear and unambiguous and the Corporate Governance Report should not only contain a cross-reference without any discussion of the matter.

C.1.3 The board's responsibility to present a balanced, clear and understandable assessment extends to annual and interim reports, other price-sensitive announcements and other financial disclosures required under the Exchange Listing Rules, and reports to regulators as well as to information required to be disclosed pursuant to statutory requirements.

Recommended Best Practices

C.1.4 An issuer should announce and publish quarterly financial results within 45 days after the end of the relevant quarter, disclosing such information as would enable shareholders to assess the performance, financial position and prospects of the issuer. Any such quarterly financial reports should be prepared using the accounting policies applied to the issuer's half-year and annual accounts.

C.1.5 Once an issuer decides to announce and publish its quarterly financial results, it should continue to adopt quarterly reporting for each of the first 3 and 9 months periods of subsequent financial years. Where the issuer decides not to announce and publish its financial results for a particular quarter, it should publish an announcement to disclose the reason(s) for such decision.

C.2 Internal controls

Principle

The board should ensure that the issuer maintains sound and effective internal controls to safeguard the shareholders' investment and the issuer's assets.

Code Provisions

C.2.1 The directors should at least annually conduct a review of the effectiveness of the system of internal control of the issuer and its subsidiaries and report to shareholders that they have done so in their Corporate Governance Report. The review should cover all material controls, including financial, operational and compliance controls and risk management functions.

Recommended Best Practices

C.2.2 The board's annual review should, in particular, consider:

(a) the changes since the last annual review in the nature and extent of significant risks, and the issuer's ability to respond to changes in its business and the external environment;

(b) the scope and quality of management's ongoing monitoring of risks and of the system of internal control, and where applicable, the work of its internal audit function and other providers of assurance;

(c) the extent and frequency of the communication of the results of the monitoring to the board (or board committee(s)) which enables it to build up a cumulative assessment of the state of control in the issuer and the effectiveness with which risk is being managed;

(d) the incidence of significant control failings or weakness that has been identified at any time during the period and the extent to which they have resulted in unforeseen outcomes or contingencies that have had, could have had, or may in the future have, a material impact on the issuer's financial performance or condition; and

(e) the effectiveness of the issuer's processes relating to financial reporting and Listing Rule compliance.

C.2.3 Issuers should disclose as part of the Corporate Governance Report a narrative statement how they have complied with the code provisions on internal control during the reporting period. The disclosures should also include the following items:

(a) the process that an issuer has applied for identifying, evaluating and managing the significant risks faced by it;

(b) any additional information to assist understanding of the issuer's risk management processes and system of internal control;

(c) an acknowledgement by the board that it is responsible for the issuer's system of internal control and for reviewing its effectiveness;

(d) the process that an issuer has applied in reviewing the effectiveness of the system of internal control; and

(e) the process that an issuer has applied to deal with material internal control aspects of any significant problems disclosed in its annual reports and accounts.

C.2.4 Issuers should ensure that their disclosures provide meaningful information and do not give a misleading impression.

C.2.5 Issuers without an internal audit function should review the need for one on an annual basis and should disclose the outcome of such review in the issuers' Corporate Governance Report.

C.3 Audit Committee

Principle

The board should establish formal and transparent arrangements for considering how it will apply the financial reporting and internal control principles and for maintaining an appropriate relationship with the company's auditors. The audit committee established by an issuer pursuant to the Exchange Listing Rules should have clear terms of reference.

Code Provisions

C.3.1 Full minutes of audit committee meetings should be kept by a duly appointed secretary of the meeting (who should normally be the company secretary). Draft and final versions of minutes of the audit committee meetings should be sent to all members of the committee for their comment and records respectively, in both cases within a reasonable time after the meeting.

C.3.2 A former partner of the issuer's existing auditing firm should be prohibited from acting as a member of the issuer's audit committee for a period of 1 year commencing on the date of his ceasing:

(a) to be a partner of the firm; or

(b) to have any financial interest in the firm,

whichever is the later.

C.3.3 The terms of reference of the audit committee should include at least the following duties:

Relationship with the issuer's auditors

(a) to be primarily responsible for making recommendation to the board on the appointment, reappointment and removal of the external auditor, and to approve the remuneration and terms of engagement of the external auditor, and any questions of resignation or dismissal of that auditor;

Note: Issuers are reminded that rule 13.51(4) requires an announcement to be published when there is a change of auditors. The announcement must also include a statement as to whether there are any matters that need to be brought to holders of securities of the issuer.

(b) to review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process in accordance with applicable standard. The audit committee should discuss with the auditor the nature and scope of the audit and reporting obligations before the audit commences;

(c) to develop and implement policy on the engagement of an external auditor to supply non-audit services. For this purpose, external auditor shall include any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and

informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally. The audit committee should report to the board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken;

Review of financial information of the issuer

(d) to monitor integrity of financial statements of an issuer and the issuer's annual report and accounts, half-year report and, if prepared for publication, quarterly reports, and to review significant financial reporting judgements contained in them. In this regard, in reviewing the issuer's annual report and accounts, half-year report and, if prepared for publication, quarterly reports before submission to the board, the committee should focus particularly on:-

  (i) any changes in accounting policies and practices;

  (ii) major judgmental areas;

  (iii) significant adjustments resulting from audit;

  (iv) the going concern assumptions and any qualifications;

  (v) compliance with accounting standards; and

  (vi) compliance with the Exchange Listing Rules and other legal requirements in relation to financial reporting;

(e) In regard to (d) above:-

  (i) members of the committee must liaise with the issuer's board of directors, senior management and the person appointed as the issuer's qualified accountant and the committee must meet, at least once a year, with the issuer's auditors; and

  (ii) the committee should consider any significant or unusual items that are, or may need to be, reflected in such reports and accounts and must give due consideration to any matters that have been raised by the issuer's qualified accountant, compliance officer or auditors;

Oversight of the issuer's financial reporting system and internal control procedures

(f) to review the issuer's financial controls, internal control and risk management systems;

(g) to discuss with the management the system of internal control and ensure that management has discharged its duty to have an effective internal control system;

(h) to consider any findings of major investigations of internal control matters as delegated by the board or on its own initiative and management's response;

(i) where an internal audit function exists, to ensure co-ordination between the internal and external auditors, and to ensure that the internal audit function is adequately resourced and has appropriate standing within the issuer, and to review and monitor the effectiveness of the internal audit function;

(j) to review the group's financial and accounting policies and practices;

(k) to review the external auditor's management letter, any material queries raised by the auditor to management in respect of the accounting records, financial accounts or systems of control and management's response;

(l) to ensure the board will provide a timely response to the issues raised in the external auditor's management letter;

(m) to report to the board on the matters set out in this code provision; and

(n) to consider other topics, as defined by the board.

Notes: The following are only intended to be suggestions as to how compliance with the above code provision may be achieved and do not form part of the code provision.

1 The audit committee may wish to consider establishing the following procedure to review and monitor the independence of external auditors:-

(i) consider all relationships between the issuer and the audit firm (including the provision of non-audit services);

(ii) seek from the audit firm, on an annual basis, information about policies and processes for maintaining independence

and monitoring compliance with relevant requirements, including current requirements regarding rotation of audit partners and staff; and

(iii) meet with the auditor, at least annually, in the absence of management, to discuss matters relating to its audit fees, any issues arising from the audit and any other matters the auditor may wish to raise.

2 The audit committee may wish to consider agreeing with the board the issuer's policies relating to the hiring of employees or former employees of the external auditors and monitor the application of such policies. The audit committee should then be in a position to consider whether in the light of this there has been any impairment or appearance of impairment, of the auditor's judgement or independence in respect of the audit.

3 The audit committee would normally be expected to ensure that the provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditor's independence or objectivity in relation to the provision of non-audit services, the audit committee may wish to consider:

(i) whether the skills and experience of the audit firm make it a suitable supplier of the non-audit services;

(ii) whether there are safeguards in place to ensure that there is no threat to objectivity and independence in the conduct of the audit resulting from the provision of such services by the external auditor;

(iii) the nature of the non-audit services, the related fee levels and the fee levels individually and in aggregate relative to the audit firm; and

(iv) the criteria which govern the compensation of the individuals performing the audit.

4 For further guidance on the duties of an audit committee, issuers may refer to the "Principles of Auditor Independence and the Role of Corporate Governance in Monitoring an Auditor's Independence" issued by the Technical Committee of the International Organization of Securities Commissions in October 2002 and "A Guide for Effective Audit Committees"

published by the Hong Kong Society of Accountants (as it was then known) in February 2002. Issuers may also adopt the terms of reference set out in those guides, or they may adopt any other comparable terms of reference for the establishment of an audit committee.

C.3.4 The audit committee should make available its terms of reference, explaining its role and the authority delegated to it by the board.

Notes: 1 This requirement could be met by making it available on request and by including the information on the issuer's website.

2 Under paragraph 2(i)(i) of Appendix 23, issuers must explain the role of the audit committee in the Corporate Governance Report.

C.3.5 Where the board disagrees with the audit committee's view on the selection, appointment, resignation or dismissal of the external auditors, the issuer should include in the Corporate Governance Report a statement from the audit committee explaining its recommendation and also the reason(s) why the board has taken a different view.

C.3.6 The audit committee should be provided with sufficient resources to discharge its duties.

Recommended Best Practices

C.3.7 The terms of reference of the audit committee should also require the audit committee:

(a) to review arrangements by which employees of the issuer may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. The audit committee should ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action; and

(b) to act as the key representative body for overseeing the issuer's relation with the external auditor.

D. DELEGATION BY THE BOARD

D.1 Management functions

Principle

An issuer should have a formal schedule of matters specifically reserved to the board for its decision. The board should give clear directions to management as to the matters that must be approved by the board before decisions are made on behalf of the issuer.

Code Provisions

D.1.1 When the board delegates aspects of its management and administration functions to management, it must at the same time give clear directions as to the powers of management, in particular, with respect to the circumstances where management should report back and obtain prior approval from the board before making decisions or entering into any commitments on behalf of the issuer.

Note: The board should not delegate matters to a board committee, executive directors or management to an extent that would significantly hinder or reduce the ability of the board as a whole to discharge its functions.

D.1.2 An issuer should formalise the functions reserved to the board and those delegated to management. It should review those arrangements on a periodic basis to ensure that they remain appropriate to the needs of the issuer.

Note: Under paragraph 2(c)(iv) of Appendix 23, issuers must include in their Corporate Governance Report a statement of how the board operates, including a high level statement of which types of decisions are to be taken by the board and which are to be delegated to management.

Recommended Best Practices

D.1.3 An issuer should disclose the division of responsibility between the board and management to assist those affected by corporate decisions to better understand the respective accountabilities and contributions of the board and management.

D.1.4 Directors should clearly understand delegation arrangements in place. To that end, issuers should have formal letters of appointment for directors setting out the key terms and conditions relative to their appointment.

D.2 Board Committees

Principle

Board committees should be formed with specific written terms of reference which deal clearly with the committees' authority and duties.

Code Provisions

D.2.1 Where board committees are established to deal with matters, the board should prescribe sufficiently clear terms of reference to enable such committees to discharge their functions properly.

D.2.2 The terms of reference of board committees should require such committees to report back to the board on their decisions or recommendations, unless there are legal or regulatory restrictions on their ability to do so (such as a restriction on disclosure due to regulatory requirements).

E. COMMUNICATION WITH SHAREHOLDERS

E.1 Effective communication

Principle

The board should endeavour to maintain an on-going dialogue with shareholders and in particular, use annual general meetings or other general meetings to communicate with shareholders and encourage their participation.

Code Provisions

E.1.1 In respect of each substantially separate issue at a general meeting, a separate resolution should be proposed by the chairman of that meeting.

Note: An example of a substantially separate issue is the nomination of persons as directors. Accordingly, each such person should be nominated by means of a separate resolution.

E.1.2 The chairman of the board should attend the annual general meeting and arrange for the chairmen of the audit, remuneration and nomination committees (as appropriate) or in the absence of the chairman of such committees, another member of the committee or failing this his duly appointed delegate, to be available to answer questions at the annual general meeting. The chairman of the independent board committee (if any) should also be available to answer questions at any general meeting to approve a connected transaction or any other transaction that is subject to independent shareholders' approval.

E.2 Voting by Poll

Principle

The issuer should regularly inform shareholders of the procedure for voting by poll and ensure compliance with the requirements about voting by poll contained in the Exchange Listing Rules and the constitutional documents of the issuer.

Code Provisions

E.2.1 The chairman of a meeting should ensure disclosure in the issuer's circulars to shareholders of the procedures for and the rights of shareholders to demand a poll in compliance with the requirements about voting by poll contained in rule 13.39(4). In particular, pursuant to rule 13.39(3), the chairman of a meeting and/or directors who, individually or collectively, hold proxies in respect of shares representing 5% or more of the total voting rights at a particular meeting shall demand a poll in certain circumstances where, on a show of hands, a meeting votes in the opposite manner to that instructed in those proxies. If a poll is required under such circumstances, the chairman of the meeting should disclose to the meeting the total number of votes represented by all proxies held by directors indicating an opposite vote to the votes cast at the meeting on a show of hands.

E.2.2 The issuer should count all proxy votes and, except where a poll is required, the chairman of a meeting should indicate to the meeting the level of proxies lodged on each resolution, and the balance for and against the resolution, after it has been dealt with on a show of hands. The issuer should ensure that votes cast are properly counted and recorded.

E.2.3 The chairman of a meeting should at the commencement of the meeting ensure that an explanation is provided of:-

(a) the procedures for demanding a poll by shareholders before putting a resolution to the vote on a show of hands; and

(b) the detailed procedures for conducting a poll and then answer any questions from shareholders whenever voting by way of a poll is required.

APPENDIX 15 OF THE GEM LISTING RULES
CODE ON CORPORATE GOVERNANCE PRACTICES

This Code on Corporate Governance Practices sets out the principles of good corporate governance, and two levels of recommendations: (a) code provisions; and (b) recommended best practices.

Issuers are expected to comply with, but may choose to deviate from, the code provisions. The recommended best practices are for guidance only. Issuers may also devise their own code on corporate governance practices on such terms as they may consider appropriate.

Issuers must state whether they have complied with the code provisions set out in this Code for the relevant accounting period in their half-year reports (and summary half-year reports, if any) and annual reports (and summary financial reports, if any).

Every issuer must carefully review each code provision set out in this Code and, where the issuer deviates from any of the code provisions, the issuer must give considered reasons:

(a) in the case of annual reports (and summary financial reports), in the Corporate Governance Report which must be issued in accordance with Appendix 16; and

(b) in the case of half-year reports (and summary half-year reports), either:

(i) by giving considered reasons for each deviation; or

(ii) to the extent that it is reasonable and appropriate, by referring to the Corporate Governance Report in the immediately preceding annual report, and providing details of any changes together with considered reasons for any deviation not reported in that annual report. Such references must be clear and unambiguous and the half-year report (or summary half-year report) must not only contain a cross-reference without any discussion of the matter.

In the case of the recommended best practices, issuers are encouraged, but are not required, to state whether they have complied with them and give considered reasons for any deviation.

PRINCIPLES OF GOOD GOVERNANCE, CODE PROVISIONS AND RECOMMENDED BEST PRACTICES

A. DIRECTORS

A.1 The Board

Principle

An issuer should be headed by an effective board which should assume responsibility for leadership and control of the issuer and be collectively responsible for promoting the success of the issuer by directing and supervising the issuer's affairs. Directors should take decisions objectively in the interests of the issuer.

Code Provisions

A.1.1 The board should meet regularly and board meetings should be held at least four times a year at approximately quarterly intervals. It is expected that such regular board meetings will normally involve the active participation, either in person or through other electronic means of communication, of a majority of directors entitled to be present. Accordingly, a regular meeting does not include the practice of obtaining board consent through the circulation of written resolutions.

A.1.2 Arrangements should be in place to ensure that all directors are given an opportunity to include matters in the agenda for regular board meetings.

A.1.3 Notice of at least 14 days should be given of a regular board meeting to give all directors an opportunity to attend. For all other board meetings, reasonable notice should be given.

A.1.4 All directors should have access to the advice and services of the company secretary with a view to ensuring that board procedures, and all applicable rules and regulations, are followed.

A.1.5 Minutes of board meetings and meetings of board committees should be kept by a duly appointed secretary of the meeting and such minutes should be open for inspection at any reasonable time on reasonable notice by any director.

A.1.6 Minutes of board meetings and meetings of board committees should record in sufficient detail the matters considered by the board and decisions reached, including any concerns raised by directors or dissenting views expressed. Draft and final versions of minutes of board meetings should be sent to all directors for their comment and records respectively,

in both cases within a reasonable time after the board meeting is held.

A.1.7 There should be a procedure agreed by the board to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the issuer's expense. The board should resolve to provide separate independent professional advice to directors to assist the relevant director or directors to discharge his/their duties to the issuer.

A.1.8 If a substantial shareholder or a director has a conflict of interest in a matter to be considered by the board which the board has determined to be material, the matter should not be dealt with by way of circulation or by a committee (except an appropriate board committee set up for that purpose pursuant to a resolution passed in a board meeting) but a board meeting should be held. Independent non-executive directors who, and whose associates, have no material interest in the transaction should be present at such board meeting.

Notes: 1 Directors are reminded of the requirement under rule 17.48A that they must abstain from voting on any board resolution in which they or any of their associates have a material interest and that they shall not be counted in the quorum present at the board meeting. The existing exceptions to the general voting prohibition are currently set out in note 5 to Appendix 3.

2 Such exceptions to the general voting prohibition should also be taken into account when considering whether a substantial shareholder or a director has a conflict of interest in a matter to be considered by the board. If the relevant exceptions apply, a regular board meeting need not be held. For this purpose, please refer to A.1.1 for the meaning of a regular board meeting.

Recommended Best Practices

A.1.9 An issuer should arrange appropriate insurance cover in respect of legal action against its directors.

A.1.10 Board committees should adopt, so far as practicable, the principles, procedures and arrangements set out in A.1.1 to A.1.8.

A.2 Chairman and Chief Executive Officer

Principle

There are two key aspects of the management of every issuer - the management of the board and the day-to-day management of the issuer's business. There should be a clear division of these responsibilities at the board level to ensure a balance of power and authority, so that power is not concentrated in any one individual.

Code Provisions

A.2.1 The roles of chairman and chief executive officer should be separate and should not be performed by the same individual. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing.

Note: Under paragraphs 2(c)(vii) and 2(d) of Appendix 16, issuers must disclose in their Corporate Governance Report the identity of the chairman and the chief executive officer and whether these two roles are segregated and the nature of any relationship (including financial, business, family or other material/relevant relationship(s)), if any, among members of the board and in particular, between the chairman and the chief executive officer.

A.2.2 The chairman should ensure that all directors are properly briefed on issues arising at board meetings.

A.2.3 The chairman should be responsible for ensuring that directors receive adequate information, which must be complete and reliable, in a timely manner.

Recommended Best Practices

A.2.4 One of the important roles of the chairman is to provide leadership for the board. The chairman should ensure that the board works effectively and discharges its responsibilities, and that all key and appropriate issues are discussed by the board in a timely manner. The chairman should be primarily responsible for drawing up and approving the agenda for each board meeting taking into account, where appropriate, any matters proposed by the other directors for inclusion in the agenda. The chairman may delegate such responsibility to a designated director or the company secretary.

A.2.5 The chairman should take responsibility for ensuring that good corporate governance practices and procedures are established.

A.2.6 The chairman should encourage all directors to make a full and active contribution to the board's affairs and take the lead to ensure that the board acts in the best interests of the issuer.

A.2.7 The chairman should at least annually hold meetings with the non-executive directors (including independent non-executive directors) without the executive directors present.

A.2.8 The chairman should ensure that appropriate steps are taken to provide effective communication with shareholders and that views of shareholders are communicated to the board as a whole.

A.2.9 The chairman should facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.

A.3 Board composition

Principle

The board should have a balance of skills and experience appropriate for the requirements of the business of the issuer. The board should ensure that changes to its composition can be managed without undue disruption. The board should include a balanced composition of executive and non-executive directors (including independent non-executive directors) so that there is a strong independent element on the board, which can effectively exercise independent judgement. Non-executive directors should be of sufficient calibre and number for their views to carry weight.

Notes: 1 Under rule 5.05, every board of directors of a listed issuer must include at least three independent non-executive directors.

2 Guidelines on independence of independent non-executive directors are set out in rule 5.09.

Code Provisions

A.3.1 The independent non-executive directors should be expressly identified as such in all corporate communications that disclose the names of directors of the issuer.

Note: Under paragraph 2(c)(i) of Appendix 16, issuers must disclose the composition of the board, by category of directors, including names of chairman, executive directors, non-executive directors and independent non-executive directors in the Corporate Governance Report.

Recommended Best Practices

A.3.2 An issuer should appoint independent non-executive directors representing at least one-third of the board.

A.3.3 An issuer should maintain on its website an updated list of its directors identifying their role and function and whether they are independent non-executive directors.

A.4 Appointments, re-election and removal

Principle

There should be a formal, considered and transparent procedure for the appointment of new directors to the board. There should be plans in place for orderly succession for appointments to the board. All directors should be subject to re-election at regular intervals. An issuer must explain the reasons for the resignation or removal of any director.

Code Provisions

A.4.1 Non-executive directors should be appointed for a specific term, subject to re-election.

Note: Under paragraph 2(e) of Appendix 16, issuers must disclose the term of appointment of non-executive directors in the Corporate Governance Report.

A.4.2 All directors appointed to fill a casual vacancy should be subject to election by shareholders at the first general meeting after their appointment. Every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years.

Notes: 1 The names of all directors submitted for election or re-election must be accompanied by the same biographical details as required for newly appointed directors set out in rule 17.50(2) (including other directorships held in listed public companies in the last three years and other major appointments) to enable shareholders to make an informed decision on their election.

2 If a director resigns or is removed from office, an issuer must comply with the disclosure requirements in rule 17.50(2) and include in its announcement about the director's resignation or removal the reasons given by the director for his resignation

(including but not limited to information relating to a relevant director's disagreement with the issuer, if any, and a statement confirming whether or not there are any matters that need to be brought to the attention of shareholders).

Recommended Best Practices

A.4.3 Serving more than nine years could be relevant to the determination of a non-executive director's independence. If an independent non-executive director serves more than 9 years, any further appointment of such independent non-executive director should be subject to a separate resolution to be approved by shareholders. The board should set out to shareholders in the papers accompanying a resolution to elect such an independent non-executive director the reasons they believe that the individual continues to be independent and why he should be re-elected.

A.4.4 Issuers should establish a nomination committee. A majority of the members of the nomination committee should be independent non-executive directors.

A.4.5 The nomination committee should be established with specific written terms of reference which deal clearly with the committee's authority and duties. It is recommended that the nomination committee should discharge the following duties:-

(a) review the structure, size and composition (including the skills, knowledge and experience) of the board on a regular basis and make recommendations to the board regarding any proposed changes;

(b) identify individuals suitably qualified to become board members and select or make recommendations to the board on the selection of, individuals nominated for directorships;

(c) assess the independence of independent non-executive directors; and

(d) make recommendations to the board on relevant matters relating to the appointment or re-appointment of directors and succession planning for directors in particular the chairman and the chief executive officer.

A.4.6 The nomination committee should make available its terms of reference explaining its role and the authority delegated to it by the board.

Notes: 1 This requirement could be met by making it available on request and by including the information on the issuer's website.

2 *Under paragraph 2(g)(i) of Appendix 16, issuers must explain the role of the nomination committee (if any) in the Corporate Governance Report.*

A.4.7 The nomination committee should be provided with sufficient resources to discharge its duties.

A.4.8 Where the board proposes a resolution to elect an individual as an independent non-executive director at the general meeting, it should set out in the circular to shareholders and/or explanatory statement accompanying the notice of the relevant general meeting why they believe the individual should be elected and the reasons why they consider the individual to be independent.

A.5 Responsibilities of directors

Principle

Every director is required to keep abreast of his responsibilities as a director of an issuer and of the conduct, business activities and development of that issuer. Given the essential unitary nature of the board, non-executive directors have the same duties of care and skill and fiduciary duties as executive directors.

Note: These duties are summarised in "Non-statutory Guidelines of Directors' Duties" issued by the Companies Registry in January 2004. In determining whether a director has met the requisite standard of care, skill and diligence expected of him, courts will generally have regard to a number of factors. These include the functions that are to be performed by the director concerned, whether the director is a full-time executive director or a part-time non-executive director and the professional skills and knowledge of the director concerned.

Code Provisions

A.5.1 Every newly appointed director of an issuer should receive a comprehensive, formal and tailored induction on the first occasion of his appointment, and subsequently such briefing and professional development as is necessary, to ensure that he has a proper understanding of the operations and business of the issuer and that he is fully aware of his responsibilities under statute and common law, the GEM Listing Rules, applicable legal requirements and other regulatory requirements and the business and governance policies of the issuer.

A.5.2 The functions of non-executive directors should include but should not be limited to the following:

(a) participating in board meetings of the issuer to bring an independent judgement to bear on issues of strategy, policy, performance, accountability, resources, key appointments and standards of conduct;

(b) taking the lead where potential conflicts of interests arise;

(c) serving on the audit, remuneration, nomination and other governance committees, if invited; and

(d) scrutinising the issuer's performance in achieving agreed corporate goals and objectives, and monitoring the reporting of performance.

A.5.3 Every director should ensure that he can give sufficient time and attention to the affairs of the issuer and should not accept the appointment if he cannot do so.

A.5.4 Directors must comply with their obligations under the required standard of dealings set out in rules 5.48 to 5.67 and, in addition, the board should establish written guidelines on no less exacting terms than the required standard of dealings for relevant employees in respect of their dealings in the securities of the issuer. For this purpose, "relevant employee" includes any employee of the issuer or a director or employee of a subsidiary or holding company of the issuer who, because of such office or employment, is likely to be in possession of unpublished price sensitive information in relation to the issuer or its securities.

Recommended Best Practices

A.5.5 All directors should participate in a programme of continuous professional development to develop and refresh their knowledge and skills to help ensure that their contribution to the board remains informed and relevant. The issuer should be responsible for arranging and funding a suitable development programme.

A.5.6 Each director should disclose to the issuer at the time of his appointment, and on a periodic basis, the number and nature of offices held in public companies or organisations and other significant commitments, with the identity of the public companies or organisations and an indication of the time involved. The board should determine for itself how frequently such disclosure should be made.

A.5.7 Non-executive directors, as equal board members, should give the board and any committees on which they serve such as the audit, remuneration or nomination committees the benefit of their skills, expertise and varied backgrounds and qualifications through regular attendance and active

participation. They should also attend general meetings and develop a balanced understanding of the views of shareholders.

A.5.8 Non-executive directors should make a positive contribution to the development of the issuer's strategy and policies through independent, constructive and informed comments.

A.6 Supply of and access to information

Principle

Directors should be provided in a timely manner with appropriate information in such form and of such quality as will enable them to make an informed decision and to discharge their duties and responsibilities as directors of an issuer.

Code Provisions

A.6.1 In respect of regular board meetings, and so far as practicable in all other cases, an agenda and accompanying board papers should be sent in full to all directors in a timely manner and at least 3 days before the intended date of a board or board committee meeting (or such other period as agreed).

A.6.2 Management has an obligation to supply the board and its committees with adequate information in a timely manner to enable it to make informed decisions. The information supplied must be complete and reliable. To fulfil his duties properly a director may not in all circumstances be able to rely purely on what is volunteered by management and further enquiries may be required. Where any director requires more information than is volunteered by management, he should make further enquiries where necessary. The board and each director should have separate and independent access to the issuer's senior management.

Notes: 1 The information provided should include background or explanatory information relating to matters to be brought before the board, copies of disclosure documents, budgets, forecasts and monthly and other relevant internal financial statements. In respect of budgets, any material variance between the projections and actual results must also be disclosed and explained.

2 For the purpose of this Code, "senior management" should refer to the same category of persons as referred to in the issuer's annual report and is required to be disclosed under rule 18.39.

A.6.3 All directors are entitled to have access to board papers and related materials. Such papers and related materials should be prepared in such form and quality as will enable the board to make an informed decision on matters placed before it. Where queries are raised by directors, steps must be taken to respond as promptly and fully as possible.

B. REMUNERATION OF DIRECTORS AND SENIOR MANAGEMENT

B.1 The level and make-up of remuneration and disclosure

Principle

An issuer should disclose information relating to its directors' remuneration policy and other remuneration related matters. There should be a formal and transparent procedure for setting policy on executive directors' remuneration and for fixing the remuneration packages for all directors. Levels of remuneration should be sufficient to attract and retain the directors needed to run the company successfully, but companies should avoid paying more than is necessary for this purpose. No director should be involved in deciding his own remuneration.

Notes: 1 Under rule 18.29A, issuers are required to give a general description of the emolument policy and long-term incentive schemes of the group as well as the basis of determining the emolument payable to their directors.

2 Under rule 18.28, directors' fees and any other reimbursement or emolument payable to a director must be disclosed in full in the annual reports and accounts of the issuer on an individual and named basis.

Code Provisions

B.1.1 Issuers should establish a remuneration committee with specific written terms of reference which deal clearly with its authority and duties. A majority of the members of the remuneration committee should be independent non-executive directors.

B.1.2 The remuneration committee should consult the chairman and/or chief executive officer about their proposals relating to the remuneration of other executive directors and have access to professional advice if considered necessary.

B.1.3 The terms of reference of the remuneration committee should include, as a minimum, the following specific duties:–

(a) to make recommendations to the board on the issuer's policy and

structure for all remuneration of directors and senior management and on the establishment of a formal and transparent procedure for developing policy on such remuneration;

Note: For the purpose of this Code, "senior management" should refer to the same category of persons as referred to in the issuer's annual report and is required to be disclosed under rule 18.39.

(b) to have the delegated responsibility to determine the specific remuneration packages of all executive directors and senior management, including benefits in kind, pension rights and compensation payments, including any compensation payable for loss or termination of their office or appointment, and make recommendations to the board of the remuneration of non-executive directors. The remuneration committee should consider factors such as salaries paid by comparable companies, time commitment and responsibilities of the directors, employment conditions elsewhere in the group and desirability of performance-based remuneration;

Note: Please refer to the Note to B.1.3(a) of this Code for the definition of "senior management".

(c) to review and approve performance-based remuneration by reference to corporate goals and objectives resolved by the board from time to time;

(d) to review and approve the compensation payable to executive directors and senior management in connection with any loss or termination of their office or appointment to ensure that such compensation is determined in accordance with relevant contractual terms and that such compensation is otherwise fair and not excessive for the issuer;

Note: Please refer to the Note to B.1.3(a) of this Code for the definition of "senior management".

(e) to review and approve compensation arrangements relating to dismissal or removal of directors for misconduct to ensure that such arrangements are determined in accordance with relevant contractual terms and that any compensation payment is otherwise reasonable and appropriate; and

(f) to ensure that no director or any of his associates is involved in deciding his own remuneration.

Note: The remuneration committee shall advise shareholders on how to vote with respect to any service contracts of directors that require shareholders' approval under rule 17.90.

B.1.4 The remuneration committee should make available its terms of reference, explaining its role and the authority delegated to it by the board.

Notes: 1 This requirement could be met by making it available on request and by including the information on the issuer's website.

2 Under paragraph 2(f)(i) of Appendix 16, issuers must explain the role of the remuneration committee (if any) in the Corporate Governance Report.

B.1.5 The remuneration committee should be provided with sufficient resources to discharge its duties.

Recommended Best Practices

B.1.6 A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance.

B.1.7 Issuers should disclose details of any remuneration payable to members of senior management, on an individual and named basis, in their annual reports and accounts.

Notes: 1 Issuers should disclose details of any remuneration payable to members of senior management. Such disclosure should be to the same standard as that required for directors of issuers under rule 18.28.

2 For the purpose of this Code, "senior management" should refer to the same category of persons as referred to in the issuer's annual report and is required to be disclosed under rule 18.39.

B.1.8 Where the board resolves to approve any remuneration or compensation arrangements which the remuneration committee has previously resolved not to approve, the board must disclose the reasons for its resolution in its next annual report.

C. ACCOUNTABILITY AND AUDIT

C.1 Financial reporting

Principle

The board should present a balanced, clear and comprehensible assessment of the company's performance, position and prospects.

Code Provisions

C.1.1 Management should provide such explanation and information to the board as will enable the board to make an informed assessment of the financial and other information put before the board for approval.

Note: Issuers are reminded of their obligation to comply with the financial reporting and disclosure requirements set out in the GEM Listing Rules. Failure to comply with such requirements constitutes a breach of the GEM Listing Rules.

C.1.2 The directors should acknowledge in the Corporate Governance Report their responsibility for preparing the accounts, and there should be a statement by the auditors about their reporting responsibilities in the auditors' report on the financial statements. Unless it is inappropriate to assume that the company will continue in business, the directors should prepare the accounts on a going concern basis, with supporting assumptions or qualifications as necessary. When the directors are aware of material uncertainties relating to events or conditions that may cast significant doubt upon the issuer's ability to continue as a going concern, such uncertainties should be clearly and prominently set out and discussed at length in the Corporate Governance Report. The Corporate Governance Report should contain sufficient information so as to enable investors to understand the severity and significance of the matters at hand. To the extent that it is reasonable and appropriate, the issuer may refer to the other relevant parts of the annual report. Any such references should be clear and unambiguous and the Corporate Governance Report should not only contain a cross-reference without any discussion of the matter.

C.1.3 The board's responsibility to present a balanced, clear and understandable assessment extends to annual, half-year and quarterly reports, other price-sensitive announcements and other financial disclosures required under the GEM Listing Rules, and reports to regulators as well as to information required to be disclosed pursuant to statutory requirements.

C.2 Internal controls

Principle

The board should ensure that the issuer maintains sound and effective internal controls to safeguard the shareholders' investment and the issuer's assets.

Code Provisions

C.2.1 The directors should at least annually conduct a review of the effectiveness of the system of internal control of the issuer and its subsidiaries and report to shareholders that they have done so in their Corporate Governance Report. The review should cover all material controls, including financial, operational and compliance controls and risk management functions.

Recommended Best Practices

C.2.2 The board's annual review should, in particular, consider:

(a) the changes since the last annual review in the nature and extent of significant risks, and the issuer's ability to respond to changes in its business and the external environment;

(b) the scope and quality of management's ongoing monitoring of risks and of the system of internal control, and where applicable, the work of its internal audit function and other providers of assurance;

(c) the extent and frequency of the communication of the results of the monitoring to the board (or board committee(s)) which enables it to build up a cumulative assessment of the state of control in the issuer and the effectiveness with which risk is being managed;

(d) the incidence of significant control failings or weakness that has been identified at any time during the period and the extent to which they have resulted in unforeseen outcomes or contingencies that have had, could have had, or may in the future have, a material impact on the issuer's financial performance or condition; and

(e) the effectiveness of the issuer's processes relating to financial reporting and Listing Rule compliance.

C.2.3 Issuers should disclose as part of the Corporate Governance Report a narrative statement how they have complied with the code provisions on internal control during the reporting period. The disclosures should also include the following items:

(a) the process that an issuer has applied for identifying, evaluating and managing the significant risks faced by it;

(b) any additional information to assist understanding of the issuer's risk management processes and system of internal control;

(c) an acknowledgement by the board that it is responsible for the issuer's system of internal control and for reviewing its effectiveness;

(d) the process that an issuer has applied in reviewing the effectiveness of the system of internal control; and

(e) the process that an issuer has applied to deal with material internal control aspects of any significant problems disclosed in its annual reports and accounts.

C.2.4 Issuers should ensure that their disclosures provide meaningful information and do not give a misleading impression.

C.2.5 Issuers without an internal audit function should review the need for one on an annual basis and should disclose the outcome of such review in the issuers' Corporate Governance Report.

C.3 Audit Committee

Principle

The board should establish formal and transparent arrangements for considering how it will apply the financial reporting and internal control principles and for maintaining an appropriate relationship with the company's auditors. The audit committee established by an issuer pursuant to the GEM Listing Rules should have clear terms of reference.

Code Provisions

C.3.1 Full minutes of audit committee meetings should be kept by a duly appointed secretary of the meeting (who should normally be the company secretary). Draft and final versions of minutes of the audit committee meetings should be sent to all members of the committee for their comment and records respectively, in both cases within a reasonable time after the meeting.

C.3.2 A former partner of the issuer's existing auditing firm should be prohibited from acting as a member of the issuer's audit committee for a period of 1 year commencing on the date of his ceasing:

(a) to be a partner of the firm; or

(b) to have any financial interest in the firm,

whichever is the later.

C.3.3 The terms of reference of the audit committee should include at least the following duties:–

Relationship with the issuer's auditors

(a) to be primarily responsible for making recommendation to the board on the appointment, reappointment and removal of the external auditor, and to approve the remuneration and terms of engagement of the external auditor, and any questions of resignation or dismissal of that auditor;

Note: Issuers are reminded that rule 17.50(4) requires an announcement to be published when there is a change of auditors. The announcement must also include a statement as to whether there are any matters that need to be brought to holders of securities of the issuer.

(b) to review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process in accordance with applicable standard. The audit committee should discuss with the auditor the nature and scope of the audit and reporting obligations before the audit commences;

(c) to develop and implement policy on the engagement of an external auditor to supply non-audit services. For this purpose, external auditor shall include any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally. The audit committee should report to the board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken;

Review of financial information of the issuer

(d) to monitor integrity of financial statements of an issuer and the issuer's annual report and accounts, half-year report and quarterly reports, and to review significant financial reporting judgements contained in them. In this regard, in reviewing the issuer's annual report and accounts, half-year report and quarterly reports before submission to the board, the committee should focus particularly on:–

(i) any changes in accounting policies and practices;

(ii) major judgmental areas;

(iii) significant adjustments resulting from audit;

(iv) the going concern assumptions and any qualifications;

(v) compliance with accounting standards; and

(vi) compliance with the GEM Listing Rules and other legal requirements in relation to financial reporting;

(e) In regard to (d) above:–

(i) members of the committee must liaise with the issuer's board of directors, senior management and the person appointed as the issuer's qualified accountant and the committee must meet, at least once a year, with the issuer's auditors; and

(ii) the committee should consider any significant or unusual items that are, or may need to be, reflected in such reports and accounts and must give due consideration to any matters that have been raised by the issuer's qualified accountant, compliance officer or auditors;

Oversight of the issuer's financial reporting system and internal control procedures

(f) to review the issuer's financial controls, internal control and risk management systems;

(g) to discuss with the management the system of internal control and ensure that management has discharged its duty to have an effective internal control system;

(h) to consider any findings of major investigations of internal control matters as delegated by the board or on its own initiative and management's response;

(i) where an internal audit function exists, to ensure co-ordination between the internal and external auditors, and to ensure that the internal audit function is adequately resourced and has appropriate standing within the issuer, and to review and monitor the effectiveness of the internal audit function;

(j) to review the group's financial and accounting policies and practices;

(k) to review the external auditor's management letter, any material queries raised by the auditor to management in respect of the accounting records, financial accounts or systems of control and management's response;

(l) to ensure that the board will provide a timely response to the issues raised in the external auditor's management letter;

(m) to report to the board on the matters set out in this code provision; and

(n) to consider other topics, as defined by the board.

Notes: The following are only intended to be suggestions as to how compliance with the above code provision may be achieved and do not form part of the code provision.

1 The audit committee may wish to consider establishing the following procedure to review and monitor the independence of external auditors:-

(i) consider all relationships between the issuer and the audit firm (including the provision of non-audit services);

(ii) seek from the audit firm, on an annual basis, information about policies and processes for maintaining independence and monitoring compliance with relevant requirements, including current requirements regarding rotation of audit partners and staff; and

(iii) meet with the auditor, at least annually, in the absence of management, to discuss matters relating to its audit fees, any issues arising from the audit and any other matters the auditor may wish to raise.

2 The audit committee may wish to consider agreeing with the board the issuer's policies relating to the hiring of employees or former employees of the external auditors and monitor the application of such policies. The audit committee should then be in a position to consider whether in the light of this there has been any impairment or appearance of impairment, of the auditor's judgement or independence in respect of the audit.

3 The audit committee would normally be expected to ensure that the provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditor's independence or objectivity in relation to the provision of non-audit services, the audit committee may wish to consider:

(i) whether the skills and experience of the audit firm make it a suitable supplier of the non-audit services;

(ii) whether there are safeguards in place to ensure that there is no threat to objectivity and independence in the conduct of the audit resulting from the provision of such services by the external auditor;

(iii) the nature of the non-audit services, the related fee levels and the fee levels individually and in aggregate relative to the audit firm; and

(iv) the criteria which govern the compensation of the individuals performing the audit.

4 For further guidance on the duties of an audit committee, issuers may refer to the "Principles of Auditor Independence and the Role of Corporate Governance in Monitoring an Auditor's Independence" issued by the Technical Committee of the International Organization of Securities Commissions in October 2002 and "A Guide for Effective Audit Committees" published by the Hong Kong Society of Accountants (as it was then known) in February 2002. Issuers may also adopt the terms of reference set out in those guides, or they may adopt any other comparable terms of reference for the establishment of an audit committee.

C.3.4 The audit committee should make available its terms of reference, explaining its role and the authority delegated to it by the board.

Notes: 1 This requirement could be met by making it available on request and by including the information on the issuer's website.

2 Under paragraph 2(i)(i) of Appendix 16, issuers must explain the role of the audit committee in the Corporate Governance Report.

C.3.5 Where the board disagrees with the audit committee's view on the selection, appointment, resignation or dismissal of the external auditors, the issuer should include in the Corporate Governance Report a statement from the audit committee explaining its recommendation and also the reason(s) why the board has taken a different view.

C.3.6 The audit committee should be provided with sufficient resources to discharge its duties.

Recommended Best Practices

C.3.7 The terms of reference of the audit committee should also require the audit committee:

(a) to review arrangements by which employees of the issuer may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. The audit committee should ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action; and

(b) to act as the key representative body for overseeing the issuer's relation with the external auditor.

D. DELEGATION BY THE BOARD

D.1 Management functions

Principle

An issuer should have a formal schedule of matters specifically reserved to the board for its decision. The board should give clear directions to management as to the matters that must be approved by the board before decisions are made on behalf of the issuer.

Code Provisions

D.1.1 When the board delegates aspects of its management and administration functions to management, it must at the same time give clear directions as to the powers of management, in particular, with respect to the circumstances where management should report back and obtain prior approval from the board before making decisions or entering into any commitments on behalf of the issuer.

Note: The board should not delegate matters to a board committee, executive directors or management to an extent that would

significantly hinder or reduce the ability of the board as a whole to discharge its functions.

D.1.2 An issuer should formalise the functions reserved to the board and those delegated to management. It should review those arrangements on a periodic basis to ensure that they remain appropriate to the needs of the issuer.

Note: Under paragraph 2(c)(iv) of Appendix 16, issuers must include in their Corporate Governance Report a statement of how the board operates, including a high level statement of which types of decisions are to be taken by the board and which are to be delegated to management.

Recommended Best Practices

D.1.3 An issuer should disclose the division of responsibility between the board and management to assist those affected by corporate decisions to better understand the respective accountabilities and contributions of the board and management.

D.1.4 Directors should clearly understand delegation arrangements in place. To that end, issuers should have formal letters of appointment for directors setting out the key terms and conditions relative to their appointment.

D.2 Board Committees

Principle

Board committees should be formed with specific written terms of reference which deal clearly with the committees' authority and duties.

Code Provisions

D.2.1 Where board committees are established to deal with matters, the board should prescribe sufficiently clear terms of reference to enable such committees to discharge their functions properly.

D.2.2 The terms of reference of board committees should require such committees to report back to the board on their decisions or recommendations, unless there are legal or regulatory restrictions on their ability to do so (such as a restriction on disclosure due to regulatory requirements).

E. COMMUNICATION WITH SHAREHOLDERS

E.1 Effective communication

Principle

The board should endeavour to maintain an on-going dialogue with shareholders and in particular, use annual general meetings or other general meetings to communicate with shareholders and encourage their participation.

Code Provisions

E.1.1 In respect of each substantially separate issue at a general meeting, a separate resolution should be proposed by the chairman of that meeting.

Note: An example of a substantially separate issue is the nomination of persons as directors. Accordingly, each such person should be nominated by means of a separate resolution.

E.1.2 The chairman of the board should attend the annual general meeting and arrange for the chairmen of the audit, remuneration and nomination committees (as appropriate) or in the absence of the chairman of such committees, another member of the committee or failing this his duly appointed delegate, to be available to answer questions at the annual general meeting. The chairman of the independent board committee (if any) should also be available to answer questions at any general meeting to approve a connected transaction or any other transaction that is subject to independent shareholders' approval.

E.2 Voting by Poll

Principle

The issuer should regularly inform shareholders of the procedure for voting by poll and ensure compliance with the requirements about voting by poll contained in the GEM Listing Rules and the constitutional documents of the issuer.

Code Provisions

E.2.1 The chairman of a meeting should ensure disclosure in the issuer's circulars to shareholders of the procedures for and the rights of shareholders to demand a poll in compliance with the requirements about voting by poll contained in rule 17.47(4). In particular, pursuant to rule 17.47(3), the chairman of a meeting and/or directors who, individually or collectively,

hold proxies in respect of shares representing 5% or more of the total voting rights at a particular meeting shall demand a poll in certain circumstances where, on a show of hands, a meeting votes in the opposite manner to that instructed in those proxies. If a poll is required under such circumstances, the chairman of the meeting should disclose to the meeting the total number of votes represented by all proxies held by directors indicating an opposite vote to the votes cast at the meeting on a show of hands.

E.2.2 The issuer should count all proxy votes and, except where a poll is required, the chairman of a meeting should indicate to the meeting the level of proxies lodged on each resolution, and the balance for and against the resolution, after it has been dealt with on a show of hands. The issuer should ensure that votes cast are properly counted and recorded.

E.2.3 The chairman of a meeting should at the commencement of the meeting ensure that an explanation is provided of:–

(a) the procedures for demanding a poll by shareholders before putting a resolution to the vote on a show of hands; and

(b) the detailed procedures for conducting a poll and then answer any questions from shareholders whenever voting by way of a poll is required.

APPENDIX B
CORPORATE GOVERNANCE REPORT

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MAIN BOARD

APPENDIX 23 OF THE MAIN BOARD LISTING RULES CORPORATE GOVERNANCE REPORT

GENERAL

1. Listed issuers shall include a report on corporate governance practices (the "Corporate Governance Report") prepared by the board of directors in their summary financial reports (if any) pursuant to paragraph 50 of Appendix 16 and annual reports pursuant to paragraph 34 of Appendix 16. The Corporate Governance Report shall contain all the information set out in paragraph 2 of this Appendix. Any failure to do so will be regarded as a breach of the Exchange Listing Rules.

   To the extent that it is reasonable and appropriate, the Corporate Governance Report included in a listed issuer's summary financial report may take the form of a summary of the Corporate Governance Report contained in the annual report and may also incorporate information by reference to its annual report. Any such references must be clear and unambiguous and the summary must not only contain a cross-reference without any discussion of the matter. The summary must contain, as a minimum, a narrative statement indicating overall compliance with and highlighting any deviation from the provisions of the Code on Corporate Governance Practices contained in Appendix 14 (the "Code").

   Listed issuers are also encouraged to disclose information set out in paragraph 3 of this Appendix in their Corporate Governance Report.

MANDATORY DISCLOSURE REQUIREMENTS

2. Listed issuers shall include the following information for the accounting period covered by the annual report and any significant events pertaining to the following information for any subsequent period up to the date of publication of the annual report, to the extent that is practicable:

(a) Corporate governance practices

(i) a narrative statement of how the listed issuer has applied the principles in the Code, providing explanation which enables its shareholders to evaluate how the principles have been applied;

(ii) a statement as to whether the listed issuer meets the code provisions in the Code. If a listed issuer has adopted its own code that exceeds the code provisions set out in the Code, such listed issuer may draw attention to such fact in its annual report; and

(iii) in the event of any deviation from the code provisions set out in the Code, details of such deviation during the financial year (including considered reasons for such deviations).

(b) Directors' securities transactions

In respect of the Model Code set out in Appendix 10:

(i) whether the listed issuer has adopted a code of conduct regarding directors' securities transactions on terms no less exacting than the required standard set out in the Model Code;

(ii) having made specific enquiry of all directors, whether the directors of the listed issuer have complied with, or whether there has been any non-compliance with, the required standard set out in the Model Code and its code of conduct regarding directors' securities transactions; and

(iii) in the event of any non-compliance with the required standard set out in the Model Code, details of such non-compliance and an explanation of the remedial steps taken by the listed issuer to address such non-compliance.

(c) Board of directors

Details in relation to the board of directors of listed issuers, which include:

(i) composition of the board, by category of directors, of the listed issuer, including name of chairman, executive directors, non-executive directors and independent non-executive directors;

(ii) number of board meetings held during the financial year;

(iii) individual attendance of each director, on a named basis, at the board meetings;

(iv) a statement of how the board operates, including a high level statement of which types of decisions are to be taken by the board and which are to be delegated to management;

(v) details of non-compliance (if any) with rules 3.10(1) and (2) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to appointment of a sufficient number of independent non-executive directors and an independent non-executive director with appropriate professional qualifications, or accounting or related financial management expertise, respectively;

Note: Listed issuers are reminded of their obligation to comply with rules 3.10(1) and (2). Failure to comply with such requirements constitutes a breach of the Exchange Listing Rules.

(vi) reasons why the listed issuer considers an independent non-executive director to be independent where he/she fails to meet one or more of the guidelines for assessing independence set out in rule 3.13; and

(vii) relationship (including financial, business, family or other material/relevant relationship(s)), if any, among members of the board and in particular, between the chairman and the chief executive officer.

(d) Chairman and chief executive officer

(i) identity of the chairman and chief executive officer; and

(ii) whether the roles of the chairman and chief executive officer are segregated and are not exercised by the same individual.

(e) Non-executive directors

The term of appointment of non-executive directors.

(f) Remuneration of directors

The following information relating to the directors' remuneration policy:

(i) the role and function of the remuneration committee (if any) or the reason(s) for not having a remuneration committee;

(ii) the composition of the remuneration committee (if any) (including names and identifying in particular the chairman of the remuneration committee);

(iii) the number of meetings held by the remuneration committee or the board of directors (if there is no remuneration committee) during the year to discuss

remuneration related matters and the record of individual attendance of members, on a named basis, at meetings held during the year; and

(iv) a summary of the work, including determining the policy for the remuneration of executive directors, assessing performance of executive directors and approving the terms of executive directors' service contracts, performed by the remuneration committee or board of directors (if there is no remuneration committee) during the year.

Note: Under Appendix 16, listed issuers are required to give a general description of the emolument policy and long-term incentive schemes as well as the basis of determining the emolument payable to their directors.

(g) Nomination of directors

The following information relating to the appointment and removal of directors:

(i) the role and function of the nomination committee (if any);

(ii) the composition of the nomination committee (if any) (including names and identifying in particular the chairman of the nomination committee);

(iii) the nomination procedures and the process and criteria adopted by the nomination committee or the board of directors (if there is no nomination committee) to select and recommend candidates for directorship during the year;

(iv) a summary of the work, including determining the policy for the nomination of directors, performed by the nomination committee or the board of directors (if there is no nomination committee) during the year; and

(v) the number of meetings held by the nomination committee or the board of directors (if there is no nomination committee) during the year and the record of individual attendance of members, on a named basis, at meetings held during the year.

(h) Auditors' remuneration

An analysis of remuneration in respect of audit and non-audit services provided by the auditors (including any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally) to the listed issuer. Such analysis must include, in respect of each significant non-audit service assignment, details of the nature of the services and the fees paid.

(i) Audit committee

The following information relating to the audit committee:

(i) its role, function and composition of the committee members (including names and identifying in particular the chairman of the audit committee);

(ii) the number of audit committee meetings held during the year and record of individual attendance of members, on a named basis, at meetings held during the year;

(iii) a report on the work performed by the audit committee during the year in discharging its responsibilities in its review of the quarterly (if relevant), half-yearly and annual results and system of internal control, and its other duties set out in the Code; and

(iv) details of non-compliance with rule 3.21 (if any) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to establishment of an audit committee.

Note: Listed issuers are reminded of their obligation to comply with rule 3.21. Failure to comply with such requirements constitutes a breach of the Exchange Listing Rules.

Note: In addition to the disclosure obligations described above, the code provisions in the Code expect issuers to make certain specified disclosures in the Corporate Governance Report. Where issuers choose not to make the expected disclosure, they must give considered reasons for the deviation in accordance with paragraph 2(a)(iii). For ease of reference, the specific disclosure expectations of the code provisions are set out below:

1 an acknowledgement from the directors of their responsibility for preparing the accounts and a statement by the auditors about their reporting responsibilities (C.1.2 of the Code);

2 report on material uncertainties, if any, relating to events or conditions that may cast significant doubt upon the listed issuer's ability to continue as a going concern (C.1.2 of the Code);

3 a statement that the board has conducted a review of the effectiveness of the system of internal control of the issuer and its subsidiaries (C.2.1 of the Code); and

4 a statement from the audit committee explaining its recommendation and the reason(s) why the board has taken a different view from that of the audit committee regarding the selection, appointment, resignation or dismissal of the external auditors (C.3.5 of the Code).

RECOMMENDED DISCLOSURES

3. The disclosures set out in this paragraph relating to corporate governance matters are provided for listed issuers' reference. They are not intended to be exhaustive or mandatory. They are rather intended to set out the areas which listed issuers may comment on in their Corporate Governance Report. The level of details needed varies with the nature and complexity of listed issuers' business activities. Listed issuers are encouraged to include the following information in their Corporate Governance Report:

(a) Share interests of senior management

(i) the number of shares held by senior management (i.e. those individuals whose biographical details are disclosed in the annual report).

(b) Shareholders' rights

(i) the way in which shareholders can convene an extraordinary general meeting;

(ii) the procedures by which enquiries may be put to the board together with sufficient contact details to enable such enquiries to be properly directed; and

(iii) the procedures for putting forward proposals at shareholders' meetings with sufficient contact details.

(c) Investor relations

(i) any significant changes in the listed issuer's articles of association during the year;

(ii) details of shareholders by type and aggregate shareholding;

Note: Listed issuers are reminded of their obligation to comply with the requirements in Appendix 16 and Practice Note 5 relating to the disclosure of interests in the listed issuer. They may wish to mention such information in this section of the Corporate Governance Report.

(iii) details of the last shareholders' meeting, including the time and venue, major items discussed and particulars as to voting;

(iv) indication of important shareholders' dates in the coming financial year; and

(v) public float capitalisation as at the end of the year.

(d)Internal controls

(i) where a listed issuer includes a statement by the directors that they have conducted a review of its system of internal control in the annual report pursuant to paragraph C.2.1 of the Code, the listed issuer is encouraged to disclose the following details in such report:

(aa) an explanation of how the system of internal control has been defined for the listed issuer;

(bb) procedures and internal controls for the handling and dissemination of price sensitive information;

(cc) whether the listed issuer has an internal audit function or the outcome of the review of the need for an internal audit function where the listed issuer has no such function;

(dd) how often internal controls are reviewed;

(ee) a statement that the directors have reviewed the effectiveness of the system of internal control and whether they consider the internal control systems effective and adequate;

(ff) criteria for the directors to assess the effectiveness of the system of internal control;

(gg) the period which the review covers;

(hh) details of any significant areas of concern which may affect shareholders;

(ii) significant views or proposals put forward by the audit committee; and

(jj) where a listed issuer has not conducted a review of its internal control during the year, an explanation why it has not done so;

(ii) a narrative statement (including the items under C.2.3 of the Code) of how the listed issuer has complied with the code provisions on internal control during the reporting period (C.2.3 of the Code); and

(iii) the outcome of the review conducted on an annual basis by an issuer without an internal audit function of the need for one (C.2.5 of the Code).

(e) Management functions

(i) the division of responsibility between the board and management.

Note: Issuers may consider that some of the information recommended under paragraph 3 is too lengthy and detailed to be included in the Corporate Governance Report. As an alternative to full disclosure in the Corporate Governance Report, issuers may choose to include some or all of this information:

(a) on its website and highlight to investors where they can:

(i) access the soft copy of this information on its website by giving a hyperlink directly to the relevant webpage; and/or

(ii) collect a hard copy of the relevant information free of charge; or

(b) where the information is publicly available, by stating where the information can be found. Any hyperlink should be directly to the relevant webpage.

APPENDIX 16 OF THE GEM LISTING RULES
CORPORATE GOVERNANCE REPORT

GENERAL

1. Listed issuers shall include a report on corporate governance practices (the "Corporate Governance Report") prepared by the board of directors in their summary financial reports (if any) pursuant to rule 18.81 and annual reports pursuant to rule 18.44. The Corporate Governance Report shall contain all the information set out in paragraph 2 of this Appendix. Any failure to do so will be regarded as a breach of the GEM Listing Rules.

   To the extent that it is reasonable and appropriate, the Corporate Governance Report included in a listed issuer's summary financial report may take the form of a summary of the Corporate Governance Report contained in the annual report and may also incorporate information by reference to its annual report. Any such references must be clear and unambiguous and the summary must not only contain a cross-reference without any discussion of the matter. The summary must contain, as a minimum, a narrative statement indicating overall compliance with and highlighting any deviation from the provisions of the Code on Corporate Governance Practices contained in Appendix 15 (the "Code").

   Listed issuers are also encouraged to disclose information set out in paragraph 3 of this Appendix in their Corporate Governance Report.

MANDATORY DISCLOSURE REQUIREMENTS

2. Listed issuers shall include the following information for the accounting period covered by the annual report and any significant events pertaining to the following information for any subsequent period up to the date of publication of the annual report, to the extent that is practicable:

   (a) Corporate governance practices

   (i) a narrative statement of how the listed issuer has applied the principles in the Code, providing explanation which enables its shareholders to evaluate how the principles have been applied;

(ii) a statement as to whether the listed issuer meets the code provisions in the Code. If a listed issuer has adopted its own code that exceeds the code provisions set out in the Code, such listed issuer may draw attention to such fact in its annual report; and

(iii) in the event of any deviation from the code provisions set out in the Code, details of such deviation during the financial year (including considered reasons for such deviations).

(b) Directors' securities transactions

In respect of the required standard of dealings set out in rules 5.48 to 5.67:

(i) whether the listed issuer has adopted a code of conduct regarding directors' securities transactions on terms no less exacting than the required standard of dealings;

(ii) having made specific enquiry of all directors, whether the directors of the listed issuer have complied with, or whether there has been any non-compliance with, the required standard of dealings and its code of conduct regarding directors' securities transactions; and

(iii) in the event of any non-compliance with the required standard of dealings, details of such non-compliance and an explanation of the remedial steps taken by the listed issuer to address such non-compliance.

(c) Board of directors

Details in relation to the board of directors of listed issuers, which include:

(i) composition of the board, by category of directors, of the listed issuer, including name of chairman, executive directors, non-executive directors and independent non-executive directors;

(ii) number of board meetings held during the financial year;

(iii) individual attendance of each director, on a named basis, at the board meetings;

(iv) a statement of how the board operates, including a high level statement of which types of decisions are to be taken by the board and which are to be delegated to management;

(v) details of non-compliance (if any) with rules 5.05(1) and (2) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to appointment of a sufficient number of independent non-executive directors and an independent non-executive director with appropriate professional qualifications, or accounting or related financial management expertise, respectively;

Note: Listed issuers are reminded of their obligation to comply with rules 5.05(1) and (2). Failure to comply with such requirements constitutes a breach of the GEM Listing Rules.

(vi) reasons why the listed issuer considers an independent non-executive director to be independent where he/she fails to meet one or more of the guidelines for assessing independence set out in rule 5.09; and

(vii) relationship (including financial, business, family or other material/relevant relationship(s)), if any, among members of the board and in particular, between the chairman and the chief executive officer.

(d) Chairman and chief executive officer

(i) identity of the chairman and chief executive officer; and

(ii) whether the roles of the chairman and chief executive officer are segregated and are not exercised by the same individual.

(e) Non-executive directors

The term of appointment of non-executive directors.

(f) Remuneration of directors

The following information relating to the directors' remuneration policy:

(i) the role and function of the remuneration committee (if any) or the reason(s) for not having a remuneration committee;

(ii) the composition of the remuneration committee (if any) (including names and identifying in particular the chairman of the remuneration committee);

(iii) the number of meetings held by the remuneration committee or the board of directors (if there is no remuneration committee) during the year to discuss remuneration related matters and the record of individual attendance of members, on a named basis, at meetings held during the year; and

(iv) a summary of the work, including determining the policy for the remuneration of executive directors, assessing performance of executive directors and approving the terms of executive directors' service contracts,

performed by the remuneration committee or board of directors (if there is no remuneration committee) during the year.

Note: Under Chapter 18, listed issuers are required to give a general description of the emolument policy and long-term incentive schemes as well as the basis of determining the emolument payable to their directors.

(g) Nomination of directors

The following information relating to the appointment and removal of directors:

(i) the role and function of the nomination committee (if any);

(ii) the composition of the nomination committee (if any) (including names and identifying in particular the chairman of the nomination committee);

(iii) the nomination procedures and the process and criteria adopted by the nomination committee or the board of directors (if there is no nomination committee) to select and recommend candidates for directorship during the year;

(iv) a summary of the work, including determining the policy for the nomination of directors, performed by the nomination committee or the board of directors (if there is no nomination committee) during the year; and

(v) the number of meetings held by the nomination committee or the board of directors (if there is no nomination committee) during the year and the record of individual attendance of members, on a named basis, at meetings held during the year.

(h) Auditors' remuneration

An analysis of remuneration in respect of audit and non-audit services provided by the auditors (including any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally) to the listed issuer. Such analysis must include, in respect of each significant non-audit service assignment, details of the nature of the services and the fees paid.

(i) Audit committee

The following information relating to the audit committee:

(i) its role, function and composition of the committee members (including names and identifying in particular the chairman of the audit committee);

(ii) the number of audit committee meetings held during the year and record of individual attendance of members, on a named basis, at meetings held during the year;

(iii) a report on the work performed by the audit committee during the year in discharging its responsibilities in its review of the quarterly, half-yearly and annual results and system of internal control, and its other duties set out in the Code; and

(iv) details of non-compliance with rule 5.28 (if any) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to establishment of an audit committee.

Note: Listed issuers are reminded of their obligation to comply with rule 5.28. Failure to comply with such requirements constitutes a breach of the GEM Listing Rules.

Note: In addition to the disclosure obligations described above, the code provisions in the Code expect issuers to make certain specified disclosures in the Corporate Governance Report. Where issuers choose not to make the expected disclosure, they must give considered reasons for the deviation in accordance with paragraph 2(a)(iii). For ease of reference, the specific disclosure expectations of the code provisions are set out below:

1 an acknowledgement from the directors of their responsibility for preparing the accounts and a statement by the auditors about their reporting responsibilities (C.1.2 of the Code);

2 report on material uncertainties, if any, relating to events or conditions that may cast significant doubt upon the listed issuer's ability to continue as a going concern (C.1.2 of the Code);

3 a statement that the board has conducted a review of the effectiveness of the system of internal control of the issuer and its subsidiaries (C.2.1 of the Code); and

4 a statement from the audit committee explaining its recommendation and the reason(s) why the board has taken a different view from that of the audit committee regarding the selection, appointment, resignation or dismissal of the external auditors (C.3.5 of the Code).

RECOMMENDED DISCLOSURES

3. The disclosures set out in this paragraph relating to corporate governance matters are provided for listed issuers' reference. They are not intended to be exhaustive or mandatory. They are rather intended to set out the areas which listed issuers may comment on in their Corporate Governance Report. The level of details needed varies with the nature and complexity of listed issuers' business activities. Listed issuers are encouraged to include the following information in their Corporate Governance Report:

(a) Share interests of senior management

(i) the number of shares held by senior management (i.e. those individuals whose biographical details are disclosed in the annual report).

(b) Shareholders' rights

(i) the way in which shareholders can convene an extraordinary general meeting;

(ii) the procedures by which enquiries may be put to the board together with sufficient contact details to enable such enquiries to be properly directed; and

(iii) the procedures for putting forward proposals at shareholders' meetings with sufficient contact details.

(c) Investor relations

(i) any significant changes in the listed issuer's articles of association during the year;

(ii) details of shareholders by type and aggregate shareholding;

Note: Listed issuers are reminded of their obligation to comply with the requirements in Chapter 18 relating to the disclosure of interests in the listed issuer. They may wish to mention such information in this section of the Corporate Governance Report.

(iii) details of the last shareholders' meeting, including the time and venue, major items discussed and particulars as to voting;

(iv) indication of important shareholders' dates in the coming financial year; and

(v) public float capitalisation as at the end of the year.

(d)Internal controls

(i) where a listed issuer includes a statement by the directors that they have conducted a review of its system of internal control in the annual report pursuant to paragraph C.2.1 of the Code, the listed issuer is encouraged to disclose the following details in such report:

(aa) an explanation of how the system of internal control has been defined for the listed issuer;

(bb) procedures and internal controls for the handling and dissemination of price sensitive information;

(cc) whether the listed issuer has an internal audit function or the outcome of the review of the need for an internal audit function where the listed issuer has no such function;

(dd) how often internal controls are reviewed;

(ee) a statement that the directors have reviewed the effectiveness of the system of internal control and whether they consider the internal control systems effective and adequate;

(ff) criteria for the directors to assess the effectiveness of the system of internal control;

(gg) the period which the review covers;

(hh) details of any significant areas of concern which may affect shareholders;

(ii) significant views or proposals put forward by the audit committee; and

(jj) where a listed issuer has not conducted a review of its internal control during the year, an explanation why it has not done so;

(ii) a narrative statement (including the items under C.2.3 of the Code) of how the listed issuer has complied with the code provisions on internal control during the reporting period (C.2.3 of the Code); and

(iii) the outcome of the review conducted on an annual basis by an issuer without an internal audit function of the need for one (C.2.5 of the Code).

(e) Management functions

(i) the division of responsibility between the board and management.

Note: Issuers may consider that some of the information recommended under paragraph 3 is too lengthy and detailed to be included in the Corporate Governance Report. As an alternative to full disclosure in the Corporate Governance Report, issuers may choose to include some or all of this information:

(a) on its website and highlight to investors where they can:

(i) access the soft copy of this information on its website by giving a hyperlink directly to the relevant webpage; and/or

(ii) collect a hard copy of the relevant information free of charge; or

(b) where the information is publicly available, by stating where the information can be found. Any hyperlink should be directly to the relevant webpage.

APPENDIX C

CONSEQUENTIAL AMENDMENTS TO THE LISTING RULES

MAIN BOARD

AMENDMENTS TO MAIN BOARD RULES (OTHER THAN REPLACEMENT OF CODE OF BEST PRACTICE IN APPENDIX 14 BY CODE ON CORPORATE GOVERNANCE PRACTICES AND INSERTION OF RULES ON CORPORATE GOVERNANCE REPORT IN APPENDIX 23)

3.18 ~~As a minimum, listed issuers should aim to comply with the guidelines for boards of directors issued by the Exchange from time to time. Listed issuers may adopt their own, more comprehensive, guidelines as an alternative.~~ [Repealed 1 January 2005]

.....

Code on Corporate Governance Practices

3.25 (1) The Code on Corporate Governance Practices contained in Appendix 14 sets out the principles of good corporate governance and two levels of recommendations: (a) code provisions; and (b) recommended best practices. Issuers are expected to comply with, but may choose to deviate from, the code provisions. The recommended best practices are for guidance only.

Note: Issuers may also devise their own code on corporate governance practices on such terms as they may consider appropriate.

(2) Issuers must state whether they have complied with the code provisions set out in the Code on Corporate Governance Practices for the relevant accounting period in their interim reports (and summary interim reports, if any) and annual reports (and summary financial reports, if any).

Note: For the relevant requirements governing preliminary results announcements, see paragraphs 45 and 46 of Appendix 16.

(3) Where the issuer deviates from the code provisions set out in the Code on

Corporate Governance Practices, the issuer must give considered reasons:

(a) in the case of annual reports (and summary financial reports), in the Corporate Governance Report which must be issued in accordance with Appendix 23; and

(b) in the case of interim reports (and summary interim reports), either:

(i) by giving considered reasons for each deviation; or

(ii) to the extent that it is reasonable and appropriate, by referring to the Corporate Governance Report in the immediately preceding annual report, and providing details of any changes together with considered reasons for any deviation not reported in that annual report. Such references must be clear and unambiguous and the interim report (or summary interim report) must not only contain a cross-reference without any discussion of the matter.

(4) In the case of the recommended best practices, issuers are encouraged, but are not required, to state whether they have complied with them and give considered reasons for any deviation.

Appendix 10

15. In relation to securities transactions by directors, a listed issuer shall disclose in its interim reports (and summary interim reports, if any) and the Corporate Governance Report contained in its annual ~~and interim~~ reports (and summary financial reports, if any):

(a) whether the listed issuer has adopted a code of conduct regarding securities transactions by directors on terms no less exacting than the required standard set out in this code;

(b) having made specific enquiry of all directors, whether its directors have complied with, or whether there has been any non-compliance with, the required standard set out in this code and its code of conduct regarding securities transactions by directors; and

(c) in the event of any non-compliance with the required standard set out in this code, details of such non-compliance and an explanation of the remedial steps taken by the listed issuer to address such non-compliance.

Appendix 16

34. A listed issuer shall include ~~the following information~~ in respect of the group:~~-~~

~~(1) a statement as to whether or not it has complied with Appendix 14 throughout the accounting period covered by the annual report. A listed issuer that has not complied with Appendix 14, or complied with only part of Appendix 14 or (in the case of requirements of a continuing nature) complied for only part of such period, must specify the paragraphs of Appendix 14 with which it has not complied and (where relevant) for what part of the period such non-compliance continued, and give reasons for any non-compliance. Insofar as a listed issuer's statement of compliance relates to paragraph 6 of Appendix 14, such statement must be reviewed by the auditors~~ a separate Corporate Governance Report prepared by the board of directors on its corporate governance practices. The report must, as a minimum, contain the information required under Appendix 23 regarding the accounting period covered by the annual report. To the extent that it is reasonable and appropriate, the issuer may incorporate by reference information in its annual report into the Corporate Governance Report. Any such references must be clear and unambiguous and the Corporate Governance Report must not only contain a cross-reference without any discussion of the matter;~~-~~ .

~~(2) in respect of the Model Code set out in Appendix 10 to the Exchange Listing Rules, a statement in relation to the accounting period covered by the annual report on:~~

~~(a) whether the listed issuer has adopted a code of conduct regarding securities transactions by directors on terms no less exacting than the required standard set out in the Model Code;~~

~~(b) having made specific enquiry of all directors, whether its directors have complied with, or whether there has been any non-compliance with, the required standard set out in the Model Code and its code of conduct regarding securities transactions by directors; and~~

~~(c) in the event of any non-compliance with the required standard set out in the Model Code, details of such non-compliance and an explanation of the remedial steps taken by the listed issuer to address such non-compliance;~~

~~(3) details of non-compliance (if any) with rules 3.10(1) and 3.10(2) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to appointment of a sufficient number of independent non-executive directors and an independent non-executive director with appropriate professional qualifications, or accounting or related financial management expertise, respectively; and~~

(4) ~~details of non-compliance with rule 3.21 (if any) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to establishment of an audit committee.~~

.....

44. A listed issuer shall include in its interim report the following information in respect of the group:

(1) ~~a statement that none of the directors is aware of information that would reasonably indicate that the listed issuer is not, or was not for any part of the accounting period covered by the interim report, in compliance with Appendix 14. If any of the directors is aware of such information, the listed issuer must verify whether the information is correct and whether there has been any non-compliance with Appendix 14. If the listed issuer finds that there has been non-compliance with Appendix 14, then the listed issuer shall briefly explain in its interim report that it has not complied with all or part of Appendix 14, as the case may be, and include a statement giving the reasons for its non-compliance~~ a statement in relation to the accounting period covered by the interim report on whether the listed issuer meets the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14. Where there are any deviations from the code provisions in the Code, the listed issuer must give considered reasons for the deviations from the code provisions, either by:

(a) giving considered reasons for each deviation; or

(b) to the extent that it is reasonable and appropriate, by referring to the Corporate Governance Report in the immediately preceding annual report and providing details of any changes together with considered reasons for any deviation not reported in that annual report. Any such references must be clear and unambiguous and the interim report must not only contain a cross-reference without any discussion of the matter;

.....

45. A listed issuer shall publish a preliminary announcement of its results in the newspapers as required under rule 13.49(1), which has been agreed with its auditors and which includes, as a minimum, the following:

.....

(5) ~~particulars of compliance with Appendix 14 as set out in paragraph 34~~ a statement as to whether the listed issuer meets the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14. The listed issuer must also disclose any deviations from the code provisions and give considered reasons for such deviations. To the extent that it is reasonable

and appropriate, such information may be given by reference to the immediately preceding interim report or to the Corporate Governance Report in the immediately preceding annual report, and summarising any changes since that report. Any such references must be clear and unambiguous;

.....

46. A listed issuer shall publish a preliminary announcement of its results in the newspapers for the first six months of each financial year required under rule 13.49(6), which shall include, as a minimum, the following information:-

.....

(4) ~~particulars of compliance with Appendix 14 as set out in paragraph 44~~a statement as to whether the listed issuer meets the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14. The listed issuer must also disclose any deviations from the code provisions and give considered reasons for such deviations. To the extent that it is reasonable and appropriate, such information may be given by reference to the Corporate Governance Report in the immediately preceding annual report, and summarising any changes since that annual report. Any such references must be clear and unambiguous;

.....

50. Summary financial reports of listed issuers shall comply with the disclosure requirements set out in the Companies (Summary Financial Reports of Listed Companies) Regulation. A listed issuer shall also disclose the following information in its summary financial report:-

(1) particulars of any purchase, sale or redemption by the listed issuer, or any of its subsidiaries, of its listed securities during the financial year or an appropriate negative statement; and

(2) ~~particulars of compliance with Appendix 14 as set out in paragraph 34~~a separate Corporate Governance Report prepared by the board of directors on its corporate governance practices. The report must, as a minimum, contain the information required under Appendix 23 regarding the accounting period covered by the annual report. To the extent that it is reasonable and appropriate, this Corporate Governance Report may take the form of a summary of the Corporate Governance Report contained in the annual report and may also incorporate information by reference to its annual report. Any such references must be clear and unambiguous and the summary must not only contain a cross-reference without any discussion of the matter. The summary must contain, as a minimum, a narrative statement indicating overall

compliance with and highlighting any deviation from the provisions of the Code on Corporate Governance Practices contained in Appendix 14;~~:~~.

~~(3) details of non-compliance (if any) with rules 3.10(1) and 3.10(2) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to appointment of a sufficient number of independent non-executive directors and an independent non-executive director with appropriate professional qualifications, or accounting or related financial management expertise, respectively; and~~

~~(4) details of non-compliance with rule 3.21 (if any) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to establishment of an audit committee.~~

.....

52. Listed issuers are encouraged to disclose the following additional commentary on management discussion and analysis in their interim and annual reports:

(i) efficiency indicators (e.g. return on equity, working capital ratios) for the last five financial years indicating the bases of computation;

(ii) industry specific ratios, if any, for the last five financial years indicating the bases of computation;

(iii) a discussion of the listed issuer's purpose, corporate strategy and principal drivers of performance;

(iv) an overview of trends in the listed issuer's industry and business;

(v) a discussion on business risks (including known events, uncertainties and other factors which may substantially affect future performance) and risks management policy;

(vi) a discussion on the listed issuer's environmental policies and performance, including compliance with the relevant laws and regulations;

(vii) a discussion on the listed issuer's policies and performance on community, social, ethical and reputational issues;

(viii) an account of the listed issuer's key relationships with employees, customers, suppliers and others, on which its success depends; and

(ix) receipts from, and returns to, shareholders.

Note: Issuers should also note the recommended disclosures set out in paragraph 3 of Appendix 23.

AMENDMENTS TO GEM RULES (OTHER THAN INSERTION OF CODE ON CORPORATE GOVERNANCE PRACTICES IN APPENDIX 15 AND RULES ON CORPORATE GOVERNANCE REPORT IN APPENDIX 16)

~~NON-EXECUTIVE DIRECTORS~~

5.13 ~~Every non-executive director, whether independent or not, must be appointed for a specific term and that term should be disclosed in the annual report and accounts of the issuer. A person accepting an appointment as a non-executive director must ensure that he can give sufficient time and attention to the affairs of the issuer and should not accept the appointment if he cannot.~~[Repealed 1 January 2005]

.....

5.30 ~~The duties of the audit committee must comprise at least the following matters:-~~

~~(1)~~ ~~reviewing, in draft form, the issuer's annual report and accounts, half-year report and quarterly reports and providing advice and comments thereon to the issuer's board of directors. In this regard:-~~

~~(a)~~ ~~members of the committee must liaise with the issuer's board of directors, senior management and the person appointed as the issuer's qualified accountant and the committee must meet, at least once a year, with the issuer's auditors; and~~

~~(b)~~ ~~the committee should consider any significant or unusual items that are, or may need to be, reflected in such reports and accounts and must give due consideration to any matters that have been raised by the issuer's qualified accountant, compliance officer or auditors; and~~

~~(2)~~ ~~reviewing and supervising the issuer's financial reporting and internal control procedures.~~[Repealed 1 January 2005]

5.31 ~~The issuer must ensure that full minutes are kept of all meetings of the audit committee.~~[Repealed 1 January 2005]

5.32 ~~The executive directors of the issuer must ensure that members of the audit committee are provided full and unlimited access to all books and accounts of the issuer and any employees, consultants and advisers they may, from time to time, wish to consult.~~[Repealed 1 January 2005]

.....

5.34 ~~Rules 5.35 to 5.45 set out the minimum standards of good practice concerning the general management responsibilities of the board of directors (and related matters) with which issuers and their directors must comply. All issuers are encouraged to devise their own minimum standards on no less exacting terms, in the interests not only of their independent non-executive directors, but of the board of directors as a whole.~~(1) The Code on Corporate Governance Practices contained in Appendix 15 sets out the principles of good corporate governance and two levels of recommendations: (a) code provisions; and (b) recommended best practices. Issuers are expected to comply with, but may choose to deviate from, the code provisions. The recommended best practices are for guidance only.

Note: Issuers may also devise their own code on corporate governance practices on such terms as they may consider appropriate.

(2) Issuers must state whether they have complied with the code provisions set out in the Code on Corporate Governance Practices for the relevant accounting period in their half-year reports (and summary half-year reports, if any) and annual reports (and summary financial reports, if any).

Note: For the requirements governing preliminary results announcements in this regard, see rules 18.50(6) and 18.78(4).

(3) Where the issuer deviates from the code provisions set out in the Code on Corporate Governance Practices, the issuer must give considered reasons:

(a) in the case of annual reports (and summary financial reports), in the Corporate Governance Report which must be issued in accordance with Appendix 16; and

(b) in the case of half-year reports (and summary half-year reports), either:

(i) by giving considered reasons for each deviation; or

(ii) to the extent that it is reasonable and appropriate, by referring to the Corporate Governance Report in the immediately preceding annual report, and providing details of any changes together with considered reasons for any deviation not reported in that annual report. Such references must be clear and unambiguous and the half-year report (or summary half-year report) must not only contain a cross-reference without any discussion of the matter.

(4) In the case of the recommended best practices, issuers are encouraged, but are not required, to state whether they have complied with them and give considered reasons for any deviation.

5.35 ~~Full board meetings should be held no less frequently than every 3 months. "Full" board meetings means meetings at which directors are physically present and not "paper" meetings or meetings by circulation.~~[Repealed 1 January 2005]

5.36 ~~The directors' fees and any other reimbursement or emolument payable to an independent non-executive director must be disclosed in full in the annual report and accounts of the issuer (see rules 18.27 and 18.28).~~[Repealed 1 January 2005]

5.37 ~~Except in emergencies an agenda and accompanying board papers should be sent in full to all directors at least 2 clear days before the intended date of a board meeting (or such other period as the board agrees).~~[Repealed 1 January 2005]

5.38 ~~Except in emergencies adequate notice should be given of a board meeting to give all directors an opportunity to attend.~~[Repealed 1 January 2005]

5.39 ~~All directors, executive and non-executive, are entitled to have access to board papers and materials. Where queries are raised by non-executive directors, steps should be taken to respond as promptly and fully as possible.~~[Repealed 1 January 2005]

5.40 ~~Full minutes should be kept by a duly appointed secretary of the meeting and such minutes should be open for inspection at any time in office hours on reasonable notice by any director.~~[Repealed 1 January 2005]

5.41 ~~If, in respect of any matter discussed at a board meeting, the independent non-executive directors hold views contrary to those of the executive directors, the minutes should clearly reflect this.~~[Repealed 1 January 2005]

5.42 ~~Arrangements should be made in appropriate circumstances to enable the independent non-executive directors of the board, at their request, to seek separate professional advice at the expense of the issuer.~~[Repealed 1 January 2005]

5.43 ~~If a matter to be considered by the board involves a conflict of interest for a director, a full board meeting should be held and the matter should not be dealt with by circulation or by committee and any director to whom the conflict relates may not form part of the quorum, nor participate in any discussion nor vote at such meeting in respect of such matter.~~[Repealed 1 January 2005]

5.44 ~~Every director on the board is required to keep abreast of his responsibilities as a director of an issuer. Newly appointed board members should receive an appropriate briefing on the issuer's affairs and be provided with relevant corporate governance materials on an ongoing basis.~~[Repealed 1 January 2005]

5.45 ~~The board of directors should give due consideration to all recommendations made to it, from time to time, by the issuer's company secretary, qualified accountant, compliance officer and audit committee.~~[Repealed 1 January 2005]

.....

5.68 In relation to securities transactions by directors, an issuer shall disclose in its half-year reports (and summary half-year reports, if any) and the Corporate Governance report contained in its annual ~~and half-year~~ reports (and summary financial reports, if any):

(1) whether the issuer has adopted a code of conduct regarding securities transactions by directors on terms no less exacting than the required standard of dealings;

(2) having made specific enquiry of all directors, whether its directors have complied with, or whether there has been any non-compliance with, the required standard of dealings and its code of conduct regarding securities transactions by directors; and

(3) in the event of any non-compliance with the required standard of dealings, details of such non-compliance and an explanation of the remedial steps taken by the issuer to address such non-compliance.

.....

18.44 The following information in respect of an issuer:-

~~(1) the composition, by name, of the audit committee (which information should be included in the corporate information section of the annual report);~~

~~(2) the work undertaken by the audit committee during the financial year (which information should be included in the report of the directors or the review of operations);~~

~~(3) the number of times that the audit committee met during the financial year;~~

(~~4~~1) the full name and professional qualifications (if any) of:-

(a) the company secretary of the issuer;

(b) the qualified accountant of the issuer appointed pursuant to rule 5.15; and

(c) the compliance officer of the issuer appointed pursuant to rule 5.19; and

(52) ~~a statement as to whether or not the issuer has complied with rules 5.34 to 5.45 concerning board practices and procedures throughout the accounting period covered by the annual report. An issuer that has not complied with rules 5.34 to 5.45, or complied with only part of rules 5.34 to 5.45 or (in the case of requirements of a continuing nature) complied for only part of such period, must specify the rules with which it has not complied and (where relevant) for what part of the period of such non-compliance continued, and give reasons for any non-compliance. Insofar as the issuer's statement of compliance relates to rule 5.36, such statement must be reviewed by the auditors~~a separate Corporate Governance Report prepared by the board of directors on its corporate governance practices. The report must, as a minimum, contain the information required under Appendix 16, regarding the accounting period covered by the annual report. To the extent that it is reasonable and appropriate, the issuer may incorporate by reference information in its annual report into the Corporate Governance Report. Any such references must be clear and unambiguous and the Corporate Governance Report must not only contain a cross-reference without any discussion of the matter~~;~~.

(6) ~~in respect of the required standard of dealings set out in rules 5.48 to 5.67, a statement in relation to the accounting period covered by the annual report as to:~~

(a) ~~whether the issuer has adopted a code of conduct regarding directors' securities transactions on terms no less exacting than the required standard of dealings;~~

(b) ~~having made specific enquiry of all directors, whether its directors have complied with, or whether there has been any non-compliance with, the required standard of dealings and its code of conduct regarding directors' securities transactions; and~~

(c) ~~in the event of any non-compliance with the required standard of dealings, details of such non-compliance and an explanation of the remedial steps taken by the issuer to address such non-compliance;~~

(7) ~~details of non-compliance (if any) with rules 5.05(1) and 5.05(2) and an explanation of the remedial steps taken by the issuer to address such non-compliance relating to appointment of a sufficient number of independent non-executive directors and an independent non-executive director with appropriate professional qualifications or accounting or related financial management expertise, respectively; and~~

(8) ~~details of non-compliance with rule 5.28 (if any) and an explanation of the~~

~~remedial steps taken by the issuer to address such non-compliance relating to establishment of an audit committee.~~

.....

18.50 The preliminary announcement of results for the financial year must contain at least the following information in respect of the group:

.....

(6) ~~a statement as to whether or not the listed issuer has complied with rules 5.34 to 5.45 concerning board practices and procedures throughout the financial year. A listed issuer that has not complied with rules 5.34 to 5.45, or complied with only part of rules 5.34 to 5.45 or (in the case of requirements of a continuing nature) complied for only part of such period, must specify the rules with which it has not complied and (where relevant) for what part of the period of such non-compliance continued, and give reasons for any non-compliance. Insofar as a listed issuer's statement of compliance relates to rule 5.36, such statement must be reviewed by the auditors~~a statement as to whether the listed issuer meets the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 15. The listed issuer must also disclose any deviations from the code provisions and considered reasons for such deviations. To the extent that it is reasonable and appropriate, such information may be given by reference to the immediately preceding half-year report or to the Corporate Governance Report in the immediately preceding annual report, and summarising any changes since that report. Any such references must be clear and unambiguous; and

.....

18.55 Each half-year report shall contain at least the following information in respect of the group:-

.....

(4) ~~a statement as to whether or not the listed issuer has complied with rules 5.34 to 5.45 concerning board practices and procedures throughout the accounting period covered by the half-year report. A listed issuer that has not complied with rules 5.34 to 5.45, or complied with only part of rules 5.34 to 5.45 or (in the case of requirements of a continuing nature) complied for only part of such period, must specify the rules with which it has not complied and (where relevant) for what part of the period of such non-compliance continued, and give reasons for any non-compliance. Insofar as the listed issuer's statement of compliance relates to rule 5.36,~~

~~such statement must be reviewed by the auditors~~a statement in relation to the accounting period covered by the half-year report on whether the listed issuer meets the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 15. Where there are any deviations from the code provisions in the Code, the listed issuer must also give considered reasons for the deviations from the code provisions, either by:

(a) giving considered reasons for each deviation; or

(b) to the extent that it is reasonable and appropriate, by referring to the Corporate Governance Report in the immediately preceding annual report and providing details of any changes together with considered reasons for any deviation not reported in that annual report. Any such references must be clear and unambiguous and the half-year report must not only contain a cross-reference without any discussion of the matter;

.....

18.78 A listed issuer must publish (in accordance with the requirements of Chapter 16) a preliminary announcement of the results for the first 6 months of each financial year, containing at least the information set out below, on the GEM website on the next business day after approval by or on behalf of the board of the results and in any event not later than 45 days after the end of such period:

.....

(4) ~~a statement as to compliance with rules 5.34 to 5.45 concerning board practices and procedures during the relevant period as required by rule 18.55(4)~~a statement as to whether the listed issuer meets the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 15. The listed issuer must also disclose any deviations from the code provisions and considered reasons for such deviations. To the extent that it is reasonable and appropriate, such information may be given by reference to the Corporate Governance Report in the immediately preceding annual report, and summarising any changes since that annual report. Any such references must be clear and unambiguous;

.....

18.81 Summary financial reports of listed issuers shall comply with the disclosure requirements set out in the Companies (Summary Financial Reports of Listed Companies) Regulation. A listed issuer shall also disclose the following information in its summary financial report:

(1) particulars of any purchase, sale or redemption by the listed issuer, or any of its subsidiaries, of its listed securities during the financial year or an appropriate negative statement; and

(2) ~~a statement as to compliance with rules 5.34 to 5.45 concerning board practices and procedures during the financial year~~a separate Corporate Governance Report prepared by the board of directors on its corporate governance practices. The report must, as a minimum, contain the information required under Appendix 16 regarding the accounting period covered by the annual report. To the extent that it is reasonable and appropriate, this Corporate Governance Report may take the form of a summary of the Corporate Governance Report contained in the annual report and may also incorporate information by reference to its annual report. Any such references must be clear and unambiguous and the summary must not only contain a cross-reference without any discussion of the matter. The summary must contain, as a minimum, a narrative statement indicating overall compliance with and highlighting any deviation from the provisions of the Code on Corporate Governance Practices contained in Appendix 15.~~:~~;

~~(3) details of non-compliance (if any) with rules 5.05(1) and 5.05(2) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to appointment of a sufficient number of independent non-executive directors and an independent non-executive director with appropriate professional qualifications or accounting or related financial management expertise, respectively; and~~

~~(4) details of non-compliance with rule 5.28 (if any) and an explanation of the remedial steps taken by the listed issuer to address such non-compliance relating to establishment of an audit committee.~~

.....

18.83 Listed issuers are encouraged to disclose the following additional commentary on management discussion and analysis in their half-year and annual reports:-

(1) efficiency indicators (e.g. return on equity, working capital ratios) for the last 5 financial years indicating the bases of computation;

(2) industry specific ratios, if any, for the last 5 financial years indicating the bases of computation;

(3) a discussion of the listed issuer's purpose, corporate strategy and principal drivers of performance;

(4) an overview of trends in the listed issuer's industry and business;

(5) a discussion on business risks (including known events, uncertainties and other factors which may substantially affect future performance) and risks management policy;

(6) a discussion on the listed issuer's environmental policies and performance, including compliance with the relevant laws and regulations;

(7) a discussion on the listed issuer's policies and performance on community, social, ethical and reputational issues;

(8) an account of the listed issuer's key relationships with employees, customers, suppliers and others, on which its success depends; and

(9) receipts from, and returns to, shareholders.

Note: Issuers should also note the recommended disclosures set out in paragraph 3 of Appendix 16.

APPENDIX D
NON-STATUTORY GUIDELINES ON DIRECTORS' DUTIES

The non-Statutory Guidelines on Directors' Duties are reproduced with the permission of the Hong Kong Companies Registry. All rights reserved. The latest version of the Guidelines is available for downloading from the "List of Circular" section of the Companies Registry's homepage on the internet (website: http://www.info.gov.hk/cr/) or at the enquiry counters of the Companies Registry on the 13th and 14th floors of the Queensway Government Offices.

Introduction

In general the responsibilities and liabilities of directors derive from various sources, including the constitution of the company, case law and statute law. If a person does not comply with his duties as a director he may be liable to civil or criminal proceedings and may be disqualified from acting as a director.

Although case law sets out and elaborates on most of these significant principles, it tends to be complex and inaccessible. The objective of these guidelines is to outline the general principles for a director in the performance of his functions and exercise of his powers.

All directors should read these guidelines which are also readily accessible on the websites of the Companies Registry, the Hong Kong Stock Exchange, the Securities and Futures Commission, the Official Receiver's Office and the Hong Kong Monetary Authority. Hard copies are also available at their offices.

Companies should give a copy of these guidelines to new directors irrespective of whether they organize induction training for directors. In addition, directors are also encouraged to refer to more detailed reviews of the role and duties of directors in law. For example, the Hong Kong Institute of Directors has issued the Guidelines for Directors (1995) and the Guidelines for Independent Non-Executive Directors (2000). Directors should also refer to the Code of Best Practice issued by the Stock Exchange of Hong Kong to improve the manner in which their companies are managed.

It is important to note that the statements in these guidelines are principles only and are not intended to be exhaustive statements of the law. Furthermore, statute or case law could require certain forms of conduct under specified circumstances. If directors are at all in doubt about the nature of their responsibilities and obligations, they should seek legal advice.

The general principles of directors' duties

Principle 1: Duty to act in good faith for the benefit of the company as a whole

A director of a company must act in good faith in the best interests of the company. This means that a director owes a duty to act in the interests of all its shareholders, present and future. In carrying out this duty, a director must (as far as practicable) have regard to the need to achieve outcomes that are fair as between its members.

Principle 2: Duty to use powers for a proper purpose for the benefit of members as a whole

A director of a company must exercise his powers for a "proper purpose". This means that he must not exercise his powers for purposes that are different from purposes for which they were conferred. The primary and substantial purpose of the exercise of a director's powers must be for the benefit of the company. If the primary motive is found to be for some other reasons (e.g. to benefit one or more directors and to gain control of the company), then the effects of his exercise of his power may be set aside. This duty can be breached even if he has acted in good faith.

Principle 3: Duty not to delegate powers except with proper authorization and duty to exercise independent judgement

Except where authorised to do so by the company's memorandum and articles of association (the "constitution") or any resolution, a director of a company must not delegate any of his powers. He must exercise independent judgement in relation to any exercise of his powers.

Principle 4: Duty to exercise care, skill and diligence

A director of a company must exercise the care, skill and diligence that would be exercised by a reasonable person with the knowledge, skill and experience reasonably expected of a director in his position. In determining whether he has fulfilled this duty, the court will also consider whether he has exercised the care, skill and diligence that would be exercised by a reasonable person with any additional knowledge, skill and experience which he has.

Principle 5: Duty to avoid conflicts between personal interests and interests of the company

A director of a company must not allow personal interests to conflict with the interests of the company.

Principle 6: Duty not to enter into transactions in which the directors have an interest except in compliance with the requirements of the law

A director of a company has certain duties where he has a material interest in any transaction to which the company is, or may be, a party. Until he has complied with these duties, he must not, in the performance of his functions as a director, authorise, procure or permit the company to enter into a transaction. Furthermore, he must not enter into a transaction with the company, unless he has complied with the requirements of the law.

The law requires a director to disclose the nature of his interest in respect of such transactions. Under certain circumstances the constitution may prescribe procedures to secure the approval of directors or members in respect of proposed transactions. A director must disclose the relevant interest to the extent required. Where applicable, he must secure the requisite approval of other directors or members.

Principle 7: Duty not to gain advantage from use of position as a director

A director of a company must not use his position as a director to gain (directly or indirectly) an advantage for himself, or someone else, or which causes detriment to the company.

Principle 8: Duty not to make unauthorized use of company's property or information

A director of a company must not use the company's property or information, or any opportunity that presents itself to the company, of which he becomes aware as a director of the company. This is except where the use or benefit has been disclosed to the company in general meeting and the company has consented to it.

Principle 9: Duty not to accept personal benefit from third parties conferred because of position as a director

A director or former director of a company must not accept any benefit from a third party, which is conferred because of the powers he has as director or by way of reward for any exercise of his powers as a director. This is unless the company itself confers the benefit, or the company has consented to it by ordinary resolution, or where the benefit is necessarily incidental to the proper performance of any of his functions as director.

Principle 10: Duty to observe the company's memorandum and articles of association and resolutions

A director of a company must act in accordance with the company's constitution. He must also comply with resolutions that are made in accordance with the company's constitution.

Principle 11: Duty to keep proper books of account

A director of a company must take all reasonable steps to ensure that proper books

of account are kept so as to give a true and fair view of the state of affairs of the company and explain its transactions. To avoid breaching the fraudulent trading provisions in section 275 of the Companies Ordinance (Cap. 32), a director must not allow the company to incur further credit knowing that there is no reasonable prospect of avoiding insolvency.

Companies Registry
January 2004

APPENDIX E
USEFUL WEBSITES OR CONTACT DETAILS

Abbott Stillman & Wilson	www.asw.net.au
Charltons	www.charltonslaw.com
Geoffrey P. Williams	geoffrey@williams.name
SACS Executive Solutions	www.sacsexec.com.au
STOPline Pty Ltd	www.stopline.com.au
The Hong Kong Companies Registry	www.info.gov.hk/cr/
The Hong Kong Institute of Directors	www.hkiod.com
The Hong Kong Securities and Futures Commission	www.hksfc.org.hk
The Hong Kong Society of Accountants	www.hksa.org.hk
The Stock Exchange of Hong Kong Limited	www.hkex.com.hk

APPENDIX F
BIBLIOGRAPHY

Further recommended reading:

1. Guy Pease & Karen McMillan. The Independent Non-Executive Director. Melbourne Aust. – Longman Professional 1993
2. Kiel & Nicholson. Boards That Work. R.McGraw Hill Aust. 2003
3. M.Porter. The Competitive Advantage of Corporate Philanthropy. Harvard Business Review. Dec. 2002.

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1. *Encycogov.com:The Encyclopaedia about Corporate Governance*
2. *J. Wolfensohn, president of the World Bank, as quoted in Financial Times June 21, 1999*
3. *Securities and Futures Ordinance (Cap.571) of the Laws of Hong Kong*
4. *Companies Ordinance (Cap.32) of the Laws of Hong Kong*
5. *See section 180(2) of the Corporations Act 2001 of Australia. The Business judgment rule will protect those directors who make business judgments in good faith and for a proper purpose, have acted on an informed basis without material personal interest and who have a rational belief that the decision is in the best interests of the corporation*
6. *Kiel & Nicholson Op Cit.*
7. *AWA Case (1992) 10 ACLC 933, Daniels & Ors (1995) 13 ACLC 614*
8. *Kiel & Nicholson Op Cit.*
9. *2003 SACS Executive Solutions Corporate Governance report*
10. *Pease & McMillan Op Cit.*
11. *ASIC v John David Rich & Ors ([2003] NSWSC 85)*
12. *ASX Corporate Governance Council. Principles of Good Corporate Governance and Best Practice Recommendations March 2003*
13. *Telecommunications Ordinance (Cap.106) of the Laws of Hong Kong*
14. *Interception of Communications Ordinance (Cap.532) of the Laws of Hong Kong*
15. *M Porter. The Competitive Advantage of Corporate Philanthropy. Harvard Business Review Dec. 2002*
16. *Loc Cit p.67*
17. *Op Cit.*
18. *Op Cit p.61*

19. *For example the Whistleblowers Protection Act 2001 of Victoria which allows any person to make a disclosure against any public office or public body.*

20. *Falconer op.cit.*

21. *Falconer op.cit.*

22. *The Main Board Listing Rules and the GEM Listing Rules*

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