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17 June 2021

Mr Nicolas Aguzin
Chief Executive Officer
Hong Kong Exchanges and Clearing Limited
8/F, Two Exchange Square
8 Connaught Place, Central
Hong Kong

Dear Mr Aguzin,

Re: Consultation Paper on Review of Corporate Governance Code and Related Listing Rules

The Hong Kong General Chamber of Commerce welcomes the opportunity to express our views on the subject consultation.

We welcome the HKEX's proposal to enhance the corporate governance and related listing rules in such areas as corporate culture and Environmental, Social and Governance disclosures and standards. At the same time, we believe that consideration should also be given to instituting a cost-benefit analysis to determine whether regulatory intervention is justified, and to adopt a gradual and flexible approach when implementing such changes.

Our comments on the specific consultative proposals are as set out in the attached.

We hope you will find our comments useful to your deliberations.

Yours sincerely,

[redacted]

Encl.

HKEX Consultation Paper on Review of Corporate Governance Code and Related Listing Rules (April 2021)

Response by The Hong Kong General Chamber of Commerce (HKGCC)

HKGCC welcomes the opportunity to respond to this consultation paper ("the Paper"). We set out first our general comments on the Paper, then our specific answers to the consultation questions in it.

1. **General Comments**

1.1. To a large extent, the Paper's proposals are designed to strengthen HKEX's existing requirements on corporate governance, by introducing new requirements that did not previously exist, or making existing requirements more stringent. These proposals come on top of other new requirements that HKEX has introduced relatively recently in this area, including those following its 2017 *Review of the Code on Corporate Governance Practice and Related Listing Rules*, and its 2019 *Review of* the *Environmental, Social and Governance Reporting Guide and Related Listing Rules*.

1.2. It should be noted that all of these changes come at a cost to businesses, which have not only to respond to the proposals if they wish to influence them, but also to adapt their policies and practices to comply with the burden imposed by any new proposals that are implemented.

1.3. We were pleased to see recently that HKEX appears to recognise this, and that *existing* regulatory provisions which are unnecessary, superfluous or outdated should be removed.[1] In these difficult economic times, it is also particularly important that *new* regulatory interventions are subject to a rigorous regulatory impact assessment before they are introduced, to ensure that they will bring definite benefits, and that those benefits exceed the costs of compliance. Generally speaking, existing requirements should only be *strengthened* (such as changing a recommended best practice to a code provision) where they have been shown to be insufficient to achieve compliance.

1.4. In the Hong Kong context, it is particularly important to bear in mind the impact that new regulatory interventions would have on small and medium-sized businesses (SMEs), which form the vast majority of Hong Kong businesses, and are key to Hong Kong's economic prosperity. Many of them are either already listed, or aspire to be in future. While larger companies may have the resources to comply with certain new regulatory requirements, SMEs would find this a much greater challenge. This is another important reason for conducting a rigorous cost-benefit analysis before any new regulatory intervention is introduced.

1.5. With these considerations in mind, we set out below our specific answers to the consultation questions.

2. **Question 1:** *Do you agree with our proposal to introduce a CP requiring an issuer's board to set culture in alignment with issuer's purpose, value and strategy?*

[1] Consultation Paper on *Listing Regime for Overseas Issuers* (March 2021).

2.1. We would need to see further information and justification for this proposal before deciding whether to support it, as explained below.

2.2. First, it is not clear what is meant by "culture", "purpose" and "value":

- As the Paper notes,[2] HKEX's 2018 *Guidance for Boards and Directors* ("the 2018 Guidance") stated that "the board should lead in shaping and developing the issuer's *risk* culture". (Emphasis added). In contrast, the Paper refers simply to "culture", not "risk culture". It therefore seems that the Paper envisages culture in a wider sense than the 2018 Guidance. However, it is not clear what the additional elements in culture are perceived to be, apart from risk. The Paper seems to recognise this lack of clarity, by stating that HKEX will provide guidance on (*inter alia*) "the key elements commonly identified in a sound culture".[3] We believe it would be premature to support a wider concept of culture without knowing what HKEX believes these key elements are, and what HKEX regards as being a "healthy culture"[4], and a "sound culture".[5]

- The Paper is also unclear what it means by "purpose". A company's objects are, as a legal requirement, set out in its Articles of Association. Presumably, the Paper means "purpose" in a different sense from the company's objects, but it is not clear what this is.

- Normally the "value" of a company refers to the amount of its market capitalisation. It seems that the Paper may be referring to something different, and wider, when it mentions value. Indeed, at one point, the Paper refers to "values" rather than "value": "The strategy to achieve a company's purpose should reflect the company's *values* and culture, and should not be developed in isolation".[6] (Emphasis added). If value does indeed mean something different from the amount of market capitalisation, it needs to be made clear what this meaning is, and how it differs from culture.

2.3. In summary, we are not in a position to support a requirement or exhortation that the issuer's board align the company's "culture" with its "purpose, value and strategy" without the necessary clarifications identified above.

2.4. Secondly, even if the above issues were clarified, the Paper does not explain why the objective of aligning the company's culture with these other matters cannot be addressed simply by amending and extending the 2018 Guidance, instead of introducing, not even a new Recommended Best Practice ("RBP"), but a (more stringent) new Code Provision to this effect. As noted in our General Comments above, regulatory intervention should only be made where it is necessary and appropriate to achieve a particular objective. Where it is necessary and appropriate, the least intrusive means of intervention to achieve the objective should be preferred. If the concepts of "culture", "purpose" and "value" were satisfactorily clarified (see

[2] Para 45.
[3] Para 51.
[4] Para 47.
[5] Para 51.
[6] Para 49.

above), we believe that an amendment to the 2018 Guidance would be sufficient and proportionate.

3. **Question 2(a):** *Do you agree with our proposal to introduce a CP requiring establishment of an anti-corruption policy?*

   3.1. At present, issuers are required, on a "comply or explain" basis, to *disclose* their preventative measures against corrupt practices.[7] This implies that they should already have in place an anti-corruption policy.[8] Moreover, issuers (and other companies) are, or should be, well aware of the rules against anti-corruption, and the consequences that a breach of the rules can entail. This also provides an incentive for them to comply with the rules, and to have in place appropriate compliance systems to enable them to do so. We do not therefore believe that an explicit CP requiring issuers to establish an anti-corruption policy would impose any additional material cost or burden on issuers, and it would have the benefit of highlighting to all issuers the importance of having such a policy in place. We therefore support this proposal.

4. **Question 2(b):** *Do you agree with our proposal to upgrade a RBP to CP requiring establishment of a whistleblowing policy?*

   4.1. We believe it is important for issuers to have in place a whistleblowing policy, so that employees can bring to the attention of the board any legal contraventions or other malpractices of which they should be aware. It is essential, however, that the confidentiality of whistleblowers is closely safeguarded. Otherwise, this would not only undermine the efficacy of the policy by deterring whistleblowing, but would also harm the interests of the whistleblowers themselves. Subject to this proviso, we therefore agree with this proposal, since it would bring clear potential benefits, without imposing material costs on issuers.

5. **Question 3:** *Do you agree with our proposal to introduce a CP requiring disclosure of a policy to ensure independent views and input are available to the board, and an annual review of the implementation and effectiveness of such policy?*

   5.1. Yes. The Paper summarises the existing requirements to ensure that independent views and input are available to the board.[9] These requirements imply that issuers should have in place a policy to ensure compliance with them. We do not believe it is unreasonable or unduly onerous to require issuers to disclose this policy, or to conduct an annual review of the implementation and effectiveness of this policy. Such disclosure would be potentially useful to investors, without unduly compromising the interests of the issuer.

6. **Question 4(a):** *Do you agree with our proposal regarding re-election of Long Serving INEDs to revise an existing CP to require (i) independent shareholders' approval; and (ii) Additional Disclosure?*

   6.1. Regarding (i), we do not agree that independent shareholders should be allowed to veto the re-election of a Long Serving INED. No explanation is given in the Paper as

[7] CP para 55.
[8] Para 59.
[9] Para 62.

to why this is appropriate, or why the existing practice of the re-election being subject to the vote of shareholders as a whole should not be continued. There is no reason to exclude majority shareholders from voting on this issue: to do so would be unfair and unjustified. We therefore oppose this proposal.

6.2. As regards (ii), the current Code already requires the papers to shareholders accompanying the resolution to include reasons why the Long Serving INED is still independent and should be re-elected. We do not see any valid grounds for objecting to these reasons being subject to additional disclosure. We therefore support this proposal.

7. **Question 4(b):** *Do you agree with our proposal to introduce a CP requiring an issuer to appoint a new INED at the forthcoming AGM where all the INEDs on the board are Long Serving INEDs, and disclosing the length of tenure of the Long Serving INEDs on the board on a named basis in the shareholders' circular?*

7.1. There are two parts to this question.

7.2. Regarding the second part- whether the length of tenure of the Long Serving INEDs should be disclosed on a named basis in the shareholders' circular- we do not see any reasonable grounds for objecting to this proposal.

7.3. Regarding the first part, however, it is difficult to see any need for issuers to be required to appoint a new INED when all existing INEDs are Long-Serving INEDs. The current Code already requires the continuing independence of Long Serving INEDs to be tested before their re-election (see above), which serves the same objective that the appointment of a new INED would be aimed at. Moreover, we are concerned that such a requirement may impose a disproportionate burden on small and medium-cap issuers, which may not have access to the same talent pool of potential INEDs as large-cap issuers. In our view, an additional requirement to appoint a new INED would therefore impose an unnecessary burden on certain issuers, without producing any countervailing public benefit. Accordingly, we do not support this proposal.

8. **Question 5:** *Do you agree with our proposal to introduce a new RBP that an issuer generally should not grant equity-based remuneration (e.g., share options or grants) with performance-related elements to INEDs as this may lead to bias in their decision-making and compromise their objectivity and independence?*

8.1. Yes, for the reason stated in this question (see above).

9. **Question 6(a):** *Do you agree with our proposal to highlight that diversity is not considered to be achieved by a single gender board in the note of the Rule?*

9.1. We fully support board diversity, including as to gender, given the recognised improvements in board effectiveness that a wide variety of perspectives and experiences can bring. We also agree that the current proportion of women on boards ("WOBs") in Hong Kong is disappointingly low, at only 12.7 per cent of Hong Kong listed company directorships in 2020 (up from 12.4 per cent in 2019).[10] The question

[10] Para 83.

is therefore not whether a substantial increase in the number of WOBs in Hong Kong is a desirable objective (it clearly is), but how this can best be achieved.

9.2. We are not persuaded that the proposed note to the current Rule on board diversity disclosure, stating that diversity is not considered to be achieved by a single gender board (i.e., a single gender board is legally unacceptable) is the best, or an appropriate, way to achieve this objective. The reasons are as follows:

- The note would effectively amount to a legal requirement on issuers to have at least one WOB at all times. This would, in our view, send the wrong signal to issuers and encourage a mindset that having one WOB was acceptable, as opposed to one which encourages the desired substantial increase in the number of WOBs over time. We agree with the following comment by the current President of The Hong Kong Institute of Chartered Secretaries (HKICS): "...progress towards increased representation of women on boards will be most successful and sustainable when it rests on a broad-based stakeholder consensus which encourages shareholders to improve the gender diversity of the directors they appoint, rather than the top-down imposition of quotas".[11]

- Many issuers (especially large cap ones) would not find the requirement to *always* have at least one WOB, even from the date that the proposed note would take effect, unduly onerous. However, we envisage that there are some issuers who would find it more difficult to ensure this requirement is met, particularly in the early stages, especially small to medium-cap issuers who might need longer time to achieve compliance. For example, suitably- qualified individuals may, after due enquiry and process, be unavailable to them at a time when they wish to fill a board vacancy. It would be unfair and unduly harsh if such an issuer were in breach of the listing rules in such circumstances, which would be the effect of the proposed note to the Rule.

9.3. We think a better way to meet the objective of achieving a substantial increase of WOBs over a reasonable period would be to follow HKICS's recommendation of a introducing a voluntary target of 30 per cent of WOBs within a period of six years.[12] This could be introduced as a CP, with a requirement to "comply or explain" at the expiry of the six years. During the interim period, the Rule could be amended to include in the disclosure requirement an obligation to explain what progress is being made in achieving the target of at least 30 per cent within the six-year period.

9.4. To ensure consistency with HKEX's previously stated policy that "we continue to focus on diversity *in the broadest sense*[13] (emphasis added), we also recommend that HKEX considers what progress has been made in achieving board diversity in aspects other than gender (such as social or ethnic background), and whether measures to encourage increased board diversity in these other aspects should also be considered.

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[11] HKICS *Missing Opportunities? A Review of Gender Diversity on Hong Kong Boards* (February 2021), foreword.

[12] Note 11 above, p 31.

[13] Consultation Conclusions in respect of HKEX's Consultation Paper *Review of the Corporate Governance Code and Related Listing Rules* (2017) para 11.

10. **Question 6(b):** *Do you agree with our proposal to introduce a MDR requiring all listed issuers to set and disclose numerical targets and timelines for achieving gender diversity at both: (a) board level; and (b) across the workforce (including senior management)?*

    10.1. As regards diversity at board level, this question is addressed in our answer to Question 6(a) above. Regarding diversity across the workforce generally, setting and achieving numerical targets and timelines is a much more challenging task, especially for large issuers which may have diverse businesses and operate in numerous jurisdictions. We recommend that the short-term focus should be on achieving a substantial increase in diversity at board level, before considering how diversity across the workforce can be increased.

11. **Question 6(c):** *Do you agree with our proposal to introduce a CP requiring the board to review the implementation and effectiveness of its board diversity policy annually?*

    11.1. Yes. Given that the current rules require issuers to have a board diversity policy, and to disclose the policy in their CG report, [14] we believe it is reasonable to expect issuers to review the implementation and effectiveness of the policy annually. We therefore support this proposal.

12. **Question 6(d):** *Do you agree with our proposal to amend the relevant forms to include directors' gender information?*

    12.1. Given our answer Questions 6(a) above, we agree that this information would be useful to include in the forms. However, consideration should be given to any sensitivities that may arise from singling- out gender, at the expense of other elements of diversity such as ethnic background, and the omission from the forms of any reference to transgender persons. It may therefore be worth consulting the Equal Opportunities Commission before finalising these forms.

13. **Question 7:** *Do you agree with our proposal to upgrade a CP to Rule requiring issuers to establish a NC chaired by an INED and comprising a majority of INEDs?*

    13.1. It is not clear from the Paper why the current CP needs to be "upgraded", i.e., made more stringent, by turning it into a Rule. As noted in our General Comments above, existing provisions should generally only be made more stringent if this is necessary to ensure compliance. The figures cited by the Paper itself suggests that this is not the case. In the CG Disclosure Analysis (covering 2019) HKEX found that *95 per cent* of the sample issuers had established a NC with majority INEDs and chaired by the board chairman in compliance with the CP,[15] and it is quite possible that this percentage has increased since then. Moreover, although the position in other jurisdictions is not a determining factor, the Paper itself notes that Australia, Singapore and the UK operate these provisions on a "comply or explain" basis: we do not see a need for Hong Kong to adopt a more stringent position.[16] We therefore do not support this proposal.

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[14] Note11 above.
[15] Para 90.
[16] Para 93.

13.2. Although not raised as a question, the Paper states that HKEX "will set out in the guidance the expected disclosures regarding INED nomination and appointment". These disclosures would include "the channels used in searching for appropriate INED candidates (whether through search firms, advertisements or personal network)".[17] With respect, we submit that the disclosure of this information is unnecessary, and a requirement to do so unduly intrusive. How an issuer finds appropriate INED candidates may also be commercially sensitive and confidential. We would therefore recommend that this information is not included in the list of matters which issuers are expected to disclose, and that HKEX's proposed guidance is subject to a market consultation before it is finalised.

14. **Question 8:** *Do you agree with our proposal to upgrade a CP to a MDR to require disclosure of the issuer's shareholders communication policy (which includes channels for shareholders to communicate their views on various matters affecting issuers, as well as steps taken to solicit and understand the views of shareholders and stakeholders) and annual review of such policy to ensure its effectiveness?*

14.1. As the Paper notes, a CP currently provides that issuers should establish a shareholder communication policy, and review it on a regular basis to ensure its effectiveness.[18] It is not clear from the Paper why this CP needs to be "upgraded", i.e., made more stringent, by turning it into a MDR requiring disclosure of the shareholder communication policy and an annual review of its effectiveness. For example, is it because issuers are not complying with the current CP? The CG Disclosure Analysis[19] did not identify this CP as one on which there were major compliance concerns. Is it because they have a shareholders' communications policy but are not disclosing it? This would seem unlikely: it would seem to defeat the purpose of having a shareholder communications policy if shareholders are not informed what it is. Even if this were the case, this issue could be addressed merely by amending the existing CP.

14.2. In the absence of such a justification, we do not support this proposal.

15. **Question 9:** *Do you agree with our proposal to introduce a Rule requiring disclosure of directors' attendance in the poll results announcements?*

15.1. Yes. We agree with the justification for this proposal, namely that it may be useful for shareholders to have a more-timely directors' attendance record than exists at present (where the record is only available annually), to assess directors' commitment to the issuer's affairs.

16. **Question 10:** *Do you agree with our proposal to delete the CP that requires issuers to appoint NEDs for a specific term?*

16.1. Yes. We agree that this CP is superfluous, given the existence of the CP that every director should be subject to retirement by rotation at least once every three years in any case. It should therefore be deleted, as proposed. As noted in our General

[17] Para 94.
[18] Para 96.
[19] Published by HKEX in December 2020, and covering the year 2019.

Comments, regulatory requirements should only be introduced or maintained where their benefits exceed their costs: this is not the case with the Specific Term CP.

17. **Question 11:** *Do you agree with our proposal to elaborate the linkage in the Code by (a) setting out the relationship between CG and ESG in the introductory section; and (b) including ESG risks in the context of risk management under the Code?*

17.1. Yes. We agree with this proposed clarification, as it will make the relationship between CG and ESG more readily comprehensible to issuers and should therefore facilitate compliance.

18. **Question 12:** *Do you agree with our proposal to amend the Rules and the ESG Guide to require publication of ESG reports at the same time as publication of annual reports?*

18.1. The Paper notes the concerns that were expressed in response to the 2019 ESG consultation that aligning date of the publication of the ESG report with that of the annual report would place a strain on issuers' time and resources, resulting in lower reporting quality. At one end of the spectrum, this is a challenge for small and medium- cap issuers which have less resources to produce the reports simultaneously. At the other end of the spectrum, large issuers with multiple businesses operating in multiple jurisdictions also find this very challenging. By concluding after the 2019 consultation that the publication deadline for the ESG report be shortened to five months after the end of the financial year, rather than aligning with that of the annual report, HKEX appeared to imply that these concerns outweighed the benefits to be gained from aligning the publication dates.

18.2. The Paper does not explain how this cost-benefit equation has now changed, such as to now justify aligning the reporting dates. The concerns about the strain on issuers' time and resources remain. In the absence of such a justification, we do not support this proposal.

19. **Question 13:** *Do you have any comments on how the re-arranged Code is drafted in the form set out in **Appendices III** and **IV** to this paper and whether it will give rise to any ambiguities or unintended consequences?*

19.1. We do not have any comment at this stage on these matters. However, we recommend that in the future consultation exercise, HKEX undertakes a comprehensive review of the Listing Rules, including the Code, with a view to removing any provisions that are unnecessary, superfluous or outdated (in the same way that it did recently with shareholder protection provisions in its consultation paper on the listing regime for overseas issuers[20]). This would minimise the regulatory burden on issuers, and facilitate compliance, while still achieving the appropriate regulatory objectives. We would welcome the opportunity to respond to such a consultation.

20. **Question 14:** *In addition to the topics mentioned in this paper, do you have any comments regarding what to be included in the CG GL which may be helpful to issuers for achieving the Principles set out in the Code?*

20.1. See our response to Question 13 above.

[20] *Consultation Paper on Listing Regime for Overseas Issuers* para 138.

21. **Question 15(a):** *Do you agree with our proposed implementation dates for all proposals (except the proposals on Long Serving INED): financial year commencing on or after 1 January 2022;*

21.1. As the responses to the Paper are due to be submitted by 18 June 2021, and we believe HKEX will need a reasonable period of time thereafter to consider the responses to the Paper and determine its consultation conclusions, we believe that the proposed implementation date of financial year commencing on or after 1 January 2022 (for those of the proposals which we support- see above) is too soon. It should be changed to financial year commencing on or after 1 January 2023, to give issuers sufficient time to prepare for any changes.

22. **Question 15(b):** *Do you agree with our proposed implementation dates for proposals on Long Serving INED: financial year commencing on or after 1 January 2023?*

22.1. For those proposals on Long Serving NEDs in Question 4 that we support (namely, Question 4(a)ii and Question 4(b) respectively on additional disclosure, and disclosing the length of tenure of the Long Serving INEDs on the board on a named basis in the shareholders' circular), we agree that the implementation date should be financial year commencing on or after 1 January 2023.

HKGCC Secretariat
June 2021