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26 July 2019

Hong Kong Exchanges and Clearing Limited
8/F, Two Exchange Square
8 Connaught Place, Central
Hong Kong

By email: response@hkex.com.hk

Dear Sir / Madam,

Re: Consultation Paper on Review of the ESG Reporting Guide and Related Listing Rules

CPA Australia represents the diverse interests of nearly 165,000 members working in 150 jurisdictions and regions around the world. We make this submission on behalf of our members and in the broader public interest.

Given the views provided by our members, please find enclosed a comprehensive summary of comments in response to the submission questions.

We have also extracted a few key points here:

- The four *Reporting Principles* might in time be expanded to include additional matters such as reliability and completeness.
- HKEX might wish to provide additional reference to those parts of the Global Reporting Initiative Standards which describe the interaction between *influence on stakeholder decisions* and *significant economic, environmental and social impacts*, as part of prioritising aspects for reporting.
- Para. 14 of Part B of Appendix 27 may either now, or at some future point, be expanded to seek from preparers a short description of how and where the ESG boundary differs from the boundary for other main disclosures, principally financial reports.
- HKEX to monitor across the Greater China regulatory and corporate environment the various factors emerging to drive climate and other environment-related disclosures with the view to achieving coherence and suitable efficiencies.
- At a future point, HKEX may consider extending disclosure of the number and rate of work-related fatalities to include rates of serious injury and occupational diseases.
- Encourage either in this or an early future iteration of the Guide and Related Listing Rules, a greater level of description of what should be included in both corporate whistleblower policy and anti-bribery and corruption policy.

If you have any queries do not hesitate to contact Dr John Purcell, Policy Adviser ESG at CPA Australia on [redacted].

Yours sincerely

[redacted]

Deborah Leung FCPA (Aust.)
Executive General Manager International
CPA Australia

Encl.

Timeframe for Publication of ESG Reports

Question 1: Do you agree with our proposal to amend MB Rule 13.91 and GEM Rule 17.103 to shorten the time required to publish an ESG report from three months after the publication of the annual report to within four months for Main Board issuers or three months for GEM issuers from the financial year-end date?

Agree (tentatively). These are considerations which go very much to existing capacity and accepted practice in the Hong Kong market and amongst the companies concerned. We would remark further only that, over time, it may be efficient to align the timing of these disclosures with main financial reporting.

Printed Form of ESG Reports

Question 2: Do you agree with our proposal to amend the Listing Rules and the Guide to clarify that issuers are not required to provide printed form of the ESG report to shareholders unless responding to specific requests, but are required to notify shareholders that the ESG report has been published on the Exchange's and the issuer's websites?

Agree. This proposal is consistent with international developments enabling shareholder to opt-in to receive hardcopy corporate reports and is more sensible in the ESG context around conserving scarce resources. The trend is of further relevance in the context of shifts that are occurring to provide corporate information on a more real-time basis with corresponding capacity to dive deeper into information initially presented in aggregated form.

General

Question 3: Do you agree with our proposal to amend the Guide to introduce Mandatory Disclosure Requirements?

Agree (tentatively). On its face, there is merit in this approach given that, particularly in common law jurisdictions[1], such as Hong Kong, there has occurred either in 'black-letter' law, regulatory guidance or reinterpretation of legal principle, recognition of a direct link between ESG responsibilities and the discharge of directors' duties. Similarly, the now widely accepted business consensus is that ESG issues and risks do not unfold remote from the rest of the business and have real economic consequence and opportunity that must be managed. The proposed formalisation and elevation is, on these bases, sound.

Two matters we query, are first, to ask whether stock exchange listing rules, in contrast to the broader corporate law, is the most appropriate mechanism for achieving these changes, and secondly, whether possible 'negative consequences' might be foreshadowed in relation to (iii) "ESG-related goals and targets." On this latter point, we draw your attention to circumstances in more litigious jurisdictions, such as Australia, where there has been a reluctance on the part of directors to make forward-looking disclosures in the absence of explicit guidance on reasonable grounds or 'safe harbour' protections.

As a final observation in response to this Consultation Paper question, we would like to emphasis the extent to which ESG reporting, though widely accepted as vital to financial market transparency and stability, remains, as between different capital markets, at markedly different stages of development and

[1] A valuable resource in this regard is the analysis of potential climate-related liability risk for companies and directors in the United Kingdom, Australia, Canada and South Africa being undertaken by the Commonwealth Climate Law Initiative: https://ccli.ouce.ox.ac.uk/

embedment in mainstream practice. The style, tone and structure of each jurisdiction's ESG disclosure regime needs to set clear expectations, whilst at the same time nurturing capacity building within firms. Research commissioned by CPA Australia in 2017[2] examining the link between sustainability ratings metrics and financial measures for a selection of companies listed on the London, Australian and Hong Kong stock exchanges, provides positive proof of cost of capital reductions the greater the depth of sustainability reporting. However, the study did show different relationships between separate governance, environmental and social metrics. These insights suggest, in terms of the proposed changes to the HKEX reporting guide and related listed rules, the continued value of the "comply or explain" approach, though importantly, complemented with ongoing dialogue between regulator and preparers as to continuous improvement in disclosure focusing on critical areas in the environmental and social spheres of economic and business performance.

Governance Structure

Question 4: If your response to Question 3 is positive, do you agree with our proposal to introduce an MDR requiring a statement from the board containing the following elements:

(a) a disclosure of the board's oversight of ESG issues?

(b) the process used to identify, evaluate and manage material ESG-related issues (including risks to the issuer's businesses); and

(c) how the board reviews progress made against ESG-related goals and targets?

Agree. In addition to the above comments, we support the idea reflected in (a) and (b) that the board is the organ of corporate governance ultimately responsible for establishing and giving oversight to a company's risk management framework. The only concern we raise, is to be certain that there does not arise an inference that ESG issues occur, and are managed, in isolation from the rest of the business. Also, we believe it important that the corporate governance framework directs the attention of directors to their responsibility for setting the company's risk appetite, allowing appropriate consideration of where and how ESG-related issues might impact risk taking.

Question 5: Do you agree with our proposal to set out in a note that the board statement should include information on the issuer's current ESG management approach, strategy, priorities and goals/targets and an explanation of how they relate to the issuer's businesses?

Agree. This proposal reflects the degree to which effective ESG management is integral to a business's prosperity and prospects, and further, is consistent with evolving disclosure regimes, such as Integrated Reporting, which seek to communicate a more holistic reflection of business model interdependencies.

Reporting Principles

Question 6: Do you agree with our proposal to amend the Guide to introduce an MDR requiring disclosure of an explanation on how the issuer has applied the Reporting Principles in the preparation of the ESG report?

Agree. By way of example, the long-accepted norm, and in some jurisdictions, such as Australia, the legislative requirement, is for boards to be treated as ultimately responsible for ensuring the application of

[2] https://www.cpaaustralia.com.au/-/media/corporate/allfiles/document/professional-resources/sustainability/sustainability-and-the-cost-of-capital-report-2017.pdf?la=en&hash=E4F6CE65F21D1B8A5DEA287D4FD870EBEC72CF6A

financial accounting rules and standards. With the maturing of ESG/ sustainability reporting as key 'documents of the company', it is reasonable to expect a similar standard of scrutiny and responsibility. By way of example, the Integrated Reporting Framework[3] asks "those charged with governance" to provide opinion about presentation in accordance with the Framework. As a further suggestion, consideration might be given to whether the four mentioned ***Reporting Principles*** might in time be expanded to include additional matters such as reliability and completeness.

Question 7: Do you agree with our proposal to amend the Reporting Principle on "materiality" to make it clear that materiality of ESG issues is to be determined by the board and that the issuer must disclose a description of significant stakeholders identified, the process and results of the issuer's stakeholder engagement (if any), and the criteria for the selection of material ESG factors?

Agree. The interaction of "materiality" and definition/description of significant stakeholders can become ambiguous when viewed across a myriad of disclosure frameworks that have emerged in sustainability and broader corporate reporting. Given the Guide and Related Listing Rules' very clear focus on ESG matters, it is appropriate that Appendix 27 (Part B para. 13) emphasises the board's role in determining these critical attributes of reporting threshold and emphasis. CPA Australia suggests that the HKEX might wish to provide additional reference to those parts of the Global Reporting Initiative (GRI) Standards[4] which describe the interaction between *influence on stakeholder decisions* and *significant economic, environmental and social impacts*, as part of prioritising aspects for reporting.

Question 8: Do you agree with our proposal to amend the Reporting Principle on "quantitative" to:

(a) require disclosure of information on the standards, methodologies, assumptions and/or calculation tools used, and source of the conversion factors used for the reporting of emissions/energy consumption (where applicable); and

(b) clarify that while KPIs for historical data must be measurable, targets may be expressed by way of directional statements or quantitative descriptions?

Agree (tentatively). The inference should be avoided, that quantification can be undertaken to such a degree as to achieve certainty and that quantification might of itself infer, without more, effective management. As such, that part of proposed para. 13 (**Quantification**) should always be read and understood in conjunction with the immediately preceding sentence which mentions 'narrative', as this is the essential element in the board's application of professional judgment.

Importantly, we suggest that consideration be given to allowance for, and discussion of, omitted information. By way of example, disclosures mandated under Australian legislative requirements for listed companies to prepare an operations and financial review, and GRI guidance on sustainability reporting principles and standard disclosures, both make provision for limited omission based on the likelihood of unreasonable prejudice.[5]

As a final remark, we query the specific reference to emissions/energy in what we interpret as a broad principle-based requirement. Perhaps, it may be more suitable to reference emission/energy "by way of

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[3] http://integratedreporting.org/wp-content/uploads/2015/03/13-12-08-THE-INTERNATIONAL-IR-FRAMEWORK-2-1.pdf See *Using the Framework* section 1G.

[4] https://www.globalreporting.org/standard. Refer GRI 101: Foundation and GRI 102: General Disclosures.

[5] As useful explanation of an *unreasonable prejudice* exemption can be found in paragraph 67 of ASIC's Regulatory Guide RG 247 which states: "disclosing the information is likely to give third parties (such as competitors, suppliers and buyers) a commercial advantage, resulting in a material disadvantage to the entity".

example". We suggest further in the disclosure of targets, that the preparer state whether they are voluntary or mandated, or whether they are based on some external authoritative standard or metric.

Reporting Boundary

Question 9: Do you agree with our proposal to amend the Guide to include an MDR requiring an explanation of the ESG report's reporting boundary, disclosing the process used to identify the specific entities or operations that are included in the ESG reports?

Agree in general terms. Whilst proposed para. 14 of Part B of Appendix 27 is an important communication of context and setting, CPA Australia believes that both preparers and users need to be aware of the complexities and subtleties in setting the reporting boundary. Even in financial accounting, conceptual understanding is not entirely fixed with ongoing debate about the reporting entity concept. Turning to ESG and other forms of non-financial reporting, more expansive or extended forms of boundary apply. Integrated Reporting, for example, encourages a reporting perspective, and thus boundary, which considers risk, opportunities and outcomes over and above that recognised in the reporter's consolidated financial reports based on control and significant influence. GRI's sustainability reporting framework, in turn, takes a different approach centred on sustainability topic/aspect with a deliberate combined emphasis inside and outside of the organisation. CPA Australia suggests, therefore, that para. 14 may either now, or at some future point, be expanded to seek from preparers a short description of how and where the ESG boundary differs from the boundary for other main disclosures, principally financial reports.

Climate Change

Question 10: Do you agree with our proposal to introduce a new Aspect A4 requiring:

(a) disclosure of policies on measures to identify and mitigate the significant climate-related issues which have impacted, and those which may impact the issuer; and

(b) a KPI requiring a description of the significant climate-related issues which have impacted, and those which may impact the issuer, and the actions taken to manage them?

Agree. CPA Australia does however suggest consideration of possible rewording. The Consultation Paper makes extensive reference to the FSB's Taskforce on Climate-related Financial Disclosures (TCFD), which is perhaps currently the most influential source for matching investor demand and expectation for such disclosures with market and corporate capacity. As an important matter of coherence and completeness in governance guidance design, we believe it might be of benefit to adapt wording from the TCFD June 2017 Final Report Recommendations using Recommended Disclosure (a) and (b)[6] from each of **Governance, Strategy** and **Risk Management**[7].

Targets

Question 11: Do you agree with our proposal to amend the Environmental KPIs to require disclosure of a description of targets set regarding emissions, energy use and water efficiency, waste reduction, etc. and steps taken to achieve them?

Agree (tentatively). Though supportive, we reiterate concerns expressed elsewhere in our response ((Questions 3 and 8) regarding the need to build upon a possible small base of competency in these

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[6] We deliberately omit (c) from **Strategy** as this deals with scenario analysis and is less likely to be pertinent to a governance framework.

[7] Refer Figure 4 page 14 of the TCFD Recommendations.

practices and the need to promote a willingness to disclose on contentious and challenging subject matter. These are challenges across all capital markets, as recently borne out in the June 2019 Status Report from the TCFD. To ensure that the best possible opportunity is given for the revised HKEX Reporting Guide and Related Listing Rules translating into substantially improved governance performance, we further suggest specifically, in relation to emissions, energy and other climate-related aspects, text reference (potentially footnotes) to those parts of the TCFD Recommendations which could aid materiality type assessments, both generally and at an industry-sector level (see for example Tables 1[8] and 2[9] and the accompanying June 2017 implementation document[10]).

In doing so it is important to strike an appropriate balance between prescription of required corporate behaviour and setting circumstances which encourage behavioural and reporting transformation. Further, there likely will arise a range of factors and instruments outside of the corporate governance guide. Therefore, we suggest that HKEX monitor across the Greater China regulatory and corporate environment the various factors emerging to drive climate and other environment-related disclosures with the view to achieving coherence and suitable efficiencies.

GHG Emissions

Question 12: Do you agree with our proposal to revise an Environmental KPI to require disclosure of Scope 1 and Scope 2 GHG emissions?

Agree, subject to our foregoing comments concerning materiality and capacity. We further suggest, as is the case with the TCFD recommendations on **Metrics and targets**, reference, “if appropriate”, to Scope 3 GHG emissions.

Question 13: Do you agree with our proposal to upgrade the disclosure obligation of all Social KPIs to “comply or explain”?

Agree. CPA Australia believes that environmental and social issues warrant equal treatment in ESG disclosures with the underlying determinant of recognition being a materiality assessment. Such holistic approaches are evident in well-established ESG reporting frameworks, in governance frameworks such as Australia’s ASX Corporate Governance Principles and Recommendations (Recommendations 7.4) and the United Kingdom’s strategic reporting requirements promulgated by their Financial Reporting Council. Additionally, it is worth noting the work of such groups as the World Economic Forum whose annual risk reports increasingly emphasise the connectivity between environmental and social risks.

Employment Types

Question 14: Do you agree with our proposal to revise a KPI to clarify “employment types” should include “full- and part-time” staff?

Agree. The proposed changes to KPIB1.1 and KPIB1.2 are sound and measured. Though not going into the same depth and granularity as those contained in, for example the GRI (GRI 401: Employment), the proposal goes a good way towards informing stakeholders on workforce characteristics and the use/wellbeing of vital human capital.

[8] Examples of Climate-Related Risks and Potential Financial Impacts

[9] Examples of Climate-Related Opportunities and Potential Financial Impacts

[10] *Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures*

Rate of Fatalities

Question 15: Do you agree with our proposal to amend the KPI on fatalities to require disclosure of the number and rate of work-related fatalities occurred in each of the past three years including the reporting year?

Agree. The proposed changes to KPIB2.1, 2 & 3 are important measures towards improved disclosure of occupational health and safety (OH&S) governance. The decision to require historical data in KPIB2.1 is valuable in terms of revealing trends in practice and operations exposing employees to significant risk. CPA Australia also suggests that, at a future point, consideration might be given to extending these disclosures to include rates of serious injury and occupational diseases.

Supply Chain Management

Question 16: Do you agree with our proposal to introduce the following new KPIs in respect of supply chain management?

(a) Description of practices used to identify environmental and social risks along the supply chain, and how they are implemented and monitored.

(b) Description of practices used to promote environmentally preferable products and services when selecting suppliers, and how they are implemented and monitored.

Agree. The proposals are consistent with international trends towards greater due diligence and governance practices over supply chain risk and performance. See for example, the various guidance developed by the OECD in relation to responsible supply chain practices in the garment and footwear sector, and from the Extractive Industries Transparency Initiative concerning ethical dealings in emerging economies, along with various pronouncement relating to responsible sourcing of otherwise recognised conflict minerals.

Significant in Australia has been the passing of the Modern Slavery Act 2018 (Cth) which is modelled on United Kingdom law and reflective of transparency practices developed most notably in California and France. Research commissioned by CPA Australia into businesses' preparedness for reporting against the new legislative requirements reveal, in many instances, an initial intention to apply detailed scrutiny to only tier-one suppliers and engage in 'desk top' examination of significantly large or high-risk perceived suppliers. This, as we have remarked elsewhere in our response to the Consultation Paper, points to the fact that regulatory development around ESG practices needs to be cognisant of pre-existing corporate capacity which must build incrementally over an acceptable period.

Specifically, in relation to the contrasting wording of proposed KPIB5.3 and KPIB5.4, we suggest that in relation to the latter, in addition to the reference to "promote environmentally preferable products and services" words be added concerning ethical sourcing, thus aligning the two indicators.

Anti-corruption

Question 17: Do you agree with our proposal to introduce a new KPI requiring disclosure of anti-corruption training provided to directors and staff?

The elevation of both the anti-corruption and whistleblower procedures to KPIs (respectively KPIB7.2 and KPIB7.3) is highly commendable. CPA Australia, though, would encourage either in this or an early future iteration of the Guide and Related Listing Rules, a greater level of description of what should be included in both corporate whistleblower policy and anti-bribery and corruption policy. See for example, Recommendations 3.3 and 3.4 of the 4th ed. of the ASX Corporate Governance Principles and Recommendation and the respective 'box' illustrations of suggested policy content.

To some degree both aspects of corporate governance practice reflect, or are coherent with, associated statutory rules in either criminal law or corporate law. This is the case in Australia with proposed strengthening of foreign bribery laws under the Crimes Legislation (Combating Corporate Crime) Bill 2018 and the passing of the Treasury Laws Amendment (Enhancing Whistleblower Protections) Bill 2018. Nevertheless, we believe it important to emphasise that 'black-letter' law cannot alone be the panacea for attacking corporate misconduct. It is on this basis that there can be observed in Australia positive measures towards engagement of the private sector to develop and adopt internal controls, ethics and compliance programmes for preventing and detecting foreign bribery. CPA Australia thus sees HKEX as playing a potentially significant role promoting and engaging with the Greater China business community as part of capacity building.

Question 18: Do you agree with the proposal to revise the Guide's wording on independence assurance to state that the issuer may seek independent assurance to strengthen the credibility of ESG information disclosed; and where independent assurance is obtained, the issuer should describe the level, scope and processes adopted for assurance clearly in the ESG report?

Agree. CPA Australia has long held the view that the credibility of ESG and other forms of non-financial disclosure is critically dependent on independent third-party assurance. Assurance underpins market confidence and the confidence directors have in the accuracy and meaningfulness of the disclosures they are making. As you state in para. 128 of the Consultation Paper, both ESG reporting frameworks and associated assurance practice guidance[11] is evolving and it is on this basis that frameworks such as Integrated Reporting and the GRI discuss assurance in non-mandatory terms. We suggest though that para. 9 of the ESG Guide might be reworded to say: "encouraging issuers to consider" rather than merely "may consider". We believe this would better signal expectations about improved rigor of reporting over time. On the specific point about describing 'level, scope and processes', this too is an important aspect in driving investor confidence and is consistent with recent developments contained in the revised 4th edition of the ASX Corporate Governance Principles & Recommendations (Recommendation 4.3).

[11] Note the current work of the International Audit and Assurance Standards Board on Extended External Reporting.