

Part B Consultation Questions

Please indicate your preference by checking the appropriate boxes. Please reply to the questions below on the proposed change discussed in the Consultation Paper downloadable from the HKEx website at: <http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201406.pdf>

Where there is insufficient space provided for your comments, please attach additional pages.

1. Do you agree with our proposal to amend the title of Section C.2 of the Code to “Risk management and internal control”?

Yes

No

Please give reasons for your views.

No comment.

2. Do you agree with the proposed amendments to Principle C.2 to define the roles of the board and the management, and state that the management should provide assurance to the board on the effectiveness of the risk management systems? Is the intention of the proposed wording sufficiently clear?

Yes

No

Please give reasons for your views.

In many cases, the roles of the board and the management may not be distinctly independent. This is particularly so for issuers of a smaller size where the executive directors of the board are also the key management personnel. In practice, their roles and responsibilities in respect of risk management and internal control cannot be clearly delineated. The proposed assurance on the effectiveness of risk management and internal control systems provided by “the management” to the board may not add practical value to enhancing corporate governance of issuers or even to protecting shareholders’ value. Therefore, the existing wording of the Principle C.2 is already sufficient to serve its purpose.

3. Do you agree with our proposal to introduce an amended RBP (C.2.6) to provide that the board may disclose in the Corporate Governance Report that it has received assurance from management on the effectiveness of the issuer's risk management and internal control systems? Is the intention of the proposed wording sufficiently clear?

Yes

No

Please give reasons for your views.

Please refer to our comments on Question 2 above.

4. Do you agree with the proposed amendments to CP C.2.1 to state that the board should oversee the issuer's risk management and internal control systems on an ongoing basis? Is the intention of the proposed wording sufficiently clear?

Yes

No

Please give reasons for your views.

The current practice of annual review by the board is already sufficient for its intended purposes. In many cases, particularly for issuers of a smaller size or with operations of less complexity, it may not be cost-effective to replace the one-off annual exercise by an on-going risk management review.

5. Do you agree with our proposal to upgrade to a CP the existing RBP C.2.3, which sets out the matters that the board's annual review should consider?

Yes

No

Please give reasons for your views.

As issuers may vary significantly in size and complexity of operations, as well as the type of risks and challenges their business face, flexibility should be maintained in respect of the internal controls disclosure requirements. The proposal will impose an unduly onerous disclosure burden on issuers and at the same time cause issuers of a smaller size to incur additional compliance costs. Therefore, the existing RBP C.2.3 should remain as a recommended best practice.

6. Do you agree with our proposal to upgrade to a CP the existing RBP C.2.4, which sets out the particular disclosures that issuers should make in their Corporate Governance Reports in relation to how they have complied with the internal control CPs during the reporting period?

Yes

No

Please give reasons for your views.

Please refer to our comments on Question 5 above.

7. Do you agree with our proposal to amend the wording of proposed CP C.2.4 to simplify the requirements and remove ambiguous language, and to make clear that the risk management and internal control systems are designed to manage rather than eliminate risks? Is the intention of the proposed wording sufficiently clear?

Yes

No

Please give reasons for your views.

No comment.

8. In relation to proposed CP C.2.4, do you agree with our proposal to upgrade the existing recommendation that issuers disclose their procedures and internal controls for handling and disseminating inside information (Section S., paragraph (a)(ii)), and amend it to include the handling of “other regulatory compliance risks”?

Yes

No

Please give reasons for your views.

While it is suggested to remove ambiguous language in the existing CP, the proposed insertion of a new phase “other regulatory compliance risks” will cause unintended ambiguity due to its undefined scope of risks. Issuers have to take the responsibility to identify all the potential regulatory compliance risks which they are or will be exposed to.

9. Do you agree with our proposal to upgrade to Mandatory Disclosures the following existing Recommended Disclosures in relation to internal controls (Section S.):

- (a) whether the issuer has an internal audit function;
- (b) how often the risk management and internal control systems are reviewed, the period covered, and where an issuer has not conducted a review during the year, an explanation why not;
- (c) a statement that a review of the effectiveness of the risk management and internal control systems has been conducted and whether the issuer considers them effective and adequate; and
- (d) significant views or proposals put forward by the audit committee?

Yes

No

Please give reasons for your views.

The existing Recommended Disclosures are already sufficient. There are no strong evidences to support that the upgrade will, in practice, add value to enhancing the effectiveness of risk management.

10. Do you agree with our proposal to move the existing recommendation that issuers disclose details of any significant areas of concern (Section S., paragraph (a)(ix)) to a new RBP C.2.7, and to amend the provision to widen its application by removing the reference to areas of concern “which may affect shareholders”?

Yes

No

Please give reasons for your views.

No comment.

11. Do you agree with our proposal to remove RBP C.2.5, which states that issuers should ensure their disclosures provide meaningful information and do not give a misleading impression?

Yes

No

Please give reasons for your views.

12. Do you agree with our proposals to remove the recommendations that issuers include in their Corporate Governance Reports:

- (a) an explanation of how the internal control system has been defined for them (Section S., paragraph (a)(i)); and
- (b) the directors' criteria for assessing the effectiveness of the internal control system (Section S., paragraph (a)(vii))?

Yes

No

Please give reasons for your views.

13. Do you agree with our proposal to upgrade RBP C.2.6 to a CP (re-numbered C.2.5) and amend it to state that an issuer should have an internal audit function, and issuers without an internal audit function should review the need for one on an annual basis and disclose the reasons for the absence of such function in the Corporate Governance Report? Is the intention of the proposed wording sufficiently clear?

Yes

No

Please give reasons for your views.

The need for an issuer to have an internal audit function depends on the complexity of its operations. For issuers of a smaller size, an in-house internal control review on an annual basis can be equally cost-effective, with a well-defined scope and proper execution. Furthermore, there are no evidences to support that the establishment of an internal audit function can fully cover or identify all risks with which an issuer may be faced. The adequacy and effectiveness of an issuer's risk management and internal control systems are not necessarily correlated with the internal audit function. Therefore, the existing RBP C.2.6 is already sufficient.

14. Do you agree with our proposal to introduce new Notes to the proposed CP C.2.5 to clarify that:

(a) the role of the internal audit function is to carry out the analysis and independent appraisal of the adequacy and effectiveness of an issuer's risk management and internal control systems; and

(b) a group with multiple listed issuers may share group resources of the holding company to carry out the internal audit function for members of the group?

Yes

No

Is the intention of the proposed wording sufficiently clear? Please give reasons for your views.

Please refer to our comments on Question 13 above.

15. Do you agree with our proposal to amend the existing CP C.2.2 to state that the board's annual review should ensure the adequacy of resources, staff qualifications and experience, training programmes and budget of the issuer's internal audit function (in addition to its accounting and financial reporting functions)?

Yes

No

Please give reasons for your views.

The set-up of an internal audit function should remain as a RBP. Therefore, the existing CP C.2.2 is already sufficient.

16. Do you agree with our proposal to amend Principle C.3 in respect of audit committees and CP C.3.3 in respect of their terms of reference to incorporate “risk management” where appropriate?

Yes

No

Please give reasons for your views.

The existing wording of Principle C.3 is sufficient for the current role of the audit committee.

17. Do you agree that the matter of establishing a separate board risk committee should be left to issuers to decide in accordance with their own circumstances?

Yes

No

Please give reasons for your views.

The need to establish a separate board risk committee largely depends on the nature and level of the risks issuers have to face under different circumstances.

18. What would be an appropriate period of time between the publication of the consultation conclusions and the implementation of the amendments set out in the Consultation Paper?

Six months

Nine months

12 months

Others (please specify:)

Please give reasons for your views.