
WHAT DO THE PANAMA PAPERS TEACH US
ABOUT THE ADMINISTRATIVE LAW OF CORPORATE
GOVERNANCE REFORM IN HONG KONG?*

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Abstract

A complex business environment calls for a flexible administrative law for the agencies that oversee corporations. Nowhere illustrates this maxim better than Hong Kong, and its need to reform corporate regulations after the Panama Papers revelations. We describe how only a “non-administrative” administrative law can best cope with the challenges facing the regulation of corporate governance. Such a flexible, results-oriented approach to administrative law develops new principles and tests, rather than gives civil servants instructions. Such an approach to corporate governance can facilitate the assessment of company governance, corporate disclosure, the self-regulation of professional groups like lawyers and accountants, as well as ensure corporations engage in “legitimate economic purposes.” We engage with the literature, showing why such a flexible approach to administrative rulemaking would more likely reduce some of the government regulation and oversight problems exposed by the Panama Papers than previous approaches toward drafting and implementing administrative law (at least in this area).

I. INTRODUCTION

The Panama Papers revealed serious defects in Hong Kong’s corporate governance. Particularly, the scandal showed the lapses in the way Hong Kong’s government regulates and checks its financial firms and professional services providers.¹ While Hong Kong’s government has failed to conduct (or at least publicly release) a study looking at the harms of the Panama Papers revelations, the European Union has.² At first, the study looks like any other ordinary impact assessment – looking at the tax law, corporate law, and the regulation of financial institutions. Look more deeply though, and one sees a

¹ For the full extent of the way that the Panama Papers shines a light on Hong Kong’s regulation, see Jane Moir, *Panama Papers: What are the Implications on Hong Kong’s “Anti-Money Laundering” Credentials?*, H.K. LAW. (July 6, 2016), <http://www.hk-lawyer.org/content/panama-papers-what-are-implications-hong-kong%E2%80%99s-%E2%80%9Canti-money-laundering%E2%80%99%E2%80%99-credentials>.

² See EUROPEAN PARLIAMENT, *THE IMPACT OF SCHEMES REVEALED BY THE PANAMA PAPERS ON THE ECONOMY AND FINANCES OF A SAMPLE OF MEMBER STATES 1-12* (2017), http://www.europarl.europa.eu/RegData/etudes/STUD/2017/572717/IPOL_STU%282017%29572717_EN.pdf.

study about EU administrative law. The study looks at the rules the EU and its Member States' ministries of finance should put in place to deal with the way they (these government bodies) should regulate, inspect and so forth. In other words, how EU member states' (and the EU's in general) administrative law should change. Administrative law represents an unloved branch of public law. Yet, as the Panama Papers revelations show, the way government ministries, agencies, and even independent bodies invested with public power, regulate and investigate (or not) strikes at the heart of administrative law.³ The old days of administrative law as fixed, specific rules – given to civil servants and other public officials – are numbered.

In this paper, we argue that a new way of thinking about administrative law is needed to remedy the problems revealed by the Panama Papers. That new way (not very new for many governments) involves regulating what public entities do and the goals of their work, rather than the way they do it. Government increasingly has and takes responsibility for the conduct of all kinds of groups in society – including companies. Government's role in influencing corporate governance shows how and why we need to re-conceive of administrative law as a law of ends, rather than means. Such law can encourage groups to assess corporate governance (or not), encourage disclosure (or not), self-regulate (or not), and even nudge corporate and other types of law toward focusing on legitimate ends rather than regulating conduct. Any conception of administrative law as simply listing an agency's rights and obligations sorely misses the need for ambiguity and flexibility in public administration (two features antithetical to the classic predictability-and-clarity way of understanding administrative law).⁴ Remediating the wrongs found in

³ Interestingly, few studies look at the administrative law side of corporate governance. One of the more popular studies finds strong norms underlying, what appears on the surface, like regular rules and regulations governing the procedural and substantive rights of the regulated. We return to this theme throughout this paper. See Zumbansen Peer, *Neither "Public" nor "Private", "National" nor "International": Transnational Corporate Governance from a Legal Pluralist Perspective*, 38 J. L. & Soc'y 50, 75 (2011).

⁴ Few in the field of public administration would dispute such a statement. The field of administrative law though, continues to see administrative action through 19th century lenses. For an analysis of the disconnect between the fields of administrative law and public administration, see Gillian E. Metzger, *Administrative Law, Public Administration, and the Administrative Conference of the United States*, 83 GEO. WASH. L. REV. 1517, 1539 (2015). Like us, Metzger uses financial law to most clearly illustrate this difference. See also Gillian E. Metzger, *Through the Looking Glass to a*

the Panama Papers will require rules far more results-focused and far less mechanical than most administrative law.

Each section of this paper illustrates how a more flexible, results-oriented view of administrative law (Hong Kong's in particular) can help to remove the poor corporate governance identified by/in the Panama Papers. The first section presents data covering the major issues and problems in Hong Kong identified in the Panama Papers. The second section shows how government rules can encourage the practical, useful and accurate measurement of corporate governance quality. The third section discusses administrative law's role in encouraging corporate disclosure. Such a role revolves far more around encouraging private actors to act (or not) than controlling or checking companies. The fourth section describes the way administrative law can channel the incentives of self-regulating bodies, like lawyers and accountants. The fifth section most concretely illustrates the issues arising in the previous sections – in the form of a principles-based test for legitimate economic purposes. Government has certain ends to incentivize – often developing administrative principles or tests to help guide civil servants as they channel private sector incentives.⁵ Each of these sections describes a facet of such incentivisation. The final section concludes.

We ask for the readers' indulgence as we make our argument with the following limitations in mind. First and most importantly, we do not make the case for or against such an approach to administrative law. We only try to observe the world – and draw conclusions about the approach which would most reduce the problems identified by the Panama Papers. Our tone reflects the outcome of that consideration – rather than any attempt to sell the reader on any particular approach. Second, we do not provide a classical literature review, showing how our understanding of the form and needs of administrative law have changed over time.⁶

Shared Reflection: The Evolving Relationship between Administrative Law and Financial Regulation, 78 *LAW & CONTEMP. PROBS.* 129, 156 (2015).

⁵ See, e.g., Vicki C. Jackson, *Constitutional Law in an Age of Proportionality*, 124 *YALE L.J.* 2680, 3203 (2015). See also Thomas Poole, *Between the Devil and the Deep Blue Sea: Administrative Law in an Age of Rights* (LSE Law Soc'y & Econ., Working Papers No. 9, 2008), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2501426.

⁶ We hardly need to provide such a review – given the wide-spread recognition of the failure of classical public administration and administrative law as branches of social science inquiry. See

Instead, we grapple directly with this evolving view of administration law's role in the broader legal framework through the four major reform areas identified by the Panama Papers. We apologise beforehand to any readers uncomfortable with our engaging the literature as we talk about changes in Hong Kong's rules and regulations – giving almost a “literature review on the fly.”⁷ Third and relatedly, we do not survey every area of administrative law (or the public sector agencies in which such law holds reign).⁸ We use the specific area of law affecting corporate governance in order to illustrate broader trends affecting all areas of the public administration.⁹ We leave to the readers' good judgement and prior knowledge the extent to which our analysis covers changes to the broader administrative field.¹⁰ Fourth, we write about prescriptive change in Hong Kong – describing the way law should effect normative rather than positive change. In other words, and parroting the literature we review, we talk certain reforms almost as a *fait accompli*. We do this to focus our paper on our main argument, dealing with the way our conception of administrative law must change, rather than weighing the pros and cons of each reform.¹¹

Francesca Bignami, *From Expert Administration to Accountability Network: A New Paradigm for Comparative Administrative Law*, 59 AM. J. COMP. L. 859, 908 (2011). See also Sabino Cassese, *New paths for Administrative Law: A Manifesto*, 10 INT'L J. CONST. L. 603, 613 (2012).

⁷ The fruitless discussion of “global administrative law” illustrates the need to keep our discussion specific – without pontificating about general trends, while offering little in the way of concrete proof. See, e.g., KARL-HEINZ LADEUR, *THE EVOLUTION OF GENERAL ADMINISTRATIVE LAW AND THE EMERGENCE OF POSTMODERN ADMINISTRATIVE LAW* 4-16 (Peer Zumbansen et al. eds, 2011). See also Richard B. Stewart, *U.S. Administrative Law: A Model For Global Administrative Law?*, 68 LAW & CONTEMP. PROBS. 63, 108 (2005).

⁸ Bingham for example tries (maladroitly) to deal with this problem by finding common values across administrative laws. See Lisa Blomgren Bingham, *The Next Generation of Administrative Law: Building the Legal Infrastructure for Collaborative Governance*, 2010 WIS. L. REV. 297, 356 (2010).

⁹ The literature commonly uses such an approach for tackling such a large and ambitious project. For just one example, in this case using environment-related administrative law to illustrate broader themes in administrative law, see Eric Biber, *Adaptive Management and the Future of Environmental Law*, 46 AKRON L. REV. 933, 962 (2013).

¹⁰ For example, many US analysts see administrative law transforming as the result of judicial activism (basically power grabbing) – rather than as coping with an increasingly complex business/social environment. We do not try to present or evaluate these claims – which obviously partly explain Hong Kong's own regulatory paroxysms. See Daniel B. Rodriguez & Barry R. Weingast, *The “Reformation of Administrative Law” Revisited*, 31 J. L. ECON. 782, 807 (2015).

¹¹ As Howson does, we forgo judging particular corporate governance reforms to look at their effect on law in general. See Nicholas Calcina Howson, *“Quack Corporate Governance” as Traditional Chinese Medicine – The Securities Regulation Cannibalization of China's Corporate Law and a State*

II. WHAT THE PANAMA PAPERS REVEAL ABOUT HONG KONG'S FAILURE TO REGULATE

A recent hacking scandal illustrates the problems with laws regulating private sector activity – and the role that off-shore entities play – in undermining such law. The massive online release of files related to the offshore incorporation services provider Mossack Fonseca illustrates some of the weaknesses in corporate governance regulation in the Asian region.¹² The 2015 revelations shows that Mossack Fonseca's affiliates in Hong Kong – like P&P Secretarial Management and its British Virgin Islands registered interest Harvest Sun Trading – helped set up thousands of shell companies.¹³ At its apogee, the firm set up 2,428 companies in 2012.¹⁴ Many of these offshore entities, namely a non-trading corporation (or entity with tradable/transferrable interests) that do not conduct significant operations related to the transformation of inputs into marketable outputs, may serve a valid economic/business purpose. Yet, many of them helped facilitate crime.¹⁵ The Panama Papers scandal thus exposed a veritable network of offshore financial centres helping facilitate corporate fraud, corruption, and corporate misgovernance.¹⁶

Regulator's Battle Against Party State Political Economic Power, 37 SEATTLE U. L. REV. 667, 716 (2014).

¹² For more on the events relates to the hacking scandal, and the related legal issues, see Lawrence Trautman, *supra* note 8.

¹³ Stuart Lau, *Revealed: Panamanian law firm Mossack Fonseca's man in Hong Kong*, SOUTH CHINA MORNING POST (Apr. 10, 2016, 12:45 AM), <http://www.scmp.com/news/hong-kong/law-crime/article/1934948/revealed-panamanian-law-firm-mossack-fonseca-man-hong-kong>.

¹⁴ See Erika Kinetza & Kelvin Chan, *Hong Kong emerges as hub for creating offshore companies*, THE JAKARTA POST (April 10, 2016, 08:16 am), <https://www.thejakartapost.com/news/2016/04/10/hong-kong-emerges-as-hub-for-creating-offshore-companies-.html>.

¹⁵ As the Tax Justice Network shows, these “shell companies” helped perpetrate fraud in roughly 10% of all reverse merger listings of Chinese companies in the US. Floyd describes how the Panama Papers implicated HSBC, a large bank with a significant presence in Hong Kong, in setting up roughly 2,300 accounts – contravening banking regulations. See Offshore Alert, *1 in 10 Reverse Mergers of Chinese Firms on US Stock Exchanges “Fraudulent”*, TAX JUST. NETWORK (Mar. 18, 2011), <http://taxjustice.blogspot.com/2011/03/1-in-10-reverse-mergers-of-chinese.html>. See also David Floyd, *Panama Papers: Top 10 Banks for Offshore Companies (CS, HSBC)*, INVESTOPEDIA (Apr. 6, 2016), <https://www.investopedia.com/articles/investing/040616/panama-papers-top-10-banks-offshore-companies-cs-hsbc.asp>.

¹⁶ We cannot describe all the ways the entire offshore system, or all the revelations unearthed in the scandal. For the data and a much more extensive discussion of Hong Kong's position in this network, see Bryane Michael & Say Hak Goo, *The Role of Hong Kong's Financial Regulations in Improving Corporate Governance Standards in China: Lessons from the Panama Papers for Hong Kong* (Univ. of H.K. Faculty of Law Research, Working Paper No. 048, 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2914865.

Hong Kong belongs to this network of offshore financial centres – some of whom sometimes help launder ill-gotten gains. Table 1 shows the jurisdiction of incorporation and number of companies listed on Hong Kong Stock Exchange (hereinafter referred to as “HKEx”). The British Virgin Islands (hereinafter referred to as “BVI”) plays a key role in Hong Kong’s foreign investment and incorporation business. Hong Kong could plausibly attract productive companies from the US, UK, Singapore, and the Mainland to list on its stock market. But what productive enterprise needs investment in the Cayman Islands, the BVI or Liberia? The Mossack Fonseca hack revealed Hong Kong’s importance in the wider networks of offshore companies cycling money to each other.¹⁷ Yet, given the wide-spread adoption of anti-money laundering and related regulations across the financial centres, combined with low taxes in many jurisdictions nowadays, one must ask what benefits do Hong Kong companies get from incorporating elsewhere?¹⁸ Given Hong Kong’s regulatory similarity with the BVI and other offshore centres, why would companies need these other offshore centres’ services at all?¹⁹

TABLE 1 WHY DO WE ACCEPT SHELLS FROM BVI AND OTHER INCORPORATION MILLS?

| | | | |
|------------------------|------|------------------|-----|
| Bermuda | 655 | Marshall Islands | 187 |
| British Virgin Islands | 1174 | Panama | 337 |
| Cayman Islands | 3894 | Singapore | 228 |
| China | 296 | Taiwan | 80 |
| Japan | 185 | UK | 282 |
| Liberia | 206 | USA | 499 |

The data in the table shows the number of Hong Kong listed companies domiciled in each of the jurisdictions shown. 16 islands appear in the top 50 jurisdictions (ranked by head-count number of companies domiciled there).

Source: webb-site.com

¹⁷ See Kinetza & Chan, *supra* note 14.

¹⁸ Most authors have already answered this question as evading national corporate and business laws. See Richard K. Gordon, *On the Use and Abuse of Standards for Law: Global Governance and Offshore Financial Centers*, 88 N.C. L. REV. 501, 594 (2010). See also James McConvill, *An Unstoppable Force Rather Than an Illegitimate Farce: Exploring the Role of Offshore Financial Centres Amid Renewed Criticism*, 25 EUR. BUS. L. REV. 877, 891 (2014).

¹⁹ For more on this convergence, see J. Sharman, *Power and Discourse in Policy Diffusion: Anti-Money Laundering in Developing States*, 52 INT’L STUD. Q., 635, 656 (2008).

Hong Kong's financial and company secretarial advisory institutions' participation in the offshore shenanigans elucidated by the Panama Papers shows why companies need these offshore centres.²⁰ Figure 1 shows the sheer number of Hong Kong financial institutions and related parties identified in Papers.²¹ The Panama Papers data indicate that at least 12 offshore banks and 3 intermediaries in Hong Kong had dealings with Mossack Fonseca. These numbers may not appear large. But taking into account finance and securities companies as well, over 500 companies had a touch with Hong Kong. Both the Panama Papers, and numerous other studies, show how offshore companies can incentivise corporate managers and owners to engage in poor corporate governance practices. The recent World Bank study on shell companies, in particular, provides numerous examples of poor corporate governance practices facilitating the use of shell companies to siphon away money from these corporations themselves.²² A Basel Committee on Banking Supervision communiqué signed by several officials, even from tax havens themselves (such as Jersey, Bermuda, Cayman, and Guernsey), urged the closing of shell banks and

²⁰ Company secretary advisors consist of companies whose niche market focuses on providing corporations with advice on incorporation, filing corporate documents, accounting services, and even sometimes providing "nominee" directors and shareholders. For more information on these providers, and the corporate secretary more generally, see H.K. KONG INST. CHARTERED SECRETARIES (CSJ), THE SIGNIFICANCE OF THE COMPANY SECRETARY - IN HONG KONG'S LISTED COMPANIES 20-39 (2012), https://www.hkics.org.hk/media/publication/attachment/PUBLICATION_A_2336_Research%20Report%202012_Eng.pdf.

²¹ The leak of the Panama-based law firm Mossack Fonseca's client data lead to revelations about the use of offshore companies. The wide-spread media attention paid to these data dubbed the circumstances leading to the use of Mossack Fonseca's services as the Panama Papers scandal. We refer to the Panama Papers data in this paper as data from the International Consortium of Investigative Journalists' (ICIJ) Offshore Leaks Database. The database includes information from the Panama Papers, the Offshore Leaks and the Bahamas Leaks. Yet, we refer to Panama Papers only as a shorthand for these combined search results to make our paper easier to read. See Dale Fast, *History of Biology and Medicine*, SAINT XAVIER U., https://faculty.sxu.edu/~fast/general_biology/hisory.htm (last updated Oct. 31, 2001).

²² See WORLD BANK, THE PUPPET MASTERS: HOW THE CORRUPT USE LEGAL STRUCTURES TO HIDE STOLEN ASSETS AND WHAT TO DO ABOUT IT (World Bank Publications Press 2011). For example, Anglo-Leasing (Kenya) won a lucrative government tender to supply passport services at a cost five times higher than the lowest bidder. This UK mailbox-registered company subcontracted to the French firm who actually put in the lowest bid to do the work. In another case, investigators found that DaimlerChrysler Automotive Russia SAO sent improper payments to 25 bank accounts scattered around the world in order to engage in, and hide, bribe payments. Without these avenues to launder money, these firms' corporate governance might have been better.

offshore booking centres as early as 2003.²³ These data (illustrated in Figure 1) and public statements illustrate the broader conclusion reached by academics themselves – that these offshore companies tend to undermine the quality of corporate governance.

FIGURE 1 PANAMA PAPERS' FINANCIAL INSTITUTIONS LINKED WITH HONG KONG



The figure shows the results of searches on the ICIJ's Panama Papers Database (which includes other documents from previous leaks). We searched on the keyword "bank", "finance" and "securities" for each broad category, and then searched in the second instance for any connection with Hong Kong. Source: ICIJ (2016).

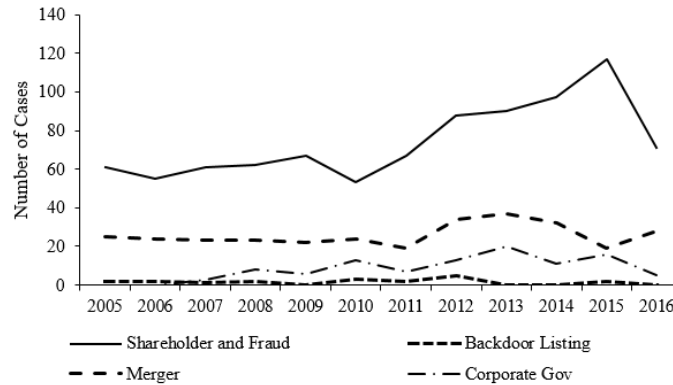
The lack of corporate governance-related disputes brought to court means that Hong Kong jurisprudence cannot develop the same kind of legal innovations and doctrines which have arisen in the US and UK. Figure 2 shows the number of cases appearing in Hong Kong's courts due to poor corporate governance, fraud or disputes over mergers and so forth. Shareholder fraud represents the largest reason for litigation in Hong Kong's courts among the four factors we searched for – shareholder fraud, disputes over mergers, backdoor listings, and/or corporate governance-related disputes.²⁴ Such disputes have increased very slightly, in absolute terms, over the course of the last decade. The lack of such cases means that, unlike in the US, these cases have created no law – administrative or otherwise – as a way of remedying corporate governance and other problems. If legal doctrines and concepts like "derivative actions",

²³ Basel Committee on Banking Supervision, *Shell Banks and Booking Offices*, BANK FOR INT'L SETTLEMENT (Jan. 2003), <https://www.bis.org/publ/bcbs95.pdf>.

²⁴ For the last factor, we simply searched on the key word "corporate governance" – thus we do not try to dig too deeply into exactly what the experts categorize under that rubric.

“proper purpose” and “corporate opportunity” emerged from the crucible of litigation, then not enough cases have gone into Hong Kong’s crucible (courts) to dent the law.²⁵

FIGURE 2 ARE ROUGHLY 80 LITIGATED CASES OF FRAUD WORTH CORPORATE GOVERNANCE REFORM IN HONG KONG?



The figure shows the number of cases in which each of the keywords shown appear. We extrapolated the 2016 data based on the number of cases up to 25 September.

Source: Lexis Hong Kong (2016).

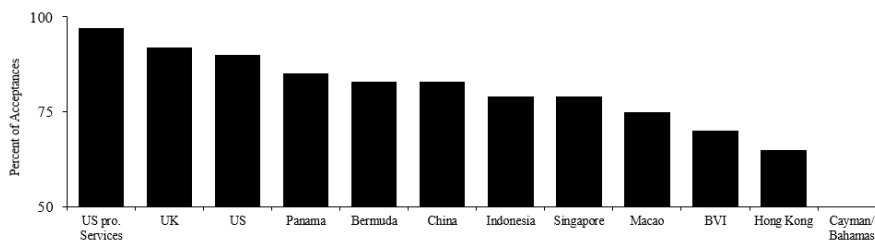
The extent to which professional service providers aided in setting up the offshores which facilitated poor corporate governance shows the need for a broader policy response – and thus the action of public officials and civil servants guided by administrative laws. Figure 3 shows the percent of professional services firms accepting an approach to provide shell company incorporation services to an individual posing as a client engaged in illegal/unethical conduct.²⁶ Hong Kong’s professionals refuse suspicious applications for shell companies far more often than other jurisdictions. Yet, as Figure

²⁵ Donald Clarke & Nicholas Howson, *Pathway to Minority Shareholder Protection: Derivative Actions in the People’s Republic of China*, in *THE DERIVATIVE ACTION IN ASIA: A COMPARATIVE AND FUNCTIONAL APPROACH* (Cambridge Univ. Press 2012). See Wen-Jing Chen, *An Overview of Shareholder Litigation*, in *A COMPARATIVE STUDY OF FUNDING SHAREHOLDER LITIGATION* (2017).

²⁶ In the experiment, the individuals posing as clients hinted or even claimed they needed the company to move bribe payments for persons convicted of crimes for example. In other words, the person providing the incorporation services clearly knew the intended use (abuse) of the corporation. Most jurisdictions laws forbid incorporation service providers from serving these kinds of customers. See MICHAEL FINDLEY et al., *GLOBAL SHELL GAMES: TESTING MONEY LAUNDERERS’ AND TERRORIST FINANCIERS’ ACCESS TO SHELL COMPANIES* (2014).

shows, Hong Kong's law firms lodge only a small fraction of suspicious transaction reports submitted by financial services firms – something every service provider must do under law.²⁷ Reducing the use of offshores to facilitate corruption – or at the very least self-serving corporate behaviour by managers and owners – will undoubtedly require more government inspections, oversight and rules imposed on professional service firms.²⁸ Clearly, the administrative law governing the way financial regulators, professional services regulators, and risk-analysts in numerous government departments dealing with money laundering, self-serving by corporate insiders, and other corporate governance failures needs such revision.²⁹

FIGURE 3 HONG KONG'S DODGY PROFESSIONAL SERVICE PARTNERS ABOARD



The figure shows the percent of professional service providers willing to set up a shell company for academics posing as terrorists or persons with questionable motives. We have subtracted the original data from 100 (as the original data showed the percent refusing to provide services). The tax havens themselves are clean. Their clients, however, very easily facilitate the creation of shell companies.

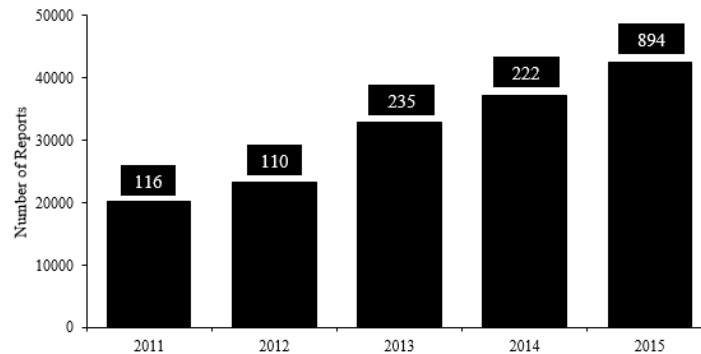
Source: Findley et al. (2012).

²⁷ See Stephen Mulrenan, *Asia: Panama Papers – No News is Good News*, INT'L B. ASS'N (June 7, 2016), <https://www.ibanet.org/Article/NewDetail.aspx?ArticleUid=7829e0b5-1d4d-4477-b3fb-46140cdad0a>.

²⁸ A recent policy brief produced by/for Hong Kong's Legislative Council shows the extent of such extra oversight. See LC Paper No. CB(1)1456/16-17(08), Bills Committee on Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) (Amendment) Bill 2017 and Companies (Amendment) Bill 2017 Background Brief (Oct. 9, 2017)(enacted), <https://www.legco.gov.hk/yr16-17/english/bc/bc07/papers/bc0720171010cb1-1456-8-e.pdf>.

²⁹ The literature on Hong Kong's corporate governance rules extends too far to review here. For a discussion of some of the issues, see Yu-Hsin Lin, *Controlling Controlling-Minority Shareholders: Corporate Governance and Leveraged Corporate Control*, 2017 COLUM. BUS. L. REV. 453, 510 (2017). If Hong Kong's corporate governance rules worked so well, why then would Mainland companies seek to comply with even harsher rules in order to attract investors? See also Meng Fangpeng, *Legal vs. Reputational Bonding: Board Independence of Chinese Companies Listed in Hong Kong 4-8* (CFRED Working Paper No. 8, 2002) https://www.law.cuhk.edu.hk/en/research/cfred/download/CFRED_WP8_Frank%20Meng_Legal_vs_Reputation_Bonding_2.pdf.

FIGURE 4 LESS THAN 2% OF HONG KONG'S SUSPICIOUS TRANSACTION REPORTS FROM LAW FIRMS



The figure shows the number of suspicious transaction reports filed with Hong Kong's anti-money laundering agency for the period shown. The black boxes show the number of these reports from law firms...roughly 2% of them. More than 2% of Hong Kong's legal advisors must know that their clients, using their services, are up to no good.

Source: Findley et al. (2012).

These data from the Panama Papers show why Hong Kong needs a new and different conception of administrative law – at least in financial and corporate affairs, if not more generally. Regardless of whether Hong Kong's civil servants and businesses follow existing rules, Hong Kong financial institutions' and intermediaries' desire to create and use questionable offshore corporations clearly represents a public policy issue. As we show in the following sections, disincentivizing activities which contribute to poor corporate governance requires administrative rulemaking which focuses on results – and provides civil servants with broader doctrines and tests, rather than specific rules of behaviour.³⁰ In other words, such an administrative law should be “non-administrative”, namely far less bureaucratic, specific and rules-based.³¹ Many of the principles

³⁰ The literature has come to a consensus that principles-based administrative rulemaking is not an all-of-nothing proposition. Yet, finding the right balance between broader results-oriented rules, and specific rules of action for regulators and others, represents the key task. See Linda M. Sama & Victoria Shoaf, *Reconciling Rules and Principles: An Ethics-Based Approach to Corporate Governance*, 58 J. BUS. ETHICS 177, 185 (2005). See also Surendra Arjoon, *Striking a Balance Between Rules and Principles-based Approaches for Effective Governance: A Risks-based Approach*, 68 L. BUS. ETHICS 53, 82 (2006).

³¹ Despite decades of calls for such administrative law, we refer to such law as non-administrative rather than enlightened, and share our peers' views that current attempts to make administrative even more detailed represents a “scholarly dead end.” See Sidney A. Shapiro et al., *The Enlightenment of*

eventually adopted in the private sectors should start in administrative law (namely be used in the public sector first).³²

III. REGULATING CORPORATE GOVERNANCE INDICATORS AND ASSESSMENT

The assessment of the quality of corporate governance in Hong Kong and the Mainland represents more than just interesting data. Authors like Abbott and Snidal argue that governance systems have completely changed in recent years.³³ Calling the new system *Transnational New Governance*, these authors argue that the onus of regulation and enforcement has moved from government agencies to the wider business sector and civil society. Yet, as corporate governance survey work shows, academics and others conduct these assessments on an *ad hoc* basis – jeopardizing their comprehensiveness and repeatability.³⁴ Political concerns and the formality attached to official corporate governance peer reviews – like those championed by the Financial Stability Board – distort the data too much to use in academic or policy settings.³⁵ The Financial Stability Board has no apparent mechanism or funding source in place to ensure regular objective evaluation (ie. not simply asking government officials what they think about their jurisdiction's corporate governance rules). The review by Organisation for Economic Co-operation and Development (hereinafter referred to as

Administrative Law: Looking inside the Agency for Legitimacy, 47 WAKE FOREST L. REV. 463, 502 (2012).

³² For example, many countries' administrative law has evolved to include a precautionary principle, risk-based criteria and proportionality as part of core administrative doctrine. Many multinationals now use these principles when taking decisions. Who can say whether further evolution along these lines will lead to rules focused far more on outcomes than means/processes? See Jin Zining, *Introducing the Precautionary Principle into Administrative Law: Facing the Challenges to the Rule of Law*, 19 ACADEMIA SINICA L.J. 53, 97 (2016).

³³ See Kenneth W. Abbott & Duncan Snidal, *Strengthening International Regulation through Transnational New Governance: Overcoming the Orchestration Deficit*, 42 VAND. J. TRANSNAT'L L. 501, 578 (2009).

³⁴ See, e.g., Yan Leung-Cheung & Hasung Jang, *Scorecard on Corporate Governance in East Asia: A Comparative Study*, in INSTITUTIONAL APPROACH TO GLOBAL CORPORATE GOVERNANCE: BUSINESS SYSTEMS & BEYOND 9, (JAY CHOI & SANDRA DOW eds. 2008).

³⁵ The "assessment" consists of asking government officials from each jurisdiction what they think about the various corporate governance rules in place in their jurisdiction. For more on the Financial Stability Board's intention to engage in such corporate governance peer review, see Financial Stability Board (FSB), *FSB Launches Peer Review of the G20/OECD Principles of Corporate Governance and Invites Feedback from Stakeholders*, (Aug. 8, 2016), <https://www.fsb.org/2016/08/fsb-launches-peer-review-of-the-g20oecd-principles-of-corporate-governance-and-invites-feedback-from-stakeholders/>.

“OECD”) on corporate governance around the world ostensibly represents an excellent starting point for evaluating corporate governance rules in Hong Kong.³⁶ Yet, these evaluations fail to gather information about the implementation and effects of these corporate governance rules. Many even criticize that assessments based on codes of corporate governance were developed directly or indirectly (through their work on OECD, CSLA and other assessors’) by the companies being assessed themselves.³⁷

The most obvious way to rectify such a lack of objective measurement consists of encouraging a government or quasi-government body to conduct such measurement – and this invokes the need for administrative law-making. The simplest approach to such law-making might consist of “crowding in” such assessment from a credible third-party – like the OECD’s Centre for Cooperation with Non-Members. The OECD has increasingly worked with regional institutions like the Asian Development Bank on corporate governance-related dialogue and meetings for the better part of a decade.³⁸ Unlike peer review done by the Financial Stability Board, and the OECD itself, such cooperation usually involves sending so-called experts to China and elsewhere, to make observations and ratings. Such cooperative arrangements though represent a bugbear for administrative law – in effect outsourcing activities to foreign entities.³⁹ These experts often cannot escape the politicisation of the institutions they do these studies for – in effect making them not-

³⁶ Isaksson et al. provides a broad overview of corporate governance regulations, while the OECD deals in-depth with the specific topics of related party transactions, takeover bids and shareholder meetings. See Mats Isaksson, Winfrid Blaschke, Héctor Lehuedé and Akira Nozaki, SUPERVISION AND ENFORCEMENT IN CORPORATE GOVERNANCE 9-31 (2017), https://read.oecd-ilibrary.org/governance/supervision-and-enforcement-in-corporate-governance_9789264203334-en#page4. See also OECD, OECD CORPORATE GOVERNANCE FACTBOOK (2013), <http://www.oecd.org/daf/ca/Corporate-Governance-Factbook.pdf>.

³⁷ We talk about the potential influence on CSLA (one of the funders of the Asian Corporate Governance Association’s assessments) later. For a discussion of such influence and the way assessing these codes bypasses the main issues, see Beate Sjøfjell, *When the Solution Becomes the Problem: The Triple Failure of Corporate Governance Codes*, 23-55 (Univ. of Oslo Faculty of Law Legal Studies Research, Working Paper No. 2016-11, 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2828579###.

³⁸ For background and information on the latest meeting, see OECD, OECD-ASIAN ROUNDTABLE ON CORPORATE GOVERNANCE 15-25 (2016), <http://www.oecd.org/daf/ca/2016oecd-asiancorporategovernanceroundtable.htm>.

³⁹ See Herbert V. Morais, *The Quest for International Standards: Global Governance vs. Sovereignty*, 50 U. KAN. L. REV. 779, 822 (2002).

very-expert.⁴⁰ While expedient in the short-term, such contracting-out can impair a government's own long-term efforts at monitoring.⁴¹ More damningly, these principles may not even apply – in part or at all – to China (where more than 50% of Hong Kong's listed companies hail from).⁴²

The establishment of a local entity with over-sight competencies for these assessments, but without the actual obligation to carry them out, might bring the best hope for developing administrative law in this area. The Financial Services Development Council represents a quasi-government group tasked with, among other things, doing these kinds of surveys.⁴³ Such evaluation would help develop Hong Kong's administrative law by requiring the development and assessment of rules for the Council to conduct these surveys. The US's recent review of their survey regulations provides both government officials and outsiders with knowledge about those procedures (increasing transparency) and the ability to change/improve them (improving performance).⁴⁴ Such regulation serves an instrumental purpose in the US Evidence-Based Policymaking Commission's work.⁴⁵ Such work may seem simply mechanical or instrumental. Yet, as a Norwegian law review recently noted, even simple procedures for collecting data may comprise an "algorithm" (albeit a very simple one) which increasingly guides

⁴⁰ See Terence C. Halliday, *Legal Yardsticks: International Financial Institutions as Diagnosticians and Designers of the Laws of Nations*, in GOVERNANCE BY INDICATORS: GLOBAL POWER THROUGH QUANTIFICATION AND RANKINGS (K. DAVIS et al. eds., Oxford University Press, 2012).

⁴¹ For a description of these problems in the areas of financial standards and codes, see Layna Mosley, *Regulating Globally, Implementing Locally: The Financial Codes and Standards Effort*, 17 REV. INT'L POL. ECON. 724, 761 (2010). See *id.*

⁴² If Cardona and Farnoux complain that emerging markets must participate more fully in the elaboration of these principles and codes, Wang notes the completely failure of these codes to address the way that non-compliance helps the government or powerful persons. See Michel Cardona & Marc Farnoux, *International Codes and Standards: Challenges and Priorities for Financial Stability*, 1 FIN. STABILITY REV. 143, 154 (2002). See also Jiangyu Wang, *The Political Logic of Corporate Governance in China's State-Owned Enterprises*, 47 CORNELL INT'L L. J. 631, 670 (2014).

⁴³ Specifically citing the Council's Terms of Reference requires the Council, "to conduct policy research and industry surveys for the formulation of proposals to the Government and regulators." *Terms of Reference*, FIN. SERV. DEV. COUNCIL (2013), <http://www.fsdc.org.hk/en/about/mission>.

⁴⁴ US Office of Management and Budget, *Privacy and Confidentiality in the Use of Administrative and Survey Data*, OBAMA WHITEHOUSE ARCHIVES (July 15, 2016), https://obamawhitehouse.archives.gov/sites/default/files/omb/mgmt-gpra/privacy_and_confidentiality_in_the_use_of_administrative_and_survey_data_0.pdf.

⁴⁵ See Evidence-Based Policymaking Commission Act of 2016, Pub. L. No. 114-140, § 4, 130 Stat. 317, 318.

government activity and behaviour.⁴⁶ These algorithms seek particular outcomes – so why regulate the means rather than the ends of their action?

To what extent would administrative law direct an informal body like the Financial Services Development Council and its possible survey work? The Financial Services Development Council itself represents a body which many would not consider a government agency capable of promulgating citable administrative law.⁴⁷ The Council has members who may adopt administrative law in their own government departments. The government relies heavily on work by similar councils (often due to political reasons).⁴⁸ Because their decisions and resources never seem controversial enough to be challenged in court, we do not have an official ruling about the extent of their legality (namely whether they can provide public services, take over work done by others, etc.).⁴⁹ While increasing interest has emerged in reforming these councils and quasi-governmental bodies, academics still cannot agree on whether governments had ever vested legal authority into them (except perhaps as contractors in providing services that businesses could also provide).⁵⁰ Clearly, the law regulating the Council's work must – and does – regulate the ends of its work, rather than the way members and attached civil servants to the Council conduct that work.⁵¹

⁴⁶ Dag Wiese Schartum, *Law and Algorithms in the Public Domain*, 10ETIKK I PRAKSIS 15, 26 (2016).

⁴⁷ As of this writing, the informal body – composed of civil servants – has a request in place to officially hire non-civil servant staff. See EC(2016-17)20, Item for Establishment Subcommittee of Finance Committee (Jan. 4, 2017), <https://www.legco.gov.hk/yr16-17/english/fc/esc/papers/e16-20e.pdf>.

⁴⁸ For an easy to read and understandable overview, see Jake Van Der Kamp, *Does Hong Kong Really Need So Many Obscure and Antiquated "Specialist" Bodies?*, SOUTH CHINA MORNING POST (Sept. 27, 2017), <http://www.scmp.com/business/companies/article/2113076/does-hong-kong-really-need-so-many-obscure-and-antiquated>.

⁴⁹ Despite extensive classification of these bodies and their lawmaking powers, the literature still has not reached any consensus on what the limits of these quasi-autonomous non-governmental organisations' competencies. See Yselt Marique, *The Rule-Making Powers of Independent Administrative Agencies ('QUANGOs'): Comparative Analysis in Fifteen Countries*, 19 SOC. SCI. ELECTRONIC PUB. 109, 120 (2007).

⁵⁰ See Katharine Domett & Muiris MacCarthaigh, *Quango Reform: the Next Steps?*, 36 PUB. MONEY & MGMT. 249, 256 (2016).

⁵¹ Indeed, call its organic regulation a "Terms of Reference" speaks volumes about the regulatory intent to focus on ends rather than means. The Council's governance lies, not in a formal contract per se, but clearly an implicit contract allows the Council to work on public activities as long as certain

What about leaving these assessments up to the market (and thus completely unregulated)? The most important tool at present for assessing corporate governance in Hong Kong (and possibly the whole Asian region) consists of the Asian Corporate Governance Association's (hereinafter referred to as "ACGA") and CSLA's *Corporate Governance Review*.⁵² Table 2 shows a sample of its latest rankings – from 2015.⁵³ The organisation has published these assessments since 2003 – providing potentially comparative data for over 13 years.⁵⁴ Such a track records beats hands-down other institutions, like the Asian Development Bank, which conducts one-off *ad hoc* assessments according to their popularity and funding.⁵⁵ Even the IMF has not been able to assess China's corporate governance.⁵⁶ At first glance, having the non-governmental sector do these assessments – according to their own rules and whims – looks like the way to go.

ends emerge. For the theory of such governance and its fit in administrative law, see Anthony M. Bertelli, *Governing the Quango: An Auditing and Cheating Model of Quasi-Governmental Authorities*, 16 J. PUB. ADMIN. RES. & THEORY 239, 261 (2005).

⁵² *Library - Regional Analysis - ACGA Reports*, ACGA (2016), <https://web.archive.org/web/20160214151401/>.

⁵³ See ACGA, *Market scores: 2010 to 2014*, CG WATCH 2014, fig.1 (2014), <https://www.acga-asia.org/cgwatch-detail.php?id=151>.

⁵⁴ The authors note several changes in definitions which hinder attempts to compare scores across years. We have not assessed such comparability in-depth, so we do not talk more about it. See ACGA, CG WATCH, (Amar Gill & Jamie Allen eds, 2003), <https://www.acga-asia.org/cgwatch-detail.php?id=157>.

⁵⁵ At least they mainly follow the OECD Principles. See ASIAN DEVELOPMENT BANK (ADB), ASEAN CORPORATE GOVERNANCE SCORECARD: COUNTRY REPORTS AND ASSESSMENTS (2013-2014) 1-16 (2014), <https://think-asia.org/bitstream/handle/11540/763/asean-corporate-governance-scorecard.pdf?sequence=1>. See also ADB, ASEAN CAPITAL MARKETS FORUM, CORPORATE GOVERNANCE SCORECARD: COUNTRY REPORTS AND ASSESSMENTS (2012-2013) (2013), <https://think-asia.org/bitstream/handle/11540/833/asean-corporate-governance-scorecard.pdf?sequence=1>.

⁵⁶ International Monetary Fund, REPORTS ON THE OBSERVANCE OF STANDARDS AND CODES (ROSCS), INTERNATIONAL MONETARY FUND (June 21, 2019), <https://www.imf.org/external/NP/rosc/rosc.aspx>.

TABLE 2 THE CSLA-ACGA CORPORATE GOVERNANCE SCORES PROVIDE
A POSSIBLE BASELINE FOR FUTURE ASSESSMENTS?

Table 2-1 Market category scores

| (%) | Total | CG Rules & Practices | Enforcement | Political & Regulatory | IGAAP | CG Culture |
|-------------------|-------|-------------------------|-------------|---------------------------|-------|---------------|
| 1. = Hong Kong | 68 | 61 | 71 | 69 | 72 | 51 |
| 1. = Singapore | 64 | 63 | 56 | 64 | 85 | 54 |
| 3. Japan | 60 | 48 | 62 | 61 | 72 | 55 |
| 4. = Thailand | 58 | 62 | 51 | 48 | 80 | 50 |
| 4. = Malaysia | 58 | 55 | 47 | 59 | 85 | 43 |
| 6. Taiwan | 56 | 48 | 47 | 63 | 75 | 47 |
| 7. India | 54 | 57 | 46 | 58 | 57 | 51 |
| 8. Korea | 49 | 46 | 46 | 45 | 72 | 34 |
| 9. China | 48 | 42 | 40 | 44 | 67 | 34 |
| 10. = Philippines | 40 | 40 | 18 | 42 | 65 | 33 |
| 10. = Indonesia | 39 | 34 | 24 | 44 | 62 | 32 |

Source: Asian Corporate Governance Association

Table 2-2 China – Show'em the money

| High CG BUYs /Low CG Sells | | |
|----------------------------|--------------|--|
| Company | CG Score (%) | Re-rating drivers |
| High CG BUYs | | |
| Legend | 71.1 | Increasing premium for growth in an uncertain environment for equities. BUY. |
| Brilliant | 69.5 | Exceptional track record of value creation to continue with move into sedans. BUY. |
| CNOOC | 61.3 | Announcements of new discoveries will highlight value relative to global peers. BUY. |
| Low CG SELLS | | |
| Southeast Power | 29.9 | Investments in financial services sector show a lack of management focus. SWITCH to GD Power. |
| China Everbright | 33.0 | Delays to listing of subsidiaries likely to halt the company's value creation efforts. U/PERFORM. |
| Shanghai Industrial | 32.8 | Investments in IT sector unlikely to boost company's poor value creation record in the short term. LT BUY. |
| CITIC Pacific | 45.1 | Ability to create value from telecom infrastructure investments under question. LT BUY. |

Source: CLSA Emerging Markets

Independence from government – and thus administrative law – represents both a vice and virtue. The assessment organisation's need to attract clients represents a clear vice. The CSLA, an investment

advisor, represents one of the Association's large funders. Judging by the ACGA's 2012 report, most of the assessment seems to revolve around general market trends, with one or two companies' cases described as examples.⁵⁷ Discussion of the 14 or so companies the report focused on contained 2-3 sentences, with information seemingly taken from the news.⁵⁸ A quick overview of the report suggests that the sponsoring organisations do not practice favouritism vis-à-vis powerful companies.⁵⁹ Yet, the incentives will always remain to provide assessments and consulting at the same time and to the same companies. Simply putting administrative law constraints on the ACGA's ratings work, if the Association receives government money, would only alter the degree (not the impact) of restrictions placed on the entity.⁶⁰ Sponsorship from a market regulator or market maker could significantly dull CSLA and ACGA's incentives to talk-up potential clients – even if potentially burnishing its credibility.⁶¹

What about regulating such assessment through a regulated body? Could legislation or regulation change the HKEx *Listing Rules* to encourage, or even require, participation in – and aid with – such assessments?⁶² Other institutions do not have the funding, interest in promoting market quality and institutional support that HKEx has.⁶³ The HKEx earned HK\$8 billion in 2015.⁶⁴ As its official website shows, the HKEx also advertises at length its corporate social responsibility. If the HKEx supports the ACGA \$1 million

⁵⁷ CSLA & ACGA, CG WATCH 2012 CORPORATE GOVERNANCE IN ASIA 69-73 (2012), <https://www.acga-asia.org/upload/files/CG%20Watch%202012.pdf>.

⁵⁸ *Id.*, at 75-76.

⁵⁹ *Id.*, at Figure 68 (China: Biggest CG gainers/decliners (alphabetical order)).

⁶⁰ Sang-Cheoul Lee & YunXia Wang, *A Study on the Establishment and Transformations of Chinese Type Quangos*, 10 INT'L REV. PUB. ADMIN. 45, 57 (2005).

⁶¹ Study after study shows that attachment to government (and thus its administrative law) brings a certain amount of public trust and confidence – due to the possibility of democratic control. Gash and Rutter interestingly try to find the principles underlying the optimal level of such independent funding. See Tom Gash & Jill Rutter, *The Quango Conundrum*, 82 THE POL'Y. Q. 95 (2011) (U.K.).

⁶² See HKEx, Main Board Listing Rules (2019), https://en-rules.hkex.com.hk/sites/default/files/net_file_store/new_rulebooks/c/o/consol_mb.pdf.

⁶³ The Financial Services Development Council, research institutions at the local universities, and even the Company Register represent less desirable alternatives. In the case of the first two, they have no sustainable revenue source. In the latter, the conflict of interest obviously exists between register and assessor.

⁶⁴ See HKEX, HKEX 2015 ANNUAL REPORT 37-61 (2016), https://www.hkexgroup.com/-/media/HKEX-Group-Site/ssd/Investor-Relations/Regulatory-Reports/documents/2016/160321ar_e.pdf.

(roughly US\$128,000) annually, such money should be enough to pay for the social goods aspects of its work. HKEx has “community” as a core value, as “help[ing] to build a sustainable community by supporting local initiatives that create effective and lasting benefits to the community.”⁶⁵ The HKEx should not have the right to influence assessments – even if these assessments might influence itself and its members.⁶⁶ Indeed, having an Ordinance on the limits and authorisations allowable under/for such assessments – like the US has – would go a long way toward developing Hong Kong’s own administrative law in this area.⁶⁷ Unlike in other cases where public authorities use independent assessments, the general investing public uses corporate governance assessments – ensuring these assessments’ “fair form and utilisation”. The coverage of these assessments – and whether they would include unlisted as well as listed companies – remains a topic for further discussion.

What good would such assessments do? As we have argued above, having such assessments would help researchers and others look for correlations between corporate governance practices and administrative regulations such as those allowing for the use of offshore entities. Most importantly though, such assessments would help Hong Kong’s and Mainland Chinese companies’ improve their profitability and managerial self-dealing and fraud.⁶⁸ Some authors

⁶⁵ See HKEx, HKEX 2015 CORPORATE SOCIAL RESPONSIBILITY REPORT 24-28 (2016), <https://www.hkexgroup.com/-/media/HKEX-Group-Site/ssd/Investor-Relations/Regulatory-Reports/documents/2016/e160321csr.pdf>.

⁶⁶ Influence represents a fascinating topic when dealing with quasi-independent agencies and entities. The US provides the most convincing proof that using administrative law (and related administrative disputes) provides the best way of deciding where the line between public and private should lie. In such law, the current standard consists of the requirement that independent bodies be fairly “formed and utilized.” In other words, rules should ensure the independence of advisory/assessment group members (the “formed” part of the phrase) and public bodies use their advice (the “utilized” part of the phrase). See Margaret Sova McCabe, *Assessing the Administrative Law Weaponry in the “War on Science”*, YALE J. ON REG.: NOTICE & COMMENT (Oct. 27, 2017), <http://yalejreg.com/nc/assessing-the-administrative-law-weaponry-in-the-war-on-science-by-margaret-sova-mccabe/>.

⁶⁷ Ordinances in Hong Kong represent the city’s own form of legislation. For more on the US’s statute, see Steven P. Croley & William F. Funk, *The Federal Advisory Committee Act and Good Government*, 14 YALE J. ON REG. 451, 558 (1997).

⁶⁸ Summarizing more than a decade of econometric research, Michael and Goo show how adopting corporate governance provisions espoused by the OECD Guidelines has improved Hong Kong listed firms’ equity returns, increase corporate profits (even among unlisted firms) and decrease earnings management, tunnelling and other forms of managerial abuse of company assets/revenues. See Bryane Michael & Say-Hak Goo, *What Does Corporate Governance Regulation in Hong Kong Teach Us About*

may question the OECD's role in promoting corporate governance reform – or influencing administrative law – outside their member states.⁶⁹ Yet, assessments based on the OECD corporate governance guidelines and principles arose exactly because of public corporate governance scandals.⁷⁰ Many authors claim such assessments do not go far enough.⁷¹ Yet, few could doubt the usefulness of such assessments in reducing the kind of fraud and self-dealing exposed by the Panama Papers.

IV. DISCLOSURE-BIASED PRINCIPLES IN ADMINISTRATIVE LAW (AND THUS CORPORATE LAW?)

Why would more disclosure ensure these assessments' "fair form and utilisation"? In theory, the Listing Rules' requirement to publish enough information in corporate governance reports to allow for third-party assessment of corporate governance using the OECD Guidelines would encourage investors' and third party's feedback.⁷² The market for corporate governance information (investors, other stakeholders and regulators) would need to ensure "fair form" (that assessments come from independent, well-rounded, unbiased and probably diverse sources).⁷³ In theory, market incentives ensure

Incremental Legal Change, 38 BUS. L. REV. 89, 100 (2017). For a similar review covering Mainland firms, see also Michael & Goo, *supra* note 16.

⁶⁹ See Mathias Siems & Oscar Alvarez-Macotela, *The G20/OECD Principles of Corporate Governance 2015: A Critical Assessment of Their Operation and Impact*, 4 J. OF BUS. L. 310 (2017) (U.K.).

⁷⁰ Fianna Jesover & Grant Kirkpatrick, *The Revised OECD Principles of Corporate Governance and their Relevance to Non-OECD Countries*, 13 CORP. GOVERNANCE: AN INT'L REV. 107, 138 (2005).

⁷¹ Victor Zitian Chen et al., *Are OECD-Prescribed "Good Corporate Governance Practices" Really Good in an Emerging Economy*, 28 ASIA PAC. J. MGMT. 115, 138 (2011).

⁷² The literature provides too many studies of the regulator's role in encouraging investors to demand more information and/or better corporate governance practices. For a specific, legally-related example focused on the US, see Edward Rock, *Securities Regulation as Lobster Trap: A Credible Commitment Theory of Mandatory Disclosure*, 23 CARDOZO L. REV. 675, 704 (2002). For a general, more environment-based study outside the US, see R.M. Haniffa & T. E. Cooke, *Culture, Corporate Governance and Disclosure in Malaysian Corporations*, 38 ABACUS317 (2002) (Austl.).

* ⁷³ Almost too many corporate governance models and assessments exist to catalogue, from Moody's (a popular bond risk rating agency) to independent academic studies using their own bespoke criteria. No assessment of these assessments yet exists. In other words, we cannot know which assessment "is better." The closest proxy consists of looking at information availability or other corporate governance metrics on the extent to which analysts predict company revenue, profits and other variables accurately. See, e.g., Bhat, Gauri, Ole-Kristian Hope & Tony Kang, *Does Corporate Governance Transparency Affect the Accuracy of Analyst Forecasts?*, 46 ACCT. & FIN. 715, 732 (2006).

“utilisation” by both companies (who react to assessments) and administrative bodies (who would regulate to solve market failures identified by low corporate governance scores).⁷⁴ But what in Hong Kong’s administrative law might encourage disclosure?

One option consists of extending the doctrine of fiduciary trust developed over the decades in the public sector. Under such a doctrine, civil servants represent “public servants” – who should faithfully serve the public.⁷⁵ If civil servants have such a fiduciary duty in areas ranging from public service provision to regulation of the economy, then such a duty obviously also covers their handling of corporate governance regulations.⁷⁶ Siebecker argues that increased disclosure could result from expanding fiduciary obligations on corporate executives.⁷⁷ Such an obligation would bring corporate executives’ duty of care or public trust closer to that expected of a civil servant. Yet, for such a principle to work, such a trust/duty must evolve in the public administration itself, to the point where private sector equivalents might be theorised.⁷⁸ Not everyone believes that such fiduciary duties to inform the public, for example, do or should extend to the private sector.⁷⁹ Yet, if government-

⁷⁴ For Sun and co-authors, the financial crisis represents its own indicator of poor corporate governance – one far more extreme than simple numbers on an assessment. See William Sun et al., *A Systemic Failure of Corporate Governance: Lessons from the On-going Financial Crisis*, EUR. FIN. REV. (Feb. 12, 2012), <https://www.europeanfinancialreview.com/?s=A+Systemic+Failure+of+Corporate+Governance%3A+Lessons+from+the+On-going+Financial+Crisis>.

⁷⁵ We would not look as far back as the Roman Empire – like Natelson does -- for the government employees’ implied or explicit fiduciary duty toward taxpayers. Yet, even modern environmental jurists like Wood seek to extend already existing fiduciary duties to cover administrative law covering policy areas like environmental protection. See Robert G. Natelson, *The Government as Fiduciary: A Practical Demonstration from the Reign of Trajan*, 35 U. RICH. L. REV. 191, 236 (2001). See also Mary Christina Wood, *Advancing the Sovereign Trust of Government to Safeguard the Environment for Present and Future Generations (Part II): Instilling a Fiduciary Obligation in Governance*, 39 ENVTL. L. 91, 140 (2009).

⁷⁶ Indeed, a Canadian court recently upheld such a fiduciary duty, finding that managers (public or private) have a duty to the wider organization – and society in general – not just to a specific group like shareholders. See Edward M. Iacobucci, *Corporate Fiduciary Duties and Prudential Regulation of Financial Institutions*, 16 THEORETICAL INQ. L. 183, 210 (2015).

⁷⁷ See Michael R. Siebecker, *Trust & Transparency: Promoting Efficient Corporate Disclosure through Fiduciary-Based Discourse*, 87 WASH. U. L. REV. 115, 174 (2009).

⁷⁸ Indeed, Criddle places such a trust at the center of any solution to the agency problems affecting the effective exercise of administrative law. See Evan J. Criddle, *Fiduciary Foundations of Administrative Law*, 54 UCLA L. REV. 117, 184 (2006).

⁷⁹ Davis particularly sees an insurmountable wedge between the very basis on which public versus private duties rest. See Seth Davis, *The False Promise of Fiduciary Government*, 89 NOTRE DAME L. REV. 1145, 1208 (2014).

sponsored enterprises represent a middle ground between public and private sectors, then clearly some middle ground must also exist vis-a-vis duties to corporate stakeholders (like the duty to disclose).⁸⁰ If politicians feel the pulse of society's views on rights and duties, then rights and duties in existing administrative law probably serve as the starting point for thinking about the way that corporate duties should evolve.⁸¹

Clearly something prevents these norms from either working in Hong Kong's administrative law or translating into the private sector. Figure 5 shows Hong Kong's own scores for financial transparency (or lack thereof).⁸² As is shown, Hong Kong ranks second worst among the jurisdictions polled for financial transparency. Hong Kong's unwillingness to sign up to several key international tax and anticorruption agreements represents one of the key reasons for Hong Kong's poor rating.⁸³ Hong Kong's large-scale overhaul of its money laundering rules probably makes part of this score too pessimistic. Yet, failing to sign up to key international transparency agreements represents a symptom rather than cause of secrecy. Behaviours typifying good corporate governance, like increased tax payments, become more prevalent as financial disclosures are enhanced.⁸⁴

Hong Kong's lack of a disclosure culture in its corporate governance attitudes underpins most of the reasons for Hong Kong's bad financial secrecy scores.⁸⁵ Enrique and co-authors' idea of letting

⁸⁰ For an attempt to theorise this middle ground, see Charles Cooper et al., *Regulation of GSEs, Administrative Law, and Fiduciary Duties*, 10 N.Y.U. J. L. & BUS. 265, 300 (2014).

⁸¹ As with any argument in this area, critics might argue that business – rather than the government – better reflects citizens' views and preferences. See David L. Ponet et al., *Translating Fiduciary Principles into Public Law: Responding to D. Theodore Rave, Politicians as Fiduciaries*, 126 HARV. L. REV. 91, 101 (2013).

⁸² Tax Justice Network, FINANCIAL SECRECY INDEX - 2015 RESULTS (2016), <https://web.archive.org/web/20170814131725/>.

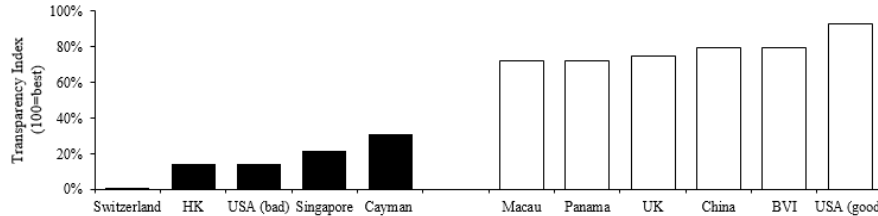
⁸³ Signing on to international transparency commitments represents the 14th out of the 15 key financial secrecy indicators assessed by the Tax Justice Network. For exact scores, see TAX JUSTICE NETWORK, FINANCIAL SECRECY INDEX 2015 METHODOLOGY (2016).

⁸⁴ Sanjay Gupta et al., *The Effect of Mandatory Financial Statement Disclosures of Tax Uncertainty on Tax Reporting and Collections: The Case of FIN 48 and Multistate Tax Avoidance*, 36 J. THE AM. TAX'N ASS'N. 203, 229 (2014).

⁸⁵ Qu and Leung illustrate with data the close connection between Chinese disclosure culture and how Chinese firms conduct corporate governance. As disclosure norms change, so should the governance practices encouraging disclosure. See Wen Qu & Philomena Leung, *Cultural impact on*

each company decide its own optimal disclosure requires some underlying norms best made in the crucible of administrative law and appeal.⁸⁶ Can administrative law help change this?

FIGURE 5 HONG KONG IS SEVEN TIMES WORSE THAN PANAMA FOR FINANCIAL SECRECY



The figure shows the Tax Justice Network's Financial Secrecy Index for 2015. We reversed the values (such that Switzerland's highest value for secrecy of 1466 because the lowest value for transparency and visa-versa). Many have critiqued the index as unreflective of large financial centres (clearly as BVI and the USA score at the upper end of the index). Yet, Hong Kong's rank as the second worst jurisdiction for financial secrecy raises concerns. The index combines 15 scores of objective indicators. See source for methodology.

Source: Tax Justice Network (2016).

If directly writing rules and imposing them on companies won't work, what can lawmakers in a place like Hong Kong do? Hong Kong businesses and business schools can make the changes their UK and US peers have already made to introduce transparency into management perspectives. The US adjusted, with its usual wave of management gurus and fads, and extolled the virtues of transparency.⁸⁷ Consultants like PwC have already profited from

Chinese Corporate Disclosure-A Corporate Governance Perspective, 21 *MANAGERIAL AUDITING J.* 241 (2006) (Austl.).

⁸⁶ In other words, companies cannot decide on these norms atomistically (for themselves) without a wider culture and shared understanding of rules decided during administrative and other disputes. See Luca Enriques et al., *Mandatory and Contract-Based Shareholding Disclosure*, 15 *UNIF. L. REV.* 713, 742 (2010).

⁸⁷ Transparency cheerleading took place from the self-help management books to the panegyrics in Forbes and the other mainstream business media. See DON TAPSCOTT & DAVID TICOLL, *THE NAKED CORPORATION: HOW THE AGE OF TRANSPARENCY WILL REVOLUTIONIZE BUSINESS*, (3rd ed. 2003). See also Julia Kirby, *Trust in the Age of Transparency*, *HARV. BUS. REV.* (July, 2012), <https://hbr.org/2012/07/trust-in-the-age-of-transparency>. See also Neil Patel, *Why a Transparent Culture Is Good for Business*, *FAST COMPANY* (Oct. 09, 2014), <https://www.fastcompany.com/3036794/why-a-transparent-culture-is-good-for-business>. See also Alex Knapp, *In the Era of Transparency, Trust Is the Key to Success*, *FORBES* (Nov. 16, 2012), <https://www.forbes.com/sites/alexknapp/2012/11/16/in-the-era-of-transparency-trust-is-the-key-to-success/#24e0da2b19ba>.

turning the transparency fad into sellable services.⁸⁸ The UK has followed its consensual model – of having government coordinate the transparency effort.⁸⁹ Given the importance of business groupings in Hong Kong, a pan-sectoral body like the Hong Kong Trade Development Council can/should cheerlead corporate transparency. Such cheerleading may include educating businesses about the benefits of transparency and disclosure. Such work may also consist of making industry standards and norms encouraging transparency according to each sector’s own particularities. Most important, the relevant body can help reverse the presumption in most corporations that information should be concealed unless explicitly authorised to be publicly disseminated.⁹⁰

Stakeholders in the corporate ecosystem should prefer transparency because better decisions come from fully disclosed information.⁹¹ Authors like Dallas have noted that lack of transparency distorted corporate governance to such a degree as to contribute to the financial crisis of 2007-2008.⁹² Against this background, corporate governance rules have increasingly moved away from requiring transparency for specific activities and toward a general “presumption of transparency” (that the company shall report

⁸⁸ *Strengthen Trust and Transparency: Enhance Trust Across Your Network*, PWC, 2016, <https://www.pwc.com/gx/en/about/analyst-relations/strengthen-trust-and-transparency.html>.

⁸⁹ DEPARTMENT FOR BUSINESS INNOVATION AND SKILLS, *TRANSPARENCY & TRUST: ENHANCING THE TRANSPARENCY OF UK COMPANY OWNERSHIP AND INCREASING TRUST IN UK BUSINESS*, Apr. 2014, BIS/14/672, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/304297/bis-14-672-transparency-and-trust-consultation-response.pdf.

⁹⁰ Such a concept will not develop quickly. Even as late as 2014, the Hong Kong Institute of Certified Public Accountants was admonishing accountants and advisors to comply with even the minimums set by the Hong Kong corporate governance code. A new paradigm of openness seems light years away from their button-up analysis. See HONG KONG INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS (HKICPA), *A GUIDE ON BETTER CORPORATE GOVERNANCE DISCLOSURE 4-14* (2013), https://www.hkicpa.org.hk/-/media/HKICPA-Website/HKICPA/%20section5_membership/Professional-Representation/corporate-governance/CG-Guide_Full-version.pdf?la=en&hash=DF9E9136E64D0EC37C853E5F5CAF2DE2.

⁹¹ In theory, no information can be complete and perfect (as an economist would understand it). For an analysis of the incentives which drive information and corporate governance, see Bushman et al., *Transparency, Financial Accounting Information, and Corporate Governance*, 9 *ECON. POL'Y REV.* 65, 87 (2003).

⁹² While most scholars agree about the lack of transparency in securitization, most still do not agree on the extent to which opacity contributed to the crisis. Dallas might argue that lack of information leads to short-termism, as constrained information makes guessing about consequences more difficult. For a comprehensive analysis, see Dallas & Lynne, *Short-Termism, the Financial Crisis, and Corporate Governance*, 37 *J. CORP. L.* 265, 364 (2011).

and disclose as a default option unless such disclosures cause harm).⁹³

Should a “reversed presumption of transparency/disclosure” consist of a right to information? If such a right has made wide inroads in the public administration, corporate interest groups and bodies like The Hong Kong Trade Development Council (or other suitable body) could endorse the right to information as a core value in companies’ mission statements.⁹⁴ In the specific area of working conditions and information affecting consumers, many see business associations’ encouraging their companies to follow international laws, which their own countries have not yet adopted, as a way forward.⁹⁵ To that end, these business associations directly advocate for increased transparency, or fund studies arguing for such transparency.⁹⁶ Even a submission to the EU Parliament recognises that the best way to influence such disclosure consists of using business associations to spread norms which are quickly developing in these countries’ own administrative law.⁹⁷ Reversing the presumption of confidentiality means agents of a business would consider all the information they produce or receive as publicly disclosable, unless labelled confidential – except in cases like accounting firms or law firms, where the business has no rights over the information “lent” to it to do client work.⁹⁸ The needs for privacy differ between companies and individuals – with companies

⁹³ Such a presumption fits in with the corporate governance-as-relationship view that the 2014 UK Code of Corporate Governance adopts. See FINANCIAL REPORTING COUNCIL (FRC), THE UK CORPORATE GOVERNANCE CODE, 2014, <https://www.frc.org.uk/getattachment/59a5171d-4163-4fb2-9e9d-daeafd7153b5/UK-Corporate-Governance-Code-2014.pdf>.

⁹⁴ For such a strategy, and a discussion of this right’s progress in government, see Helen Darbshire, *Proactive Transparency: The Future of the Right to Information? A Review of Standards, Challenges, and Opportunities* 1-16 (WBI & CommGAP, Working Paper 56598, 2010), <http://documents.shihang.org/curated/zh/100521468339595607/pdf/565980WPOBox351roactiveTransparency.pdf>.

⁹⁵ Eva Kocher et al., *No Accountability without Transparency: Legal Instruments for Corporate Duties to Disclose Working and Employment Conditions*, FRIEDRICH EBERT STIFTUNG STUDY 1-6 (June, 2012), <http://library.fes.de/pdf-files/iez/09206.pdf>.

⁹⁶ See Maya Forstater, *Beneficial openness? Weighing the Costs and Benefits of Financial Transparency* 9-17 (Research Council of Nor., CMI Working Paper No. 3, 2017), <https://www.cmi.no/publications/file/6201-beneficial-openness.pdf>.

⁹⁷ See ROBERT SCHUMAN CENTRE FOR ADVANCED STUDIES, OPENNESS, TRANSPARENCY AND THE RIGHT OF ACCESS TO DOCUMENTS IN THE EU (2016).

⁹⁸ “Legal origins” (namely the type of law used in a jurisdiction) significantly determines a jurisdiction’s attitudes to such disclosure. See Ole-Kristian Hope, *Firm-level Disclosures and the Relative Roles of Culture and Legal Origin*, 14 J. INT’L FIN. MGMT. & ACCT. 218, 248 (2003).

using such privacy for commercial advantage (or to protect the privacy of its agents).⁹⁹ Such norms may (and should) encourage company agents to disclose the information which does not help a company's competitive position, or information where the benefits of the public's right exceeds the costs to the company.¹⁰⁰ Just as administrative law has been evolving to deal with the benefits of the "collective processing" of increasingly complex information, so should the rules governing corporate disclosure.¹⁰¹ If all companies agree to release information, no one company will find itself disadvantaged.¹⁰² At the very least, such a presumption of transparency will help reduce the extent of insider trading and other ills which bedevil Hong Kong's exchanges.¹⁰³

Rulemaking by Hong Kong's Securities and Futures Commission (hereinafter referred to as "SFC") could promote such a change in administrative law toward stimulating a presumption-of-transparency culture. First, the SFC could adopt the spirit of the International Organization of Securities Commissions (hereinafter referred to as "IOSCO") principles, perhaps by issuing related broad guidelines.¹⁰⁴ While these principles deal with cross-border securities sales, they lay an important foundation for a general change in administrative jurisprudence, if adopted in Hong Kong's principles-based regulation.¹⁰⁵ One can read and adopt the standards mechanically,

⁹⁹ For an excellent primer on such privacy, see DAVID SOLOVE, *UNDERSTANDING PRIVACY* 32-71 (Harvard Univ. Press 2008).

¹⁰⁰ Such norms cannot conflict with established business and legal principles (namely the "business system"). Yet, these principles are not set in stone, and may change with intervention. See Carla CJM Millar et al., *Corporate Governance and Institutional Transparency in Emerging Markets*, 59 J. OF BUS. ETHICS 163, 174 (2005).

¹⁰¹ Wendy E. Wagner, *Administrative Law, Filter Failure, and Information Capture*, 59 DUKE L.J. 1321, 1432 (2010).

¹⁰² This is a fluid and quickly changing part of the law in developed economies. Steinman, for example, provides a fascinating glimpse into a recent US case involving the issues of disclosure and harm. A digression about the role of regulatorily mandated disclosure, the estimation of harms from non or incorrect disclosure, and judicial remedies would take us too far off topic. See Joan Steinman, *Spokeo, Where Shalt Thou Stand*, 68 VAND. L. REV. EN BANC 243, 256 (2015).

¹⁰³ Such a presumption would reduce the headaches associated with complying with the new disclosure-of-inside-information rules. For a discussion of those rules and the judgment calls involved, see *Disclosure of Inside Information – An Update*, CSJ (June 7, 2015), <http://csj.hkics.org.hk/site/2015/06/07/disclosure-of-inside-information-an-update/>.

¹⁰⁴ *International Disclosure Standards for Cross-Border Offerings and Initial Listings by Foreign Issuers*, FSB (Sept. 01, 1998), https://www.fsb.org/1998/09/cos_980901e/ (last visited June 12, 2019).

¹⁰⁵ As the SFC adroitly notes, "To address the fast-changing market circumstances and practices, the Commission believes that, generally speaking, principles-based regulation that focuses on a higher-level

without thinking about the deep, underlying reasons for these standards.¹⁰⁶ Yet, even once financial institutions and listed companies adopt those principles, analysts like Lu would have reforms of both the International Disclosure Standards and the IOSCO itself, as well as the IOSCO's conduct of a "corporate governance impact assessment."¹⁰⁷ Second, the SFC can continue implementing the Financial Stability Board's and G20's recommendations on disclosure.¹⁰⁸ Hong Kong's authorities have noted numerous "planned steps" in their disclosure action plan. "Industry consultation" and "monitoring international developments" should focus on the final users of information, instead of just pushing disclosure for disclosure's sake.

Other rulemakings by the SFC could help change the direction of administrative jurisprudence (and thus the way business regulates itself). In line with its mandate to monitor firms' compliance with rules, including disclosure-related ones, the SFC could more actively assess and critique publicly-deficient disclosure practices.¹⁰⁹ Private markets and civil society have no incentive or resources to do such monitoring.¹¹⁰ Public censure also matches the objective of encouraging more transparency/disclosure – something in the regulator's own interest. Indeed, the SFC's disclosure team could advise the users, as well as the producers, of disclosable information. At present, the team answers questions from Hong Kong listed companies about what information they need to give out publicly. Yet, the users of such information far exceed the producers of such

articulation of what the Commission expects intermediaries to do is more appropriate than a large volume of detailed standards." See SFC, REGULATORY FRAMEWORK FOR INTERMEDIARIES 7 (June, 2011), <https://www.sfc.hk/web/doc/EN/aboutsfc/Regulatoryframework.pdf>.

¹⁰⁶ For example, standard IV.A.1 relates to collecting the "name, business experience, functions and areas of experience in the company." Such information clearly aids investors and analysts quickly understand the company. As such, the company should place the information in a prominent place with these readers/users in mind. See *Id.*

¹⁰⁷ Bingbin Lu, *International Harmonization of Disclosure Rules for Cross-Border Securities Offerings: A Chinese Perspective*, 1 CORP. GOVERNANCE L. REV. 245, 304 (2005).

¹⁰⁸ See *FSB- G20 Monitoring Progress - Hong Kong*, FSB (Nov. 04, 2011), https://www.fsb.org/wp-content/uploads/r_111104h.pdf?page_moved=1.

¹⁰⁹ Naturally, such law should respect the usual principles by which persons affected could appeal any administrative decision – such as fairness, proportionality, reasonableness and so forth. See Konstantin Davydov, *Judicial Control over Discretionary Administrative Acts: The European Experience*, 5 THE TOPICAL ISSUES PUB. L. 3, 17 (2014).

¹¹⁰ A point Pargendler makes adroitly. See Mariana Pargendler, *The Corporate Governance Obsession*, 42 J. CORP. L. 359, 402 (2016).

information.¹¹¹ Their small and scattered nature reduces the incentives of any one information user from militating for more disclosure. By offering a resource (such monitoring) to information users, the SFC could lower the costs of increasing disclosure/transparency. The SFC would also receive vital feedback from the market about where informational bottlenecks exist.¹¹² These rules validate Licht's decades old call to end the distinction between public and private law in regulating corporate governance and disclosure – they are two sides of the same coin.¹¹³

V. USING ADMINISTRATIVE LAW AS A LEVER FOR SELF-REGULATING BODIES

Nothing requires Hong Kong's professional services firms to move toward a risk-based approach toward choosing clients. Under such a system, these service providers would try to detect high-risk clients with poor corporate governance practices. Nothing in the Solicitor's Practice Ordinance requires solicitors to look at clients' risks (or any kind of risks affecting the practice).¹¹⁴ Hong Kong should follow the US's "gatekeeper" approach to introducing risk-based assessment and risk management into the legal and other service professions.¹¹⁵ The UK's Solicitors Regulatory Authority and the UK Law Society have best "mainstreamed" such a risk-based

¹¹¹ Indeed, one of the main reasons for the existence of a regulator like the SFC stems from its ability to overcome collective action problems by requiring corporate disclosures which no one person or group has sufficient interest and/or resources to try and bargain for themselves. See Faith Stevelman Kahn, *Transparency and Accountability: Rethinking Corporate Fiduciary Law's Relevance to Corporate Disclosure*, 34 GA. L. REV. 505, 528 (2000).

¹¹² Naturally, the SFC does not work in a vacuum – and its work would motivate other institutions to engage in oversight. For a discussion of the UK experience, see Kathryn Cearn & Eilis Ferran, *Non-Enforcement-Led Public Oversight of Financial and Corporate Governance Disclosures and of Auditors*, 8 J. CORP. L. STUD. 191, 224 (2008).

¹¹³ Amir N. Licht, *International Diversity in Securities Regulation: Roadblocks on the Way to Convergence*, 20 CARDOZO L. REV. 227, 286 (1998).

¹¹⁴ Specifically Rule 2 on general conduct does not mention the need of solicitors to identify or manage risks. See Solicitor Practice Rules, (1997) Cap. 159H (H.K.) (BLIS). (The rule has been updated several times subsequently).

¹¹⁵ Shephard describes in great length all the various documents and initiatives created as a way to encourage lawyers to adopt the risk-based approach to money laundering and corporate malfeasance which is quickly becoming the norm in the services. See Kevin Shepherd, *The Gatekeeper Initiative and the Risk-Based Approach to Client Due Diligence: The Imperative for Voluntary Good Practices Guidance for U.S. Lawyers*, 2010 J. THE PROF. LAW. 83, 142 (2010).

approach into its legal services industry.¹¹⁶ Moreover, the Authority issued new rules as part of its Handbook to move toward the wider adoption of principles-based, outcomes-based regulation.¹¹⁷ Similarly, nothing in Hong Kong's Professional Accountants Ordinance encourages the Hong Kong Society of Accountants or the Hong Kong Institute of Certified Public Accountants to adopt a risk-based approach as a means to accomplish one of its primary tasks as to "discourage dishonourable conduct and practices by certified public accountants."¹¹⁸ Even in the Companies Ordinance, nothing requires boards to set up risk committees or manage risks like staff complicity in money laundering or other financial crime.¹¹⁹ While the Hong Kong Institute of Chartered Secretaries imposes risk-based guidelines on its members, the Institute makes no mention of internal rules about its own risk management practices (if any).¹²⁰

The easiest way to encourage a risk-based assessment of clients and their engagements (work) would be requiring Hong Kong's law firms, accounting firms and corporate services firms to set up risk committees and a risk register – as well as adopt a risk-based approach to compliance.¹²¹ Specifically, lawmakers could eventually adjust Hong Kong's laws to reflect the obligation/right of professional services firms and company boards to adopt a risk-management perspective as way of dealing with compliance and risk – as well as scrutinize high-risk clients by extra monitoring. Institutions like the OECD have already taken on-board most academics' view that risk assessment represents the best way to

¹¹⁶ The Authority has produced a number of clearly written, easily found reference materials describing the use of such a risk-based approach. See *SRA Risk Framework*, SOLIC. REG. AUTHORITY (Mar. 21, 2014), <https://www.sra.org.uk/risk/risk-framework.page>. See also *The Risk-Based Approach – What Is It?*, L. SOCIETY (Sept. 10, 2008), <https://www.lawsociety.org.uk/support-services/advice/article/s/what-is-risk-based-approach/>.

¹¹⁷ Professional Services Group Risk Registers – A Practical Approach for Solicitors, AON RISK SOLUTIONS (2013), <https://www.aon.com/unitedkingdom/products-and-services/industry-expertise/attachments/global-professions/risk-register-practical-approach-white-paper.pdf>.

¹¹⁸ See Professional Accountants Ordinance, (2004) Cap. 50, § 7(h) (H.K.) (BLIS).

¹¹⁹ The only related requirement concerns directors' disclosure of risks in their report. See Companies Ordinance, (2014) Cap. 622, S5-2, Schedule 5, § 1(b) (H.K.) (BLIS).

¹²⁰ See *About Us*, HKICS (2016), https://www.hkics.org.hk/index.php?_room=4.

¹²¹ Recent analyses of the global financial crisis of 2007-8 have particularly stressed the need to introduce broader risk management principles into company law and the sectoral rules governing the financial sector. See WILLIAM SUN et al., CORPORATE GOVERNANCE AND THE GLOBAL FINANCIAL CRISIS: INTERNATIONAL PERSPECTIVES (Cambridge Univ. Press 2011).

balance rules-based and principles-based corporate governance regulations.¹²² Unlike at present, such an approach would cover more than just money laundering.¹²³ Such an approach would reduce the need for extensive and detailed regulations as well as costly compliance systems – thus saving listed firms and others money.¹²⁴ Such an approach would also probably encourage compliance with corporate governance and other regulations.¹²⁵ Yet, such an approach would need to start in administrative law – as civil servants and other administrators administer these requirements.¹²⁶

Yet, the way we analyse the Panama Papers and other scandals determines the way we think about designing the administrative law needed to tackle the problems these scandals highlight. Most analysts wrongly focus on legality of the structures and rules used by Mossack Fonseca and others to create and use offshore corporations – rather than the harms they cause.¹²⁷ They also wrongly focus on the narrow, specific harms of establishing offshore companies – in avoiding taxes for example.¹²⁸ The inability of lawmakers to change the domestic legislation that allows intermediaries to set up offshore

¹²² See OECD, RISK MANAGEMENT AND CORPORATE GOVERNANCE, CORPORATE GOVERNANCE (2014), <http://www.oecd.org/daf/ca/risk-management-corporate-governance.pdf>.

¹²³ In contrast to the UK or US, most of our searches on risk-based approaches in Hong Kong yielded results only for banks and financial service firms and/or only for money laundering risks. See SFC, Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering/Counter-Financing of Terrorism, Updated AML/CFT Self-Assessment Checklist, Apr. 16, 2019, <https://www.sfc.hk/edistributionWeb/gateway/EN/circular/aml/doc?refNo=19EC24>.

¹²⁴ The cost savings represent one of the key reasons for most professions (especially banking) to advocate such risk-based approaches. For a fuller description, see Christine L. Ford, *New Governance, Compliance, and Principles-Based Securities Regulation*, 45 AM. BUS. L.J. 1 (2008).

¹²⁵ We have already shown evidence that firms fail to comply with corporate governance and money laundering regulations because of their cost and complexity. Such a results-based, risk-oriented focus might thus lower costs and encourage compliance. See Jackie Harvey, *Compliance and reporting issues arising for financial institutions from money laundering regulations: a preliminary cost benefit study*, 7 J. MONEY LAUNDERING CONTROL 333 (2004).

¹²⁶ Such administrative law has become increasingly complex everywhere. For a fascinating discussion of how legislation – and related administrative rulemaking – has affected the professions in the US, see Larry Cata Backer, *The Sarbanes-Oxley Act: Federalizing Norms for Officer, Lawyer and Accountant Behavior*, 76 ST. JOHN'S L. REV. 897, 952 (2002).

¹²⁷ See Brooke Harrington, *Panama Papers: The Real Scandal Is What's Legal*, THE ATLANTIC (Apr. 6, 2016), https://works.bepress.com/brooke_harrington/39/.

¹²⁸ The Guardian represents one of the countless media outlets portraying the Panama Papers Scandal in a sombre light because of the negative effects these offshore entities had on tax collection. See Juliette Garside, *Fund Run by David Cameron's Father Avoided Paying Tax in Britain*, THE GUARDIAN (Apr. 4, 2016), <https://www.theguardian.com/news/2016/apr/04/panama-papers-david-cameron-father-tax-bahamas>.

entities results from the wrong conclusions used by critics of these rules.¹²⁹ As we already showed, the real harm resulting from the rules stemmed from the opacity which gave rise to no corporate governance of the offshore entities themselves and the poor corporate governance of companies associated with them. As the journalists who brought the Panama Papers to light noted, “the offshore system relies on a sprawling global industry of bankers, lawyers, accountants and these go-betweens who work together to protect their clients’ secrets. These secrecy experts use anonymous companies, trusts and other paper entities to create complex structures that can be used to disguise the origins of dirty money.”¹³⁰

Regulatory amendments should thus focus on the corporate governance consequences of intermediaries’ setting up offshore structures – and not on ethics or rule-following.¹³¹ Indeed, in the more flexible US legal environment, focusing on these consequences led to the creation of anti-avoidance doctrines – which review the intent behind the behaviour against circumvent rules for tax gain.¹³² What role will intermediaries play in setting up and operating offshore companies when tax authorities around the world adopt “place of effective management” (or a similar test) when deciding on regulation and taxation?¹³³ The academic literature seems to show that, in the longer run, legal doctrines emerge – and lawmakers tend to ban these practices – exactly because of scandals like the Panama Papers imbroglio.¹³⁴ Yet, codifying new laws and regulations (by trying to break-up these kinds of doctrines into specific admonitions

¹²⁹ Many administrative scholars have noted the extent of this problem – namely looking to add more procedures rather than looking at how rules address underlying mischief (problems). See Javier Barnes, *Towards a Third Generation of Administrative Procedures*, in *COMPARATIVE ADMINISTRATIVE LAW* (Peter Lindseth & Susan Rose-Ackerman eds., 2010).

¹³⁰ *Giant Leak of Offshore Financial Records Exposes Global Array of Crime and Corruption*, INT’L CONSORTIUM OF INVESTIGATIVE JOURNALISTS (Apr. 3, 2016), <https://www.icij.org/investigations/panama-papers/20160403-panama-papers-global>.

¹³¹ Such a focus reflects a broader push in the social sciences to judge law by its systemic consequences rather than by normative criteria. For an excellent review, see David Scheffer, *The Ethical Imperative of Curbing Corporate Tax Avoidance*, 27 *ETHICS & INT’L AFF.* 361, 369 (2013).

¹³² Development of an anti-avoidance doctrine in law. See Jasmine Fisher, *Fairer Shores: Tax Havens, Tax Avoidance, and Corporate Social Responsibility*, 94 *B.U. L. REV.* 337, 365 (2014).

¹³³ See Tracy Gutuza, *Has Recent United Kingdom Case Law Affected the Interplay between Place of Effective Management and Controlled Foreign Companies*, 24 *SOUTH AFR. MERCANTILE L. J.* 424, 437 (2012).

¹³⁴ For an unusually lucid (even if somewhat dated) account, see Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 *YALE L. J.* 1521, 1612 (2005).

to civil servants and others) adds to complexity – and thus confusion. Even as early as 2001, the US and others’ experience has shown that principles-based regulation represents the best way to apply these doctrines.¹³⁵

How can the presumption of disclosure/transparency enter Hong Kong’s administrative – and thus general – law? In line with the presumption of transparency, Hong Kong’s professional bodies and associations (like the Law Society, the Hong Kong Institute of Certified Public Accountants and the Hong Kong Institute of Chartered Secretaries) could encourage transparency – rather than confidentiality – as a corporate governance “default position.”¹³⁶ Rules for the professions should encourage these professions to provide advice which enhances – rather than hinders – transparency. The Mossack Fonseca case threw the transparency of professional service firms themselves into the spotlight – as just another case of “gatekeeper failure.”¹³⁷ Government regulators should not discourage professional services firms – through these associations or directly – from offering advice on tax or regulatory avoidance – as self-interest will always drive companies to hire advisors.¹³⁸ Instead, we note better governed firms – including professional services firms – engage in less avoidance, using loopholes and skirting the law.¹³⁹ Thus, as professional associations and bodies (or “gatekeepers” as

¹³⁵ See Lawrence Zelenak, *Codifying Anti-Avoidance Doctrines and Controlling Corporate Tax Shelters*, 54 SOUTHERN METHODIST U. L. REV. 177, 194 (2001). The organic development of new administrative law principles need not follow the US experience of overly trying to systematize such change. See Gillian Metzger & Kevin Stack, *Internal Administrative Law*, 115 MICH. L. REV. 1239, 1309 (2017).

¹³⁶ Such transparency clearly represents a social good – as such transparency helps all professional service providers, even if such transparency temporary puts one at a competitive disadvantage. For evidence, see Marion Brivot, *Controls of Knowledge Production, Sharing and Use in Bureaucratized Professional Service Firms*, 32 ORG. STUD. 489, 508 (2011).

¹³⁷ Stopping the cycles of such failure will require structural changes in the way these gatekeeping professional services firms share information. See John Coffee, *Understanding Enron: “It’s About the Gatekeepers, Stupid”*, 57 THE BUS. L. 1403, 1420 (2002).

¹³⁸ Indeed, these advisors should encourage better corporate governance – given repeated findings that better corporate governance constitutes an excellent tax avoidance scheme. See Dirk Kiesewetter & Johannes Manthey, *The Relationship between Corporate Governance and Tax Avoidance – Evidence from Germany using a Regression Discontinuity Design*, 218 ARQUS QUANT. RES. IN TAX’N DISCUSSION PAPER 1, 18 (2017).

¹³⁹ For more proof, see Jon Kerr, Richard Price & Francisco Roman, *The Effect of Corporate Governance on Tax Avoidance: Evidence from Governance Reform* (Apr. 22, 2016) (unpublished manuscript) (on file with author), <https://www.ntanet.org/wp-content/uploads/proceedings/2016/184-kerr-price-roman-effect-corporate-paper.pdf>.

American scholars call them) encourage transparency and good corporate governance, such work will discourage the kind of activities which represent reputation risks for intermediaries and their clients.¹⁴⁰ Administrative rules should make Hong Kong's civil servants expect such disclosure/transparency – adding to such a presumption of transparency.¹⁴¹ Principles-based regulation represents a key way to shape civil servants' expectations for transparency as well as other conduct like companies' acting based on legitimate economic purposes.¹⁴²

VI. HOW FAR CAN THE REGULATORY TEST FOR LEGITIMATE ECONOMIC PURPOSES GO?

The legitimate economic purpose test represents one of the clearest, and most commonly known, principles by which administrative law defines the tax reporting obligations of firms.¹⁴³ While the test itself does not comprise administrative law, the way that civil servants interact with the test does.¹⁴⁴ The Hong Kong tax code requires tax assessors to consider “the form and substance of the transaction” (much like the Mainland rules) and the intent (whether for reasonable commercial purposes or simply to obtain a tax benefit).¹⁴⁵ While Hong Kong's tax code has not adopted the

¹⁴⁰ Kevin Shepherd, *Guardians at The Gate: The Gatekeeper Initiative and the Risk-Based Approach for Transactional Lawyers*, 43 REAL PROP. TRUST & EST. L. J.607, 671 (2009).

¹⁴¹ “Hong Kong's own administrative rules right now governing such transparency hardly represent a paragon for others to follow...providing yet one more reason why administrative law reform must come first.” For the difficulties in adopting these kinds of rules, see Adrian Sawyer, *Hong Kong's Involvement With International Tax Reform: What's the “BEPS”?*, 25 ASIA PAC. L. REV. 170, 189 (2017).

¹⁴² See, e.g., Donald Kettl, *The Transformation of Governance: Globalization, Devolution, and the Role of Government*, 60 PUB. ADMIN. REV. 82, 86 (2000).

¹⁴³ If administrative law represents the unloved cousin of public law, then tax law represents the unloved child of that administrative law. For even an acknowledgement that tax issues comprise a practically, as well as academically, interesting part of administrative law, see Amandeep Grewal, *Taking Administrative Law to Tax*, 63 DUKE L.J. 1625, 1633 (2014).

¹⁴⁴ The problem runs deeper than what most realize. The application of this test – or indeed any legal test – butts up against the slippery nature of the transnational corporation (as a shell company or otherwise). The practical impossibility of applying Hong Kong law to such a transnational entity makes rulemaking precarious at best – much less rules about applying such rulemaking. For a questioning of the legal foundations of such an administrative law, see Fleur Johns, *The Invisibility of the Transnational Corporation: An Analysis of International Law and Legal Theory*, 19 MELBOURNE U. L. REV. 893, 923 (1994).

¹⁴⁵ See Inland Revenue Ordinance, (1989) Cap. 112, § 61A (H.K.) (BLIS). The rule does not require or define the principles of a legitimate commercial purpose test like the one we describe in this article.

reasonable commercial purpose language, its “dominant purpose” test basically serves the same purpose.¹⁴⁶ As shown in Table 3, Yang provides a fascinating account of the way the “reasonable commercial purposes” test evolved in Hong Kong and on the Mainland.¹⁴⁷ On the Mainland, the tax authorities over time expanded their application of the test. In contrast, the principle in Hong Kong bifurcated into seven sub-tests and Hong Kong’s courts weakened the provision by ruling against the tax authorities on numerous occasions. Despite Hong Kong’s hostility to applying a “reasonable commercial purposes test,” the principle is not foreign to Hong Kong law and practice.

TABLE 3 THE DIFFERENT TRAJECTORIES OF ECONOMIC PURPOSE TESTS IN HONG KONG AND ON THE MAINLAND

| Mainland | Hong Kong |
|---|--|
| The reasonable commercial purpose principle evolved ever-more reaching from 2008’s article 120 of the tax rules to the 2015 tax Bulletin 7. | Started with a complex 7-part test for allowing an offshore transaction, with cases like Ngai Lik Electronics significantly weakening the principle in practice. |

Source: interpreted/summarized from Yang.

The introduction of a legitimate economic purpose test into Hong Kong’s administrative law would help pave the way for principles-based approaches. Specifically, lawmakers and regulators could introduce the test into Hong Kong’s tax code, listing rules and in financial service providers/intermediaries’ risk profiles. Section 61 of the Inland Revenue Ordinance allows the tax authorities to assess extra taxes for “any transaction which reduces or would reduce the amount of tax payable by any person [if] artificial or fictitious.”¹⁴⁸

We thus interpret the converse of structuring a transaction or party to obtain a tax benefit as a legitimate commercial purpose.

¹⁴⁶ Inland Revenue Department Hong Kong, Departmental Interpretation and Practice Notes, (2006) No. 15, at 33, https://www.ird.gov.hk/eng/pdf/e_dipn15.pdf.

* ¹⁴⁷ Yating Yang, *China (People’s Rep.)/Hong Kong: A Comparative Study of the General Anti-Avoidance Rules of Mainland China and Hong Kong – Legislation, Interpretation and Application*, IBFD (2016), https://www.ibfd.org/IBFD-Products/Journal-Articles/Bulletin-for-International-Taxation/collections/bit/html/bit_2016_07_cn_1.html.

¹⁴⁸ Inland Revenue Ordinance, (2012) Cap. 112, § 61 (H.K.) (BLIS).

The three sub-articles basically apply a legitimate economic purpose test by targeting “transactions designed to avoid liability for tax” (article 61a), “utilization of losses to avoid tax” (section 61b) and “avoidance arrangement of no effect” (section 61c).¹⁴⁹ Making such a legitimate economic purpose test more explicit in those articles would help ensure that businesses understand the logic behind the prohibitions contained in those articles. Civil servants would also adopt the habit of evaluating the ends of government action – rather than means. Similarly, any intermediary transaction with a company whose structure obviously lacks a legitimate economic purpose (like a manufacturer or service provider incorporated in the Bahamas) should clearly represent a higher commercial risk.¹⁵⁰ The Hong Kong Stock Exchange’s listing rules could furthermore require a local incorporation or incorporation in the jurisdiction where the listed company makes and/or sells its goods and services.¹⁵¹ The goal involves introducing the broader method of regulating by principles – rather than simply confining the use of such regulations to particular situations.¹⁵²

Hong Kong’s comply-or-explain culture of corporate governance – basically a principles-based test – shows Hong Kong regulators’ experience in imposing these kinds of regulations on companies. Such a culture requires firms to comply with the corporate governance rules, or explain why they have not complied with

¹⁴⁹ *Id.*

¹⁵⁰ Many experts have documented the risks of transacting with offshore entities – in the lack of recourse to certain laws (like bankruptcy law) and anonymity which stifles accountability. See GLOBAL FINANCIAL INTEGRITY, CHANCING IT: HOW SECRET COMPANY OWNERSHIP IS A RISK TO INVESTORS (2016), <https://gfintegrity.org/report/chancing-it-how-secret-company-ownership-is-a-risk-to-investors/>.

¹⁵¹ Even if the exchange and companies do not completely adhere to the rule, at least the jurisdictions of incorporation will show more variation than at present (as shown in Figure 59). For a look at the US’s offshore-incorporated listed firms, see The U.S. Securities and Exchange Commission, *Foreign Companies Registered and Reporting with the U.S. Securities and Exchange Commission*, 2014, <https://www.sec.gov/divisions/corpfin/international/foreigngeographic2014.pdf>.

¹⁵² Lawmakers and senior public officials themselves should not (and probably cannot) use such a results-based approach, for use when traditional administrative law does not work. A paradigm change is a paradigm change. For a proposal for such silo-ing, see Robin K Craig et al., *A Proposal for Amending Administrative Law to Facilitate Adaptive Management*, 12 ENVIRONMENT RESEARCH LETTER (July 10, 2017), <https://iopscience.iop.org/article/10.1088/1748-9326/aa7037/pdf>. For a more developed expression of this, see Robin Craig & J. Ruhl, *Designing Administrative Law for Adaptive Management*, 67 VAND. L. REV. 1, 87 (2014).

them.¹⁵³ Unlike minimalist regulations, comply-or-explain regulations strive to provide the flexibility to react appropriately to market circumstances, while still following guidelines for good corporate governance – basically the same kind of goal as a legitimate economic purpose test (or any other test).¹⁵⁴ Following such an approach, businessmen actually help civil servants understand and apply regulation, in a way that minimally intrudes on the company.¹⁵⁵

In theory, comply or explain rules can support a legitimate economic purposes test. As we have shown, complex and opaque offshore structures harm shareholder value and allow poor corporate governance practices to abound.¹⁵⁶ If such offshore structures actually produce real and substantial benefits, these companies should explain them to the public – as required by Hong Kong’s Code of Corporate Governance.¹⁵⁷ Indeed, such disclosures may well help academics and policymakers better understand the benefits of allowing such offshore incorporations.¹⁵⁸ One way to do this consists of introducing an explicit “legitimate economic purpose test” in article 61/61a into the Inland Revenue Ordinance (during the

¹⁵³ For a description of such regulation, and an assessment, see Sridhar Arcota, Valentina Bruno and Antoine Faure-Grimaud, *Corporate Governance in the UK: Is the Comply or Explain Approach Working?*, 30 INT’L REV. OF L. & ECON. 193, 201 (2010). For more on Hong Kong’s own comply-or-explain regime, see David Graham, *Comply or Explain – A Guide to Compliance with Hong Kong’s Corporate Governance Code*, CSJ (Sep. 5, 2014) <http://csj.hkics.org.hk/site/2014/09/05/comply-or-explain-a-guide-to-compliance-with-hong-kongs-corporate-governance-code/>.

¹⁵⁴ Indeed, the minimalist school – whereby civil servants exercise discretion in cases where regulated parties to do not act according to established principles – has evolved into the more nuanced view we provide in this article. For the predecessor views, see Charles Sabel & William Simon, *Minimalism and Experimentalism in the Administrative State*, 100 GEO. L.J. 53, 93 (2012).

¹⁵⁵ For evidence and further arguments, see Ruth Aguilera, Alvaro Cuervo-Cazurra, *Codes of Good Governance Worldwide: What is the Trigger?*, 25 ORG. STUD. 415, 443 (2004).

¹⁵⁶ Numerous academic studies find that shareholders would balk at offshore incorporations if given the chance. Such results confirm our own conclusions – as such incorporations can kill shareholder value. See Holub Johnson, *Questioning Organizational Legitimacy: The Case of U.S. Expatriates*, 47 J. BUS. ETHICS 269, 293 (2003).

¹⁵⁷ A number of academics argue in favour of leaving offshore incorporations unregulated. Yet, if disclosure and transparency help markets work better, these authors should not object to full public disclosure of the benefits these offshore structures endow. See Jill Fisch, *Leave It to Delaware: Why Congress Should Stay out of Corporate Governance*, 37 DEL. J. CORP. L. 731, 782 (2013). See also Ehud Kamar, *Beyond Competition for Incorporations*, 94 GEO. L.J. 1725, 1770 (2006).

¹⁵⁸ We understand very poorly the benefits of offshore incorporation (besides the obvious tax benefits). For a discussion of this lack of understanding, see Peter Buckley et. al., *The Economic Geography of Offshore Incorporation in Tax Havens and Offshore Financial Centres: The Case of Chinese MNEs*, 15 J. ECON. GEOGRAPHY 103, 128 (2015).

next major legal revision), in offshore listings, and in risk profiling clients/partners. Similarly, regulators at the Hong Kong Stock Exchange and the Securities and Futures Commission could add a provision to the Hong Kong Code of Corporate Governance requiring companies to confirm that the jurisdiction they have incorporated in matches the firm's economic purpose, or explain why not. Both changes would encourage companies (and their regulators) to focus on final economic purposes – while offering flexibility in cases where other business needs dominate.¹⁵⁹

Other innovations in tax law might help inspire changes to the broader legal framework in the fight against corporate maladministration. Notably, Hong Kong's adoption of anti-abuse doctrines in its tax sphere might usefully serve to promote better corporate governance in the listing sphere. Hong Kong is a member of an OECD group working on regulations designed to stop treaty abuse that Mossack Fonseca's clients exploited so widely.¹⁶⁰ That forum uses the term Principal Purpose Test as a rough equivalent to the reasonable commercial purpose test we described previously.¹⁶¹ Yet, at present, the Securities and Futures Commission's authorisation for companies incorporated abroad to list and transact in Hong Kong depends more on rule-following rather than the actual purpose and result of these rules.¹⁶² As the SFC's Joint Policy Statement regarding the listing of overseas companies from September 2013 notes, the "Listing Rules require an overseas

¹⁵⁹ This approach contrasts with other attempts to reframe administrative law, such as the German *Neue Verwaltungsrechtswissenschaft*, which claims to look at the very foundations of such rulemaking itself. See Andreas Vosskuhle & Thomas Wischmeyer, *The 'Neue Verwaltungsrechtswissenschaft' Against the Backdrop of Traditional Administrative Law Scholarship in Germany*, in *COMPARATIVE ADMINISTRATIVE LAW* 85 (Peter Lindseth & Susan Rose-Ackerman eds., 2nd ed. 2019).

¹⁶⁰ The G20/OECD Base Erosion and Profit Shifting Project has developed common regulations aimed at reducing the tax loopholes which incentivize poor corporate governance on the Mainland as elsewhere. See BEPS ACTIONS, <http://www.oecd.org/tax/beps/beps-actions.htm> (last visited June 12, 2019). For a list of members, see INCLUSIVE FRAMEWORK COMPOSITION: BEPS MEMBERS, <http://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf> (last visited June 12, 2019).

¹⁶¹ In that context, lawmakers seek to regulate the holding companies whose structures muddy corporate relationships and reduce transparency to the outside world. See Juliana Dantas et al., *BEPS Action 6: Preventing Treaty Abuse - A Threat to Holding Structures?*, LEXOLOGY (May 26, 2016) <https://www.lexology.com/library/detail.aspx?g=4be6cf03-3bc1-44d8-93ae-e943c413d6e5>.

¹⁶² For a list of countries (and the extra rules needed for each), see LIST OF ACCEPTABLE OVERSEAS JURISDICTIONS, https://www.hkex.com.hk/listing/rules-and-guidance/other-resources/listing-of-overseas-companies/list-of-acceptable-overseas-jurisdictions?sc_lang=en (last visited June 12, 2019).

company to demonstrate that its jurisdiction of incorporation has shareholder protection standards at least equivalent to those of Hong Kong. If this is not possible, overseas companies can achieve equivalent standards by varying their constitutive documents to provide them.”¹⁶³ For the BVI specifically, the HKEx Country Guide finds – in granting authorisation for BVI companies to list in Hong Kong, that “we do not consider BVI’s shareholder protection standards to be materially different to our own.”¹⁶⁴ As described in Figure 7, the HKEx (and SFC for that matter) have broad discretion over the recognition of foreign corporate governance and other standards. They do not describe the extent to which risk assessment (rather than simple compare-and-contrast of law) plays a role in determining who can list. Would a simple principle or test make such a determination more predictable and transparent than no standard at all?

FIGURE 7 WHO EMPOWERS THE EXCHANGE TO REGULATE FOREIGN COMPANIES LISTED IN HONG KONG?

Where does the Hong Kong Stock Exchange’s authority to regulate foreign-listed companies come from? This so far academic question has practical applications if Hong Kong is to adopt more corporate-governance-friendly listing rules covering foreign companies (especially from the Mainland). The Securities and Futures Ordinance gives the Securities and Futures Commission the power to deal with foreign regulators and authorities.* A Memorandum of Understanding delegates that authority to the Hong Kong Stock Exchange to regulate day-to-day (continued) listing matters and trading.** Yet, just how far does that authority extend? Can the Exchange travel to these companies abroad and make determinations about corporate governance-related matters? Do certain types of SFC agreements with foreign authorities represent ‘international relations?’ (a political question to be sure) as prohibited in Hong Kong’s Basic Law.

¹⁶³ See SFC & HKEx, JOINT POLICY STATEMENT REGARDING THE LISTING OF OVERSEAS COMPANIES (Sept. 27, 2013), https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Other-Resources/Listing-of-Overseas-Companies/Joint-Policy-Statement-20130927/new_jps_0927.pdf.

¹⁶⁴ See HKEx, Country Guide – British Virgin Islands (Apr. 2014), https://www.hkex.com.hk/-/media/hkex-market/listing/rules-and-guidance/other-resources/listing-of-overseas-companies/a-list-of-acceptable-overseas-jurisdictions/cg_bvi.

We do not have the space to do a full analysis here. Tradition has clearly sided with the HKEx imposing these rules.*** Why does the authority to recognise other jurisdictions' corporate governance standards fall to the SFC and the HKEx? Why don't foreign companies listed on the exchange have so few rights to take decisions about the Exchange and its policies when they constitute over 40% of listing companies? Why does listing in Hong Kong give the Hong Kong government the right to determine the corporate governance standards of foreign companies operating in foreign jurisdictions? While we base our recommendations on the common understanding of existing law, the legal purist may feel very uneasy with the authority the HKEx (and even the SFC) use to justify regulating foreign companies listed in Hong Kong.

* Securities and Futures Ordinance at 5(1.h) available online.

** Memorandum of Understanding Regarding Listing Matters, at 2.4 available online.

*** The Hong Kong Stock Exchange represents one of the Hong Kong Exchanges and Clearing Limited's subsidiaries.

What specific rules might encourage a focus on the overall economic purposes of corporate activity? The Panama Papers pointed to four practices in particular that undermine corporate governance in the wider business environment.¹⁶⁵ First, rules that allow or encourage mailbox company colonies (or large numbers of corporations based out of a mail centre or building in which none of these companies' economic activity occurs.)¹⁶⁶ Second, rules requiring foreign-only operation of companies (namely companies incorporated in a particular jurisdiction that are forbidden from operating in that jurisdiction).¹⁶⁷ If these jurisdictions consider the company unfit to operate within their borders, why would they consider them more fit to operate abroad? Third, domestic rules

¹⁶⁵ Alibaba (a Chinese technology company) illustrates the risks and potential harms of non-transparent governance of an offshore incorporation entity. See Lin Yu-Hsin & Thomas Mehaffy, *Open Sesame: The Myth of Alibaba's Extreme Corporate Governance and Control*, 10 BROOK. J. CORP., FIN. & COM. L. 437, 471 (2016).

¹⁶⁶ Numerous stories and studies have shown that these mailbox company colonies aim to avoid taxation rather than to enable more productive corporate operations. For a recent case where authorities required changes to complicated governance structures, see Jesse Drucker & Jeremy Kahn, *U.K.'s Tax Deal With Google Wasn't Just About Offshore Havens*, BLOOMBERG (Feb. 4, 2016), <https://www.bloomberg.com/news/articles/2016-02-03/u-k-s-tax-deal-with-google-wasn-t-just-about-offshore-havens>.

¹⁶⁷ Under the International Business Companies Act, BVI companies are "ring fenced" – meaning they cannot conduct business domestically. Numerous studies show the harms of these provisions. See Guttorm Schjelderup, *Secrecy Jurisdictions*, 23 INT'L TAX & PUB. FIN. 168, 189 (2016).

allowing for directors' meetings with individuals who have no knowledge of the companies they supposedly govern and shareholder meetings conducted as a formality without any important company policies or decisions being discussed. Fourth, rules allowing for the sale and subsequent operation shelf companies – as these shelf companies obviously had no legitimate economic purpose when incorporated. These rules have traditionally corresponded with companies having poor/little actual corporate governance – and provided ways for corruption and fraud to undermine corporate governance in larger, more established companies on the Mainland and elsewhere.¹⁶⁸ Yet, rather than simply banning transactions with these kinds of entities, a “non-administrative” administrative law would allow such transactions if they served a legitimate economic purpose.

Naturally, shell and shelf companies pose significant risks to corporate governance in Hong Kong and outside. If judged by media reports, the dire current situation begs for additional regulation. These reports claim that 40% of the 22 companies listed on HKEx (on the main board) for the three month period ending in February 2016 consisted of shell companies.¹⁶⁹ Share price volatility of these listed shell companies make the harms to equity markets and corporate governance in general obvious – with 56 companies' valuations increasing by more than 1,000% between 2013 and 2015, despite 39 of them losing money.¹⁷⁰ Few can document the corporate governance practices of many shell companies that have other shell companies as directors and shareholders.¹⁷¹ Hong Kong's disclosure regime should thus include shell companies, special

¹⁶⁸ Williams explains why authorities like Hong Kong's need to focus on regulatory consequences as well as conduct-effects, as offshore financial centers modify their financial services to avoid tightening regulation world-wide. The only successful approach, in light of such market adaptation, requires moving away from looking at paper rules. See Thomas Williams, *International Pressure Makes Offshore Lawyers Change Tack*, 21 INT'L FIN. L. REV. 24, 34 (2002).

¹⁶⁹ See Shirley Yam, *Hong Kong's Red-Hot Corporate Shell Game is Cause for Concern*, SOUTH CHINA MORNING POST (Feb. 26, 2016), <https://www.scmp.com/business/article/1917575/hong-kongs-red-hot-corporate-shell-game-cause-concern>.

¹⁷⁰ Benjamin Robertson et al., *The Magical Transformation of Hong Kong's Listed Companies*, BLOOMBERG (July 12, 2016), <https://www.bloombergquint.com/china/the-magical-transformation-of-hong-kong-s-listed-companies>.

¹⁷¹ Jim Zarroli, *Want to Set Up a Shell Corporation to Hide Your Millions? No Problem*, NAT'L PUB. RADIO (Apr. 13, 2016), <https://www.npr.org/2016/04/13/474101127/want-to-set-up-a-shell-corporation-to-hide-your-millions-no-problem>.

purpose vehicles and companies that work with them...something that anyone acting with an eye toward increasing transparency cannot avoid concluding.¹⁷²

Hong Kong's code of corporate governance should introduce a special section for offshore, shell/shelf, special purpose vehicles and conduit companies. Numerous studies have documented both the good and bad sides of using these kinds of structures.¹⁷³ Most authors argue that regulators should not try to "fix" these structures – but rather increase their transparency.¹⁷⁴ Requiring that special purpose vehicles have a unique designation (like SPV rather than Ltd. or Inc.) can help ensure parties understand the nature of the entity they do business with. If these entities truly are companies, then why do they not issue the same large corporate governance reports as the traded entities that use them? Numerous studies have described how to modify accounting and reporting procedures for these entities.¹⁷⁵

Four amendments to the Code of Corporate Governance in particular could help reinforce the idea of focusing on final economic purposes. First, Hong Kong's policymakers could introduce rules in the Listing Rules companies from jurisdictions (or companies which transact with them) which require additional due diligence and a classification as a high risk entity if that company's jurisdiction allows or encourages: a) mailbox company colonies, b) foreign-only operation and c) directors and shareholder meetings with individuals having little knowledge of the companies they affiliate with, and d) sale and operation of shelf companies. Second, they could introduce a provision in the Code of Corporate Governance to require

¹⁷² Even common sense would lead businessmen to know more about their customers. For evidence about the wide-spread abuses of the current opaque system, see MICHAEL FINDLEY et al., *GLOBAL SHELL GAMES: TESTING MONEY LAUNDERERS' AND TERRORIST FINANCIERS' ACCESS TO SHELL COMPANIES* (2014).

¹⁷³ Ahlawat and co-authors in particular describe the pros and cons of these structures, along with their lack of transparency, particularly well. See Sunita Ahlawat, Danielle Bolomo & Kyle Ropp, *Whether Sensible Business Tool or Deceptive Scheme to Conceal, the Special Purpose Entities Are Here to Stay*, 3 ACCT. & FIN. RES. 77, 86 (2014).

¹⁷⁴ Newman in particular represents one voice in this camp. See Neal Newman, *Enron and the Special Purpose Entities-Use or Abuse-The Real Problem-The Real Focus*, 13 L. & BUS. REV. THE AM. 97, 138 (2007).

¹⁷⁵ Our paper – focused on corporate governance – does not try to discuss the accounting and reporting rules around these entities. For more, see BASEL COMMITTEE ON BANKING SUPERVISION, *REPORT ON SPECIAL PURPOSE ENTITIES* (Bank for Int'l Settlements Press 2009).

companies conducting any transactions with a shell company, offshore company from the BVI, Cayman Islands, Bahamas, or other jurisdictions decided by the HKEx to disclose such business and the nature of that business.

Third, they could require SPV at end of company name (like Limited) to designate that the entity is a special purpose vehicle. Fourth, they could require offshore, shell/shelf, special purpose vehicles, and “hollow” holding companies to issue corporate governance reports outlining their operations in the same way that normal companies do. These activities would increase transparency, rather than setting fixed proscriptive or restrictive rules.

Stepping back, the Panama Papers experience teaches us that the Exchange should regulate the practices of shareholder protection rather than simply standards. Clearly, the legitimate economic purpose test and anti-abuse provisions we discussed previously focus more on intent and action – rather than just written regulations and policies. The SFC and HKEx should focus more on practice in foreign jurisdictions and by foreign companies than on their printed policies. The easiest way to introduce such changes into the way we relate to (and regulate) companies’ behaviour abroad consists of amending the Joint Statement, so that the second paragraph reads:

“Listing Rules require an overseas company to demonstrate that its jurisdiction of incorporation has shareholder protection standards and practices at least equivalent to those of Hong Kong. If this is not possible, overseas companies can achieve equivalent standards and practices by varying their constitutive documents as well as governance and enforcement practices to provide them”.¹⁷⁶

VII. CONCLUSION

The Panama Papers clearly show the need for Hong Kong’s lawmakers and regulators to adopt rules encouraging better corporate governance. Judging by the past, Hong Kong’s financial, corporate, tax and other regulations have failed to prevent the abuses identified in the Panama Papers. Yet, these failures tell us something more general about Hong Kong’s administrative law – and its weaknesses. Effective regulations need to focus on ends, not means.

¹⁷⁶ *Supra* note 163.

Administrative law which focuses on these ends encourages public officials, civil servants, and even inspectors to focus on these ends. Administrative law affects the way companies regulate themselves (both through self-governing associations and in their own internal rules).

Naturally, not everyone will approve of regulations focused on ends rather than means. Such an approach removes some of the certainty of administrative law focused on processes and procedures.

¹⁷⁷ Such an approach has had die-hard advocates – even in places like Japan – where industry and market-related administrative law has been forced to adopt a greater emphasis on outcomes since the 1990s.¹⁷⁸ Yet, regulations covering wide swaths of corporate life – like accounting regulations—have moved towards governing results, not means.¹⁷⁹ Regulating by results also reduces the need or desire to engage in the inappropriate “transplanting” of rules from other jurisdictions whose performance certain policymakers might want to emulate.¹⁸⁰ Regulation by results also confronts the very real competition between regulatory regimes already occurring.¹⁸¹ In some sense, administrative law’s shift toward outcomes will simply reflect the changes already occurring in other parts of our regulatory apparatus.

We illustrated how a new approach to administrative law could encourage good corporate governance in several areas. Public officials’ action can affect and incentivize the ranking/rating of corporate governance practices. They both require and expect a certain disclosure. Administrative law can make both ratings and disclosures the default norm, in government as well as in business

¹⁷⁷ Obviously, having procedurally-focused corporate governance law makes judging and resolving disputes easier. See Norman Veasey, *An Economic Rationale for Judicial Decision Making in Corporate Law*, 53 THE BUS. L. 681, 700 (1998).

¹⁷⁸ See Duck, Ken, *Now That the Fog Has Lifted: The Impact of Japan’s Administrative Procedures Law on the Regulation of Industry and Market Governance*, 19 FORDHAM INT’L L.J. 1686, 1763 (1996).

¹⁷⁹ The principles-based IFRS (or International Financial Reporting Standards) have required such an outcome/result based view for at least a decade. See Salvador Carmona & Marco Trombetta, *On the Global Acceptance of IAS/IFRS Accounting Standards: The Logic and Implications of the Principles-Based System*, 27 J. OF ACCT. & PUB. POL’Y 455, 461 (2008).

¹⁸⁰ Troy Paredes, *A Systems Approach to Corporate Governance Reform: Why Importing U.S. Corporate Law Isn’t the Answer*, 45 WILLIAM & MARY L. REV. 1055, 1158 (2004).

¹⁸¹ Ehud Kamar, *A Regulatory Competition Theory of Indeterminacy in Corporate Law*, 98 COLUM. L. REV. 1908, 1959 (1998).

alike. Principles-based rules focused on ends can also set a positive example – and a level of expectation – for self-regulating professions. No one could dispute that companies should pursue legitimate economic purposes. They should not unnecessarily avoid paying taxes. Corporations should also not withhold information simply because they can. If econometric evidence shows the benefits of good corporate governance, “non-administrative” administrative law (as we have defined it in this paper) represents the way that civil servants and regulators can encourage companies to follow such good governance. If other areas of the public administration work like corporate regulation, then perhaps it is time to rethink the way we write administrative rules.