

## 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.

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.

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.

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.

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.

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, but subject to certain qualifications and clarifications (see the detailed response below)

☐ No

Please give reasons for your views.

CP C.2.4 is subject to the “comply or explain” principle. However, sub-paragraph (c) (board acknowledgement as to its responsibility for risk management and internal control), which mirrors principle C.2 (stating the board’s responsibility in this area), should be a mandatory disclosure (Section Q) rather than being subject to the “comply or explain” regime.

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.

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, partially

☐ No

Please give reasons for your views.

We would agree with upgrading the existing recommended disclosure in relation handling and disseminating inside information to a CP, but not to extending this to “other regulatory compliance risks” (the latter requirement is “new”). This is not necessary, as compliance risks are specified elsewhere in the appendix as a category of risks to be covered in the board’s review. Disclosure re: its handling would therefore have been covered by implication in (a) (“the process used to identify, evaluate and manage significant risks”).

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.

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.

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.

We noted that the consultation proposal (e.g., paragraphs 80 and 88) permits the outsourcing of internal audit function. We would suggest that, for the avoidance of doubt, this matter be made more explicit in CP C2.5, by, for example, adding another note, along the lines of the following:

*3 Compliance may be achieved either by way of establishing an in-house internal audit function or outsourcing the function to competent persons.*

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.

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.

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.

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.

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.

Given the substantial changes that some issuers would need to make in order to enhance their risk management and internal control functions, board and audit committee practices, as well as recruiting suitable personnel, a reasonable lead time should be allowed. This would also avoid issuers just adopting a “box-ticking” approach, without genuinely appreciating and adopting the principles underlying the changes. However, issuers should be encouraged to implement the changes early.

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