

July 16, 2023

Dear Sir/Madam  
Hong Kong Exchanges and Clearing Limited

## HKEX Consultation Paper on Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework (April 2023)

On behalf of the Hong Kong Investment Funds Association, I would like to share our views regarding the captioned consultation paper (CP).

### A recap of the HKEX proposals:

HKEX proposes to mandate all issuers to make climate-related disclosures in their ESG reports (i.e. upgrade from the current “comply or explain”). New climate-related disclosures based on the International Sustainability Standards Board (ISSB) Climate Standard will be introduced as a new Part D of Appendix 27; and there will be certain consequential amendments, too. In addition, acknowledging the readiness of issuers and the concerns raised, the HKEX proposes interim provisions for certain disclosures during the Interim Period.

### Our comments:

#### (a) Overall comments -

Hong Kong is amongst the first jurisdictions to transpose the ISSB requirements and we greatly applaud the HKEX for its commitment and dedication to bring this important initiative to the local market in the earliest instance.

With respect to the proposals outlined in the CP, which pertain to addressing climate risks, we are generally supportive, subject to certain areas that can be enhanced/clarified (see (b) on P2). But importantly, we believe that there is a fundamental gap in the HKEX proposals – there is basically no reference to ISSB General requirements Standard (IFRS S1).

IFRS S1 and S2 should go hand-in-hand. S2 has been designed to be applied in the context of S1 and following its architecture and conceptual foundations. Climate disclosures produced in application of S2 without the conceptual and qualitative principles articulated in S1 can potentially result in lack of consistency and comparability. S2 cannot work without the general requirements standards.

While it can be said that Appendix 27 covers issues beyond climate (other environmental issues and social issues), and also contains general requirements and reporting principles regarding presentation and relevance of information, which are consistent with the general features for sustainability reporting under ISSB S1, it falls short of the requirements of S1.

Firstly, S1 defines the concept of materiality and provides useful application guidance, articulating how materiality assessments should be conducted. This is a key overarching concept in S1 that articulates how materiality should be interpreted and applied. In addition, the definition of materiality in Appendix 27 is not fully aligned with that of the S1, spanning to other stakeholders. This may potentially result in diverging materiality assessments and therefore a lack of consistency and comparability in climate and other sustainability disclosures.

In addition to the general requirements and reporting principles included in S1, it also incorporates essential principles in relation to the qualitative characteristics of decision useful information.

Another fundamental aspect covered in S1 relates to the connections between different sustainability risks and opportunities as well as connections with financial information. This key concept is currently lacking in Appendix 27. These connections are essential to underpin investors' understanding of issuers' sustainability risks and opportunities, the interplay between them and their connections with the financial statements.

One area that is currently not covered in the HKEX proposals to update Appendix 27 related to the disclosure of key judgements. Again, this is one fundamental pillar included in S1, which is paramount for investors' understanding of sustainability disclosures.

Finally, while we acknowledge that S2 builds from the core content articulated in S1 building from the TCFD recommendations, and these are incorporated in the HKEX proposals, the provisions in Appendix 27 in relation to other sustainability risks and opportunities are not aligned with these and the disclosure of other sustainability information beyond climate will therefore not render comparable and consistent disclosures. The core content introduced in S1 encompasses fundamental aspects such as the strategy an issuer follows to manage sustainability risks and opportunities or the risk management processes it follows to identify, prioritize or monitor these. We are concerned that such fundamental elements for investors' decision making are not introduced as part of the HKEX proposals.

The CP has not addressed the gaps: the proposals do not mandate disclosures for sustainability-related risks and opportunities beyond climate. Nor are there any proposals to require the sustainability reporting to be aligned with financial statements and that assumptions for climate-related disclosures be consistent with the financial statements to the extent possible. We see as an important shortcoming with respect to how the proposals address the application of the SASB Standards. While the proposals encourage issuers to consider SASB standards, they fall short of S1 which makes it a requirement to consider the standards. This requirement to consider SASB Standards has been included in S1 particularly to assist issuers to identify sustainability-related risks, opportunities and related metrics beyond climate. While Appendix 27 provides certain information on types of environmental or social risks to be disclosed by issuers, other sustainability-related and opportunities may also be material for an issuer and may fall outside of those elements currently captured in Appendix 27.

These are important lynchpins which support the integrity and robustness of the global baseline. They are pivotal to ensure that comparable and meaningful information are provided to investors/users in making capital allocation decisions.

Both IFRS S1 and IFRS S2 (climate-related standards) are important contributions to a multi-year, multi-jurisdictional effort towards improving the availability, quality, comparability, timeliness, and interoperability of sustainability-related disclosures. But in the consultation paper, there is no indication regarding the direction of travel with respect to S1.

At an event held on July 13, a senior representative of HKEX indicated that the CP paves the way towards the adoption of the ISSB standards in HK, when the local standard setter and the local standards come into place, and the market reaches the required maturity. What this entails remain unclear and it is imperative that the HKEX elaborates on this and provides a clear timeline with respect to the adoption of IFRS S1. Ultimately, Hong Kong is a major financial hub and we

should set a high bar and lead by example by providing a clear timeline and credible plan to demonstrate how we can transpose the standards in full.

We are mindful of the resources and capacity requirements for issuers with respect to S1. But there is already a one-year transitional relief provided. Companies will not be required to disclose their non-climate risks and opportunities in the first year of reporting under IFRS S1. This will give entities more time to prepare for reporting on their non-climate risks and opportunities and help them with their initial implementation of the standards. Furthermore, to support companies in providing disclosures in these areas, the ISSB has agreed to introduce the concept of “reasonable and supportable information that is available at the reporting date without undue cost or effort”. With these supporting measures, we believe that there is all the more reason why the HKEX should show the commitment to transpose S1 in the earliest instance.

**(b) Specific comments on key points in the Proposals –**

- **Interim provisions:** The proposed interim provisions is pragmatic as there is a need for flexibility in areas where relevant science, standards, and reporting methodologies are still evolving and may differ across sectors. It would be helpful if the HKEX can review the readiness of issuers to comply (by sector) by the end of the Interim Period. And there is full transparency regarding the review outcome and the next steps.
- **Optional/omitted requirements:** In the proposals, there are a few IFRS S2 requirements that are either optional (e.g. climate-related opportunities and targets) or omitted (e.g. whether targets are certified by a third party). Whilst we understand that there may be legitimate and practical reasons for adopting these approaches, we believe that there should be mechanisms to phase in these requirements, say through a “comply or explain” approach.
- **Industry guidance:** We support the creation of global baseline standards with industry-specific guidance. However, instead of simply encouraging issuers to consider the industry-based disclosure requirements prescribed under other international ESG reporting frameworks, we would suggest the HKEX to align with ISSB to make the disclosure of industry-specific metrics a requirement, while at the same allow issuers to have the flexibility to decide the specific metrics to be used. We also urge the HKEX to work with ISSB and other relevant bodies to continue developing industry-specific guidance.
- **Liability:** A commonly cited reason for reluctance to provide quantitative data is about the potential liability. The liability framework should take into account the dynamic and fluid nature of the ESG landscape; and be calibrated in a proportionate manner. We would exhort the HKEX to adopt a framework that provides meaningful protection from legal liability for disclosures provided in good faith while standards continue to evolve.
- **Compatibility with other standards:** As issuers use a range of reporting standards (such as GRI), it would be helpful if the HKEX can elaborate on how the proposed requirements map and align with other commonly recognized reporting standards. In addition, the ISSB published the Exposure Draft Methodology for Enhancing the International Applicability of the SASB Standards on May 11, 2023. We wish to understand the views of HKEX on the Draft and possible implications to its proposals.

In a nutshell, while the proposals as outlined in the CP are an important step forward; we wish to stress that the proposals, as they currently stand, would not be sufficient to enable the provision of information to inform global comparisons. S1 and S2 should come together. The key is for the issuers to start the journey asap, to demonstrate commitment and to continually show progress on the strategies going forward. We would be keen to work as partners with the HKEX and the issuers on the journey to achieve the highest international standards.

If you require further information or wish to discuss this further, we would very much welcome the opportunity to exchange views.

Yours sincerely,

