March 2020

LEADERSHIP ROLE AND ACCOUNTABILITY IN ESG

Guide for Board and Directors

Contents

Introduction

On 17 May 2019, The Stock Exchange of Hong Kong Limited ("Exchange") published a "Consultation Paper on Review of the Environmental, Social and Governance Reporting Guide and Related Listing Rules" on proposed changes to the Environmental, Social and Governance ("ESG") reporting requirements. Following strongly supportive responses to this consultation, the Exchange concluded to amend the ESG Reporting Guide[1] and related Listing Rules in December 2019.

It is important to note that the new ESG reporting requirements focus on the board's governance and roles, rather than "technical reporting". An effective governance structure of ESG matters is fundamental to quality ESG performance and reporting. The board should identify and evaluate ESG risks and opportunities in the context of the issuer's strategic objectives.

This guide provides guidance to you, as the board of directors, on:

(i) Your role in the governance of ESG matters, and action steps relating to ESG governance structure for your self-assessment, under the new ESG reporting requirements;

(ii) Key steps for materiality assessment process, and your role in the process,

(iii) What you should focus on regarding climate-related risks; and

(iv) Potential impact of social issues on your company.

The role of the Board

As the board of directors, you should take leadership for and accountability in:

- Overseeing the assessment of your company's environmental and social impacts.
- Understanding the potential impact and related risks of ESG issues on your company's operating model.
- Aligning with what investors and regulators expect and require.
- Enforcing a materiality assessment and reporting process to ensure actions are well followed through and implemented.
- Promoting a culture from the top-down to ensure ESG considerations are part of the business decision-making process.

Implementation of the new ESG reporting requirements

The new requirements will become effective for financial years commencing on or after 1 July 2020. While the actual reporting will be done at a later stage, companies must set up their governance structure, refine relevant policies/systems/processes as soon as possible, to enable the eventual reporting.

[1] Appendix 27 to the Main Board Listing Rules or Appendix 20 to the GEM Listing Rules.

ESG reporting approach

There is no "one-size-fits-all" framework for ESG reporting. We would like to reiterate and remind issuers that for a "comply or explain" provision, issuers are required to report on the provision, or provide considered reasons why information in respect of the provision has not been reported.

It is important for issuers to ascertain the ESG issues that are most material to them from the outset. This helps put the company in a better position to report and address those risks as necessary, which in turn leads to greater investor confidence. For instance, if an Aspect in the ESG Reporting Guide is considered not material to an issuer's business, the issuer does not need to disclose but should explain in the ESG report that no disclosure is made because such Aspect is not material to its business. Such explanation is sufficient to meet the "comply or explain" requirement.

Section 1: The New ESG Reporting Requirements and Directors' Roles

The new ESG reporting requirements

Mandatory disclosure of a board statement including:

- Board's oversight of ESG issues
- Board's ESG management approach and strategy; process used to evaluate, prioritise and manage ESG issues (including risks)
- Board's review of progress made against ESG goals and targets; how they relate to the issuer's business

Mandatory disclosures, to explain

- "Reporting principles": application of materiality, quantitative and consistency; e.g. how are material ESG factors selected?
- "Reporting boundary": process used to identify which entities or operations are included in the ESG report.

"Environmental" Subject Area

- (New) "climate change" Aspect:
  - Climate-related issues that have impacted and those which may impact the issuer
  - Steps taken to manage the climate-related issues
- KPIs revised: Disclosure of targets, and action steps

"Social" Subject Area

- All KPIs upgraded to "comply or explain"
- (New) supply chain KPIs
- (New) anti-corruption KPI: training to directors and staff

Shortened timeframe for ESG reporting

- Within five months after the financial year-end

No printed form of ESG reports

- For standalone ESG reports only
- Save per shareholder special request

Encourage independent assurance

Director's roles

Every Hong Kong listed company has reported on ESG issues for a few years by now. To what extent do the new ESG reporting requirements require you as a director to step up your leadership role in ESG and ensure that issues are discussed at the board level?

Action steps for directors

In this section, we set out action steps and questions for directors' quick self-assessment. Adapted from "TCFD Implementation Guide"[1] , these action steps are relevant to climate change as well as ESG generally. These are supplemented by examples[2] and references to resource materials.

Where appropriate, your management team should also provide the necessary status update, analyses, and proposed way forward for board discussion. You, as a director, should bear in mind the following two key questions when going through each action step:

Where are we and what should we do?

What should the management provide for board discussion?

A consolidated list of all the action steps and questions is set out in the Appendix: List of Self-Assessment Questions for directors' ease of reference.

Step 1 Secure the support of our board of directors and executive leadership team.

Where are we and what should we do?

- As a board, do we understand the new ESG reporting requirements?
- Would this significantly impact our company?

What should the management provide for board discussion?

- Management (including company secretary) to organise a board briefing, followed by a broad gap analysis and a proposal on general directions forward. Further board discussions on specific themes can be held later, as appropriate.

[1] "TCFD Implementation Guide" published by Climate Disclosure Standards Board and Sustainability Accounting Standards Board. "TCFD" is the abbreviation for the Task Force on Climate-related Financial Disclosures.

[2] Practising Governance Limited was engaged as a consultant, including providing examples extracted from award-winning sustainability reports.

RESOURCES

The Exchange's directors e-training:

1. ESG Governance and Reporting – for information of the Exchange's ESG reporting framework and the board's leadership role in ESG matters
2. Exchange's New ESG Requirements – for the new ESG reporting requirements and the board's responsibilities under the new requirements

Step 2 Integrate ESG (including climate-related) issues into key governance processes, enhance board-level oversight.

Where are we and what should we do?

- As a board, do we need a more structured approach to ESG (including climate-related) issues, given the new reporting requirements (including review of ESG targets)?
- Would our board need the help of board committees? Should we establish a new ESG committee? Or expand the roles of an existing committee?
- What is the impact on the roles of other committees (e.g. audit, risks)?
- What should be the key terms of reference for the committee? Frequency and form of reporting to our board?
- (Where there are various business units/multiple operating locations/jurisdictions) different business units in various locations/jurisdictions may have their own circumstances. Do we need group-level policies for high-level guiding principles?

What should the management provide for board discussion?

- Management (including company secretary) to provide a proposal (including analysing the pros and cons of alternative governance approaches).

EXAMPLE

On board committees and terms of reference

Example 1
CLP Holdings

Sustainability Report 2018, P.25:

- Roles of its dedicated sustainability committee include:
  - reviewing, endorsing, and reporting to the board on the group's sustainability standards, priorities and goals; overseeing group-level strategies to attain the same
  - overseeing, reviewing, and evaluating CLP's sustainability performance
  - reviewing and advising the board on the group's reporting
  - at least two meetings annually
- Roles of audit & risks committee:
  - ensuring data in the group's sustainability reports (including external assurance obtained) are appropriate
- Terms of reference available on website

Step 3 Bring together sustainability, operations, finance, compliance, investor relations colleagues to agree on respective roles.

Where are we and what should we do?

- Do we have an executive-level ESG working group with authority and expertise, to assess and manage ESG (including climate-related) issues?
- Apart from (if applicable) a dedicated sustainability officer, do we have the input and support of operating units[3]?
- What are the roles of other teams (e.g. finance, internal audit/risk management, legal/secretarial, investor relations, human resources)? Any silo issues affecting team effectiveness?
- Any terms of reference for the working group? Frequency of meetings and internal reporting of the working group[4]?
- Does the working group report to our board? If so, how frequent?
- Does the working group have adequate resources?

What should the management provide for board discussion?

- Management to provide an analysis and recommendations on whether the current structure may need to be enhanced, sufficiency of resources dedicated to ESG issues and proposed way forward.

Step 4 Solicit feedback from engaged investors and other key stakeholders, about their views on ESG–related (including climate-related) risks and opportunities.

Where are we and what should we do?

- How did our company engage with its stakeholders? How can this process be improved?
- Have we been informed of the latest feedback from our major investors and other key stakeholders as regards our reporting on ESG issues?
- What are the ESG trends among investors generally?
- Do we understand how ESG may impact on our investors' voting or investment decisions?

What should the management provide for board discussion?

- Management (including investor relations) to provide the latest feedback of major investors and key stakeholders, and proposed enhancements. ESG trends among investors generally should also be highlighted.

EXAMPLE

See "Section 2: Materiality Assessment" below, example 9 on stakeholder engagement.

[3] See "Section 4: Social KPIs" below for operating units' input.

[4] The board's annual review of adequacy of resources for the accounting/internal audit/financial reporting function should include ESG performance and reporting. See Code Provision C.2.2, Corporate Governance Code (FAQ Series 17, no. 24L).

RESOURCES

See the Securities and Futures Commission's Survey on Integrating Environmental, Social and Governance Factors and Climate Risks in Asset Management, December 2019, for more information on investor trends.

Step 5 "Materiality": has the board discussed and determined the most important ESG (including climate-related) issues?

Where are we and what should we do?

- What is our latest list of material ESG issues? How was it determined, and when?
- Does it need refinement?
- Have we discussed climate-related issues?
- Has our company been conducting materiality assessment systematically and reporting material ESG issues under the existing ESG requirements?
- Should we focus on a few key issues instead of a long list?
  (Note: See "Section 2: Materiality Assessment" for further details on materiality assessment and the board's roles (including the "validation" process). As set out in the Introduction, if a "comply or explain" provision is not material to the company, an explanation to that effect may be appropriate.)

What should the management provide for board discussion?

- Management to provide an analysis to explain its materiality assessment process and results, and its current list of material issues as well as climate-related issues.

The following examples illustrate how some companies identified the most material issues based on their own strategies.

EXAMPLES

Example 2
CLP Holdings

Sustainability Report 2018, see table of contents:

- As part of its efforts to become a "utility of the future", key areas identified include: climate change, technology, cyber resilience and data protection, workforce
- A separate section on "standard disclosures" (addressing important but less material topics)

EXAMPLES

Example 3
Chow Tai Fook Jewellery Group

Sustainability Report 2019, see table of contents:

- Under its sustainability strategy, priority areas are: responsible sourcing; craftsmanship, innovation & technology; resource efficiency & carbon reduction; people focused

Step 6 Has the board discussed how the ESG (including climate-related) issues identified affect our overall strategy, including risk management?

Where are we and what should we do?

- What are the most important ESG issues (including risks) to our company? In terms of legal, operations (e.g. offices and production plants are forced to close down in case of extreme weather conditions like "super typhoons"), and reputation (e.g. younger generation may place a higher priority on ESG issues)?
- How would these risks affect our business strategy (e.g. as younger customers begin to drive major purchasing decisions)?
- What have our peers or industry been doing in terms of their ESG risks and strategy?

Reminder: *Companies should not lose sight of the opportunities side, for example, those brought by changes in customer preferences.*

What should the management provide for board discussion?

- Management to prepare an analysis on how the material ESG issues identified in Step 5 above relate to the company's strategy (including business and CSR strategy), vision and values.

The following examples illustrate how some companies considered ESG issues in their strategies.

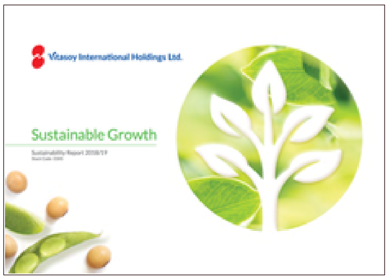
EXAMPLES

Example 4
CLP Holdings

Sustainability Report 2018, P.2:

- Please refer to example 2 under Step 5 above
- Further explains how the changing public expectations impact on its development towards "utility of the future"
  - When it was founded in 1901, public expectations were on reliability and affordability of power
  - Public expectations now extend to include environmental matters

Example 5
Vitasoy International Holdings



Sustainability Report 2018, P.3, 26:

- Mission: to provide sustainable plant-based nutrients good for health and the environment
- Growing concerns about the world's climate and population challenges
- Strategy includes increasing its plant-based products

Example 6
VTech Holdings

Sustainability Report 2019, P.18:

- Context: increasing global awareness of people's health and lifestyle
- Innovative designs and functionality elements in developing products that could help customers live with ease and safety

RESOURCES

See Session 2 of the Exchange's directors e-training "Exchange's New ESG Requirements" for sources of information for management's analysis.

Step 7 Risk management: do our existing risk management processes take account of ESG risks?

Where are we and what should we do?

- Are ESG risks considered as part of our risk management?
- Do we know whether our business units have sufficient awareness of ESG risks they face? Are they able to identify the risks and escalate them to the board?
- Does the board have adequate awareness of ESG risks faced by the industry? Is additional training required?
- ESG-related crises: are escalation procedures and business continuity plans in place?

What should the management provide for board discussion?

- Management (including internal audit/risks) to provide an analysis on how the process to evaluate and determine material ESG risks in Step 5 above is linked to the company's overall enterprise risk management system; and possible enhancements to the company's enterprise risk management system.

EXAMPLE

Example 7
Swire Pacific

Sustainability Report 2018, P. 11:

- Risk management structure
  - the board
  - group risk management committee reports on sustainability risks and performance
  - in turn advised by group sustainability committee
  - six underlying working groups covering focus areas of its sustainability vision (e.g. sustainable materials; climate resilience)
- Relevant policies available on website; including climate change policy

RESOURCES

See the Committee of Sponsoring Organizations of the Treadway Commission and World Business Council for Sustainable Development's Applying Enterprise Risk Management to Environmental, Social, and Governance Risks, October 2018 for a useful framework to manage ESG risks in the context of overall enterprise risk management.

In particular, see the section headed "4. Review and revision for ESG-related risks" for a discussion on the identification and assessment of internal and external changes that may considerably affect the company's strategy or business objectives.

Step 8 Set goals and monitor performance

Where are we and what should we do?

Our company has been reporting on Environmental KPIs for a few years under the current Listing Rules requirements.

- What has been our Environmental KPIs performance? Why?
- Has our board approved any Environmental, and/or other ESG targets in the past?
- Our board needs to set and disclose targets for Environmental KPIs A1.5, 1.6, 2.3 and 2.4[5] if they are considered to be material following a materiality assessment. Should we also set targets for other ESG areas, e.g. Social Aspects if they are material to us?
- Depending on factors like materiality and our ambition, should we set quantitative or directional targets?
- What should be the timeframe for achieving the targets (short-term, medium-term, long-term)?
- What should be the frequency, and form of reporting to our board, for monitoring progress?

What should the management provide for board discussion?

- Management to prepare update and analyses, including evaluating progress in achieving goals and industry benchmark.

[5] These KPIs relate to emissions, waste reduction, energy use and water efficiency.

RESOURCES

For target setting, refer to:

1. Section headed "Step-by-step guide to ESG reporting - Step 5 Target setting" of the Exchange's How to Prepare an ESG Report, March 2020 ("Step-by-step Guide")
2. Session 4 of the Exchange's directors e-training "Exchange's New ESG Requirements"

Step 9 Look at existing tools you may already use to collect data for ESG reporting, are there any gaps with the new ESG reporting requirements?

Where are we and what should we do?

- Are our current reporting systems and tools sufficient to enable reporting on the new Aspect on climate change?
- Are our current reporting systems and tools sufficient to enable reporting on all Social KPIs (including the new KPIs under the supply chain management and anti-corruption Aspects)?
- Do we need to do more work, such as determining the appropriate approach and setting up the system for climate change reporting? Do we have enough expertise in-house?
- Or is it a matter of consolidating and communicating what we already have? For example, various departments may already collect data on some Social KPIs (say employee-related ones), ready to be consolidated and communicated?
- Should we consider seeking external assurance for all or part of data reported on?

What should the management provide for board discussion?

- Management to provide a detailed gap analysis and proposed enhancement in reporting infrastructure to fulfil the new ESG reporting requirements.

RESOURCES

See section headed "Step-by-step guide to ESG reporting - Step 2 Understanding the requirements of the Guide" of the Exchange's Step-by-step Guide.

Section 2: Materiality Assessment

Introduction

- The revised ESG reporting requirements clarify that the board determines materiality which is:
  - the threshold at which ESG issues, determined by the board, are "sufficiently important to investors and other stakeholders" that they should be reported
- Noteworthy observations under the Exchange's latest review of ESG reports:
  - importance of conducting a materiality assessment
  - some companies may not have "thoroughly determined" whether an ESG reporting provision is material to them
  - some companies chose to "comply" with ESG reporting provisions which do not appear to be relevant to them
  - the Exchange stressed that if a "comply or explain" provision is not material to the company, an explanation to that effect may be appropriate. "To explain" is not a less preferred option

Key components in materiality assessment

As seen in the previous section, directors should discuss materiality, and solicit feedback from stakeholders (Step 4).

The following examples illustrate some key components of these processes; and roles of directors in such processes.

Detailed guidance on how to conduct a materiality assessment, including stakeholder engagement, is set out in other Exchange's resources listed below. Broadly, it involves (i) internal assessment as well as (ii) external assessment. For the latter, stakeholder engagement is an important tool that companies can use to achieve participation of stakeholders in identifying, developing, and achieving accountable and strategic responses to ESG issues.

1. Identification

Many useful resources can assist us in identifying potential material issues for further assessment. A list of potential issues can be compiled based on the company's on-going and previous stakeholder engagement, corporate strategy as well as risk priorities, with reference to established material topics in the relevant industry and global guidelines.

RESOURCES

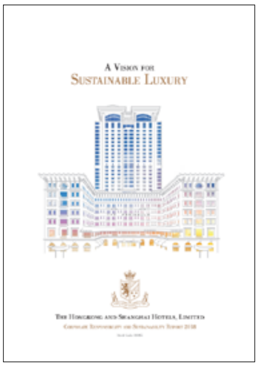
Refer to:

1. "Step-by-step guide to ESG reporting - Step 4 Materiality assessment" of the Exchange's Step-by-step Guide and its Appendix 1: Toolkit.
2. The Sustainability Accounting Standards Board's Materiality Map®.

The following example illustrates some possible tools, and that the process may continue to evolve.

EXAMPLE

Example 8
The Hong Kong and Shanghai Hotels



Corporate Responsibility and Sustainability Report 2018, P.8:

- Explains how its materiality assessment process continues to evolve
- In 2017, in addition to stakeholder engagement, it started identifying key issues based on thought leadership studies and benchmarking, Including publications of:
  - leading organisations (e.g. World Economic Forum)
  - organisations relating to industry performance (e.g. The World Travel and Tourism Council)

2. Prioritisation and stakeholder engagement

The Exchange's Step-by-step Guide provides information on conducting stakeholder engagements, including how to prioritise groups of stakeholders (internal and external); methods of engagement; and useful tools (e.g. materiality matrix). Since stakeholder engagement should be part of a company's everyday operations, it is not necessary to conduct a stakeholder engagement specifically for the purpose of preparing its ESG report.

The following example illustrates how the process was conducted in practice.

EXAMPLE

Example 9
The Hong Kong and China Gas Company

Sustainability Report 2018, P. 31:

- Both regular engagement as well as the special annual engagement exercise
- Identify key stakeholder groups (including employees, contractors and suppliers, investors, professional bodies/regulators, customers, local communities; NGOs)
- Tools: online surveys; interviews; focus group discussions
- Concerns of various groups; and how these are addressed by the company

3. Validation

Validation is an important step after stakeholder engagement where the board reviews and confirms findings of the stakeholder engagement conducted. Validation can also be conducted by senior management under the board's supervision. However, the board remains ultimately responsible for the process and outcomes of the materiality assessment.

The following examples illustrate validation actions taken by companies and the outcome.

EXAMPLES

Example 10
MTR Corporation

Sustainability Report 2018, P. 7:

- Its materiality assessment process includes: (i) identification of sustainability reporting issues; (ii) importance to the corporation under its enterprise risk management system; (iii) stakeholder engagement; and (iv) endorsement by corporate responsibility steering committee
- Outcome: e.g. during the endorsement process, ranking of some health and safety related issues was uplifted to reflect the company's priority in putting safety first

EXAMPLES

Example 11
Swire Pacific

Sustainability Report 2018, P. 107, 109:

- In the validation phase, senior managers (including sustainable development, risk management, human resources, public affairs and legal) reviewed and confirmed findings of stakeholders engagement
- Outcome: e.g. talent recruitment/retention not ranked as highly by stakeholders as in past years; nonetheless included given its significance to the group's commitment as an employer of choice (to its 93,000 employees)

Section 3: Climate Change

Introduction

Climate change-related impacts present financial risks to many, if not all sectors, in which our issuers operate. The new ESG reporting requirements, in line with the recommendations of the Task Force on Climate-related Financial Disclosures ("TCFD"), focus on disclosure of risks relating to climate change, their impacts, and mitigating steps.

Types of climate-related risks

TCFD highlights two primary types of climate-related risks:

- **Physical risks**
  - Physical risks may have financial implications for organisations such as business and supply chain disruption, and direct damage to assets. It can be further divided into acute physical risk and chronic physical risk:
    - Acute physical risk is event-driven, including extreme weather events such as droughts, floods or hurricanes.
    - Chronic physical risk is the long-term impact of climate change, such as increasing average global mean temperatures and sea level rise.
- **Transition risks**
  - Transition risks occur during the global transition to a low-carbon economy with new regulations, innovations in energy efficiency and market changes.
  - These risks may impact the structure of a business. Revenues may be affected by shifting customer demands and new regulations. Costs can be impacted by the availability and price of raw materials.

Action steps for directors

The action steps and self-assessment questions set out in Section 1 apply to climate-related issues as well. As investors are particularly concerned as to the financial impacts of climate change, directors should further ask these additional questions[6] in relation to risk management (Step 7):

What are the company's climate-related risks?

Particularly in terms of their financial impacts and how it relates to revenues, expenditures, assets, liabilities, and financial capital?

The following examples illustrate the risks aspects of climate change, as disclosed by some companies. However, it should be noted that climate change may provide opportunities as well.

---

[6] Adapted from "TCFD Implementation Guide" published by the Climate Disclosure Standards Board and the Sustainability Accounting Standards Board.

EXAMPLES

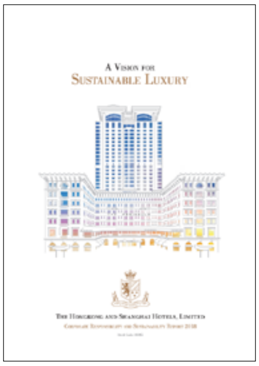
Climate change policy

Example 7
Swire Pacific

Climate change policy available on website.

Risks: physical risks, mitigating steps

Example 12
The Hong Kong and Shanghai Hotels



Corporate Responsibility and Sustainability Report 2018, P. 30:

- On physical risks aspects- e.g. flooding, extreme weather events which are also addressed in its risk management report
- Mitigation: insurance; enhancing building structure resilience (via design, build, maintenance); site and company level crisis management teams

Risks: transition risks, mitigating steps

Example 13
HSBC Holdings

Annual Report 2018, P. 29:

- Addressed both physical risks and transition risks
- Transition risks
    - the possibility that a customer's ability to meet its financial obligations will deteriorate due to the global movement from a high-carbon to a low-carbon economy
- Mitigation:
    - e.g. identified six higher transition risk sectors based on their contribution to global carbon dioxide emissions, including oil and gas, metals and mining
    - e.g. working to embed transition risk into the day-to-day credit management

Section 4: Social KPIs

Introduction

Potential impact of social issues on a company may be of no less significant than environmental risks. Understanding the social risks affecting the company can help minimise any adverse impact brought to the company.

From voluntary to "comply or explain"

Under the new ESG reporting requirements, the disclosure obligation of all Social KPIs[7] has been upgraded from voluntary to "comply or explain". The change aims to emphasise equal treatment of environmental and social risks and raise issuers' awareness of the possible impacts resulting from social issues.

Reminder: *If any of the Social KPIs is not considered to be material to an issuer's businesses, the issuer should explain rather than make irrelevant disclosures.*

New Social KPIs

The new ESG reporting requirements also introduced new KPIs under supply chain management and anti-corruption Aspects. The examples below illustrate actions taken by some companies to address the new Social KPIs including way forward.

[7] There are eight Aspects under Subject Area "Social". They are: Employment, Healthy and Safety, Development and Training, Labour Standards, Supply Chain Management, Product Responsibility, Anti-corruption and Community Investment.

1. Supply chain management

The new KPIs on supply chain management require disclosure of:

(i) practices used to identify environmental and social risks along the supply chain, and the implementation and monitoring of such practices; and

(ii) practices used to promote environmentally preferable products and services when selecting suppliers, and the implementation and monitoring of such practices.

The operations team should be involved in assessing and formulating action plans regarding this area. The following example illustrates the actions taken by a company, their evolution, and way forward.

EXAMPLE

Example 14
Vitasoy International Holdings

Sustainability Report 2018, P.38:

- "Responsible sourcing" identified as one of the top material issues following stakeholder feedback and materiality assessment
- Tools: first developed "supplier responsibility principles" and later on "responsible procurement policy"; current scope includes direct materials. Will introduce self-assessment of suppliers next year
- Priority in selection process to products/services certified by recognized authorities (e.g. Forest Stewardship Council); the goal is to evaluate and review all suppliers with consistent criteria during selection process

2. Anti-corruption

A new KPI on anti-corruption is added to require disclosure of anti-corruption training provided to directors and staff.

The company's relevant teams (e.g. legal, internal audit/risk management, human resources) should be involved in assessing and formulating action plans regarding this area.

EXAMPLE
Staff training

Example 15
HSBC Holdings

Annual Report 2018, P. 26:

- Zero tolerance for bribery and corruption
- Comply with all anti-bribery and corruption laws in all markets it operates
- Have a global anti-bribery and corruption policy, which gives practical effect to global initiatives (e.g. United Nations Global Compact , Principle 10)
- Mandatory e-training for all employees; more than 12,000 employees who undertake activities with a high risk of bribery received targeted role-based training

Appendix: List of Self-Assessment Questions

Step 1 Secure the support of our board of directors and executive leadership team.

Where are we and what should we do?

- As a board, do we understand the new ESG reporting requirements?
- Would this significantly impact our company?

What should the management provide for board discussion?

- Management (including company secretary) to organise a board briefing, followed by a broad gap analysis and a proposal on general directions forward. Further board discussions on specific themes can be held later, as appropriate.

Step 2 Integrate ESG (including climate-related) issues into key governance processes, enhance board-level oversight.

Where are we and what should we do?

- As a board, do we need a more structured approach to ESG (including climate-related) issues, given the new ESG reporting requirements (including review of ESG targets)?
- Would our board need the help of board committees? Should we establish a new ESG committee? Or expand the roles of an existing committee?
- What is the impact on the roles of other committees (e.g. audit, risks)?
- What should be the key terms of reference for the committee? Frequency and form of reporting to our board?
- (Where there are various business units/multiple operating locations/jurisdictions) different business units in various locations/jurisdictions may have their own circumstances. Do we need group-level policies for high-level guiding principles?

What should the management provide for board discussion?

- Management (including company secretary) to provide a proposal (including analysing the pros and cons of alternative governance approaches).

Step 3 Bring together sustainability, operations, finance, compliance, investor relations colleagues to agree on respective roles.

Where are we and what should we do?

- Do we have an executive-level ESG working group with authority and expertise, to assess and manage ESG (including climate-related) issues?
- Apart from (if applicable) a dedicated sustainability officer, do we have the input and support of operating units?
- What are the roles of other teams (e.g. finance, internal audit/risk management, legal/secretarial, investor relations, human resources)? Any silo issues affecting team effectiveness?

- Any terms of reference for the working group? Frequency of meetings and internal reporting of the working group?
- Does the working group report to our board? If so, how frequent?
- Does the working group have adequate resources?

What should the management provide for board discussion?

- Management to provide an analysis and recommendations on whether the current structure may need to be enhanced, sufficiency of resources dedicated to ESG issues and proposed way forward.

Step 4 Solicit feedback from engaged investors and other key stakeholders, about their views on ESG –related (including climate-related) risks and opportunities.

Where are we and what should we do?

- How did our company engage with its stakeholders? How can this process be improved?
- Have we been informed of the latest feedback from our major investors and other key stakeholders as regards our reporting on ESG issues?
- What are the ESG trends among investors generally?
- Do we understand how ESG may impact on our investors' voting or investment decisions?

What should the management provide for board discussion?

- Management (including investor relations) to provide the latest feedback of major investors and key stakeholders, and proposed enhancements. ESG trends among investors generally should also be highlighted.

Step 5 "Materiality": has the board discussed and determined what are our most important ESG (including climate-related) issues?

Where are we and what should we do?

- What is our latest list of material ESG issues? How was it determined, and when?
- Does it need refinement?
- Have we discussed climate-related issues?
- Has our company been conducting materiality assessment systematically and reporting material ESG issues under the existing ESG requirements?
- Should we focus on a few key issues instead of a long list?

What should the management provide for board discussion?

- Management to provide an analysis to explain its materiality assessment process and results, and its current list of material issues as well as climate-related issues.

Step 6 Has the board discussed whether how the ESG (including climate-related) issues identified is an important component of our overall strategy, including risk management?

Where are we and what should we do?

- What are the most important ESG issues (including risks) to our company? In terms of legal, operations (e.g. offices and production plants are forced to close down in case of extreme weather conditions like "super typhoons"), and reputation (e.g. younger generation may place a higher priority on ESG issues)?
- How would these risks affect our business strategy (e.g. as younger customers begin to drive major purchasing decisions)?
- What have our peers or industry been doing in terms of their ESG risks and strategy?

What should the management provide for board discussion?

- Management to prepare an analysis on how the material ESG issues identified in Step 5 above relate to the company's strategy (including business and CSR strategy), vision and values.

Step 7 Risk management: do our existing risk management processes take account of ESG risks?

Where are we and what should we do?

- Are ESG risks considered as part of our risk management?
- Do we know whether our business units have sufficient awareness of ESG risks they face? Are they able to identify the risks and escalate them to the board?
- Does the board have adequate awareness of ESG risks faced by the industry? Is additional training required?
- ESG-related crises: are escalation procedures and business continuity plans in place?
- **Re climate change:** What are the company's climate-related risks? Particularly in terms of their financial impacts and how it relates to revenues, expenditures, assets, liabilities, and financial capital?

What should the management provide for board discussion?

- Management (including internal audit/risks) to provide an analysis on how the process to evaluate and determine material ESG risks in Step 5 above is linked to the company's overall enterprise risk management system; and possible enhancements to the company's enterprise risk management system.

Step 8 Set goals and monitor performance

Where are we and what should we do?

- What has been our Environmental KPIs performance? Why?
- Has our board approved any Environmental, and/or other ESG targets in the past?
- Our board needs to set and disclose targets for Environmental KPIs A1.5, 1.6, 2.3 and 2.4[8] if they are considered to be material following a materiality assessment. Should we also set targets for other ESG areas, e.g. Social Aspects if they are material to us?
- Depending on factors like materiality and our ambition, should we set quantitative or directional targets?
- What should be the timeframe for achieving the targets (short-term, medium-term, long-term)?
- What should be the frequency, and form of reporting to our board, for monitoring progress?

What should the management provide for board discussion?

- Management to prepare update and analyses, including evaluating progress in achieving goals and industry benchmark.

Step 9 Look at existing tools you may already use to collect data for ESG reporting, are there any gaps with the new ESG reporting requirements?

Where are we and what should we do?

- Are our current reporting systems and tools sufficient to enable reporting on the new Aspect on climate change?
- Are our current reporting systems and tools sufficient to enable reporting on all Social KPIs (including the new KPIs under the supply chain management and anti-corruption Aspects)?
- Do we need to do more work, such as determining the appropriate approach and setting up the system for climate change reporting? Do we have enough expertise in-house?
- Or is it a matter of consolidating and communicating what we already have? For example, various departments may already collect data on some Social KPIs (say employee-related ones), ready to be consolidated and communicated?
- Should we consider seeking external assurance for all or part of data reported on?

What should the management provide for board discussion?

- Management to provide a detailed gap analysis and proposed enhancement in reporting infrastructure to fulfil the new ESG reporting requirements.

[8] These KPIs relate to emissions, waste reduction, energy use and water efficiency.

HONG KONG EXCHANGES AND CLEARING LIMITED

hkexgroup.com | **hkex.com.hk**

8/F, TWO EXCHANGE SQUARE
8 CONNAUGHT PLACE
CENTRAL, HONG KONG
T (852) 2522 1122
F (852) 2295 3106
info@hkex.com.hk