HKEX 香港交易所

November 2023

# Analysis of 2022 Corporate Governance Practice Disclosure

## CONTENT

## INTRODUCTION

1. The Stock Exchange of Hong Kong Limited ("**Exchange**") periodically conducts reviews of issuers' compliance with the Corporate Governance Code ("**CG Code**"). This report covers corporate governance reports for the 2022 financial year and marks the twelfth edition of the Exchange's review of issuers' compliance with the CG Code ("**2022 Review**" or "**this Review**").

2. The Exchange introduced important updates to the CG Code on 1 January 2022. The main changes included highlighting the importance of corporate culture in alignment with the company's purpose, values and strategy. The changes also aimed to: enhance board independence and strengthen board refreshment; and promote board and workforce gender diversity, with single gender boards to be phased out by 31 December 2024 ("**2022 Update**")[1].

3. This Review focused on issuers' compliance with some of the new requirements arising from the 2022 Update, with a particular emphasis on the following areas:

   (a) ***Corporate culture*** – the adoption of and the quality of disclosure on the new requirements;

   (b) ***Long Serving INEDs***[2] – compliance with the additional disclosure requirements and for issuers with all Long Serving INEDs, progress of their appointment of a new INED;

   (c) ***Diversity*** – compliance with the new diversity disclosure requirements and the progress of phasing out single gender boards, including tracking the extent to which single gender board listing applicants have fulfilled their board diversity promises; and

   (d) ***Risk management and internal controls*** – the quality of disclosure.

4. For the purpose of this Review, the Exchange analysed corporate governance reports ("**CG Reports**") of a sample of 400 issuers ("**Sample Issuers**") and also reviewed (i) circular disclosures in relation to the re-election of Long Serving INEDs and (ii) CG Report disclosures on the board diversity progress of single gender board listing applicants.[3]

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[1] Most of the changes took effect on 1 January 2022, except for the requirement to appoint a new INED at the forthcoming annual general meeting where all the INEDs are Long Serving INEDs, which came into effect on 1 January 2023.
[2] Independent non-executive directors who have served for more than nine years.
[3] Please refer to **Appendix I** for more details on the sampling method for the 2022 Review.

5. Key findings from this Review are summarized below, with more detailed findings set out in chapters 2 and 3 of this report:

***Corporate culture***

- All of the Sample Issuers reported compliance with the code provision ("**CP**") on corporate culture but did not always include detailed disclosure on their desired corporate culture in their CG Reports.

- Comprehensive disclosure should include (among other things) details on: (i) the link between corporate culture and the issuer's business objectives; (ii) the implementation of the desired corporate culture into the issuer's daily operations; and (iii) an assessment of the progress and success of such implementation.

***Long Serving INEDs***

- The 2022 Update has resulted in a meaningful reduction of boards whose INEDs consisted of all Long Serving INEDs. All of the relevant Sample Issuers that retained Long Serving INEDs disclosed the factors they considered in determining the INED's suitability for re-election.

- Board composition should be regularly assessed in line with changes to an issuer's business environment and other challenges. The Exchange believes that periodic board refreshment can foster the sharing of diverse perspectives.

- Where a Long Serving INED is retained, sufficient details should be disclosed regarding the suitability of such individual for re-election, including the process undertaken by the nomination committee and the board to confirm his / her continued independence.

***Diversity***

- Since the 2022 Update, the percentage of single gender board issuers has dropped by 8%. Existing single gender board issuers (around 550 issuers) should proactively seek to appoint at least one director of a different gender by the deadline of 31 December 2024.

- It is important that board composition reflects a suitable balance of skills, experience and diversity of perspectives. Issuers should formulate long-term targets and timelines to further progress gender diversity on their boards beyond the required minimum and within their wider workforce.

***Risk management and internal controls***

- All of the Sample Issuers disclosed information on their risk management and internal controls and a large majority confirmed that their existing systems are effective.

- Conducting appropriate risk assessment and implementing internal controls that help to manage such risks is key to good corporate governance. It is equally important to regularly monitor the internal controls in place and review their effectiveness at least annually.

- CG Reports should include sufficient details on the issuers' internal control review to support their findings that the internal controls remain effective.

***Other observations***

- We observed a high level of compliance with the mandatory disclosure requirements ("**MDRs**") and CPs of the CG Code, consistent with the findings of our previous reviews.

- Issuers should ensure they understand the disclosure requirements for all MDRs, (including the sub-paragraphs of relevant MDRs), and make disclosure accordingly in their CG Reports. If issuers determine that any of the MDRs is not applicable to them, they should state the same in their disclosures.

6. Delivering effective corporate governance practices is more than a box-ticking exercise. High quality reporting helps differentiate the approach that companies take and provides confidence to the market. The Exchange is committed to supporting the entire issuer community by providing training and publishing guidance materials, and these can be found in our one-stop portal "Corporate Governance Practices" on our website.

7. The Exchange will continue to promote good corporate governance. This Review provides helpful guidance on areas of the CG Code where further progress and improvements can be made. The Exchange is currently conducting a review of its corporate governance framework and expects to put forward proposals for public consultation in due course.

## A. Corporate Culture

**Key takeaways:**

- Full compliance of all Sample Issuers with new CP on corporate culture
- *Good disclosure on corporate culture*:
  - explain how corporate culture is implemented and supports long-term business objectives
  - avoid generic disclosure or overly narrow focus on corporate governance

***Background***

8. An issuer's corporate culture sets its expectations of behaviour for directors and employees, and should be tied to an issuer's purpose, values and strategy.

9. As part of the 2022 Update, the Exchange introduced a new CP[4] and provided guidance[5] highlighting (i) the board's role ("tone from the top") in establishing the issuer's purpose, values and strategy, and ensuring that these and the issuer's culture are aligned, and (ii) the directors' duty to act with integrity, lead by example and promote the desired culture. This Review assessed the quality of disclosures made on corporate culture.

***Findings***

10. All of the Sample Issuers reported they had complied with the new CP on corporate culture. We observed examples of good disclosure with detailed explanations of how the desired culture has been applied to the broader business objectives of the issuer and how its corporate culture has been communicated throughout the organisation. Some Sample Issuers connected corporate culture with ESG objectives and explained the impact on their business plans going forward. A few Sample Issuers provided illustrative graphics to show how different focus areas of their corporate culture fit together (see Example 1 below).

11. Other observations include:

   (a) Many Sample Issuers focused their culture statement on their approach to governance, internal controls and / or ethics. However, there was a general lack of detail on the implementation of the desired culture within the Sample Issuer's operations.

   (b) A few of the Sample Issuers went further and made specific disclosure on what is done in terms of messaging and training to ensure staff are applying the desired culture.

   (c) Disclosures on culture were not only found within the CG Report but also sometimes as part of the ESG report, the chairman's statement or the management discussion and analysis. Over half of the Sample Issuers did not include a specific section or paragraph

[4] CP A.1.1.

[5] Pages 9 – 12 of the Exchange's Corporate Governance Guide for Boards and Directors (December 2021).

addressed to corporate culture in their CG Reports.

**Example 1 – Illustrative graphic on culture values**
**– Source: An issuer in the catering industry**


***Our comments / guidance***

12. The Exchange welcomes the high level of compliance with the new CP on corporate culture. We wish to emphasise that a description of an issuer's overall corporate governance approach only would not provide sufficient information on the company's culture, and how this is aligned with the company's purpose, values and strategy.

13. A comprehensive disclosure would include details on the various aspects considered by the board and directors in their assessment of whether the issuer's purpose, values and strategy are aligned with its culture, and on steps taken to implement the desired culture throughout the organization. With relevant disclosures, issuers can effectively update the market on their organizational values and how these values are aligned with long-term business goals.

14. While the CG Code does not include a specific requirement on the location or the presentation of information on corporate culture, where such disclosures are made outside of the CG Report, (for example as part of the chairman's statement), issuers should provide appropriate cross references in the CG Report to make it easier for investors and the market to identify the relevant information.

## B. Long Serving INEDs

**Key takeaways:**

- Meaningful reduction of issuers with all Long Serving INEDs
- *Appointment of new INED*: issuers with all Long Serving INEDs to appoint a new INED at their AGM, or explain why they have not done so
- *Disclosure on re-election of Long Serving INEDs*: in addition to the factors considered in determining suitability for re-election, also disclose the process (i.e. steps taken by the Nomination Committee and the board) and related discussions

***Background***

15. A strong independent voice on the board is key to a board's effective operation.[6] The continued independence of independent non-executive directors ("**INEDs**") is, however, at risk where they have served on a board for an extended period of time, as familiarity with an issuer's management may affect their objectivity.

16. The 2022 Update introduced additional disclosure requirements on the proposed re-election of Long Serving INEDs[7]. These included disclosure of: the factors considered; the process; and the board or nomination committee's discussion in concluding that a Long Serving INED is still independent. This disclosure enables shareholders to better assess whether a Long Serving INED is still capable of bringing independent judgment to a board.

17. To improve board refreshment, the Exchange also introduced new requirements[8] for issuers whose INEDs are all Long Serving INEDs to: (a) disclose the length of tenure of each Long Serving INED; and (b) appoint a new INED at the forthcoming annual general meeting ("**AGM**").

18. This Review assessed the quality of issuers' explanations on the re-election of Long Serving INEDs. It also assessed compliance by issuers whose INEDs are all Long Serving INEDs with the INED tenure disclosure and the new INED appointment requirements.

***Findings***

19. As of 31 August 2023, there were approximately 1,500 directorships held by Long Serving INEDs on the boards of approximately 800 issuers (i.e. approximately 30% of all issuers listed on the Exchange).

*Issuers with all Long Serving INEDs*

20. There was a meaningful reduction in the number of issuers with all Long Serving INEDs on the board. As of 31 August 2023, there were fewer than 50 issuers (approximately 2% of all issuers) whose INEDs were all Long Serving INEDs, compared to around 150 issuers (approximately 6% of all issuers) prior to the 2022 Update.

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[6] Main Board Rule 3.10 (GEM Rule 5.05) requires each issuer to have at least three INEDs on its board.
[7] CP B.2.3.
[8] CP B.2.4. Limb (a) of CP B.2.4 came into effect on 1 January 2022, while limb (b) of CP B.2.4 came into effect on 1 January 2023.

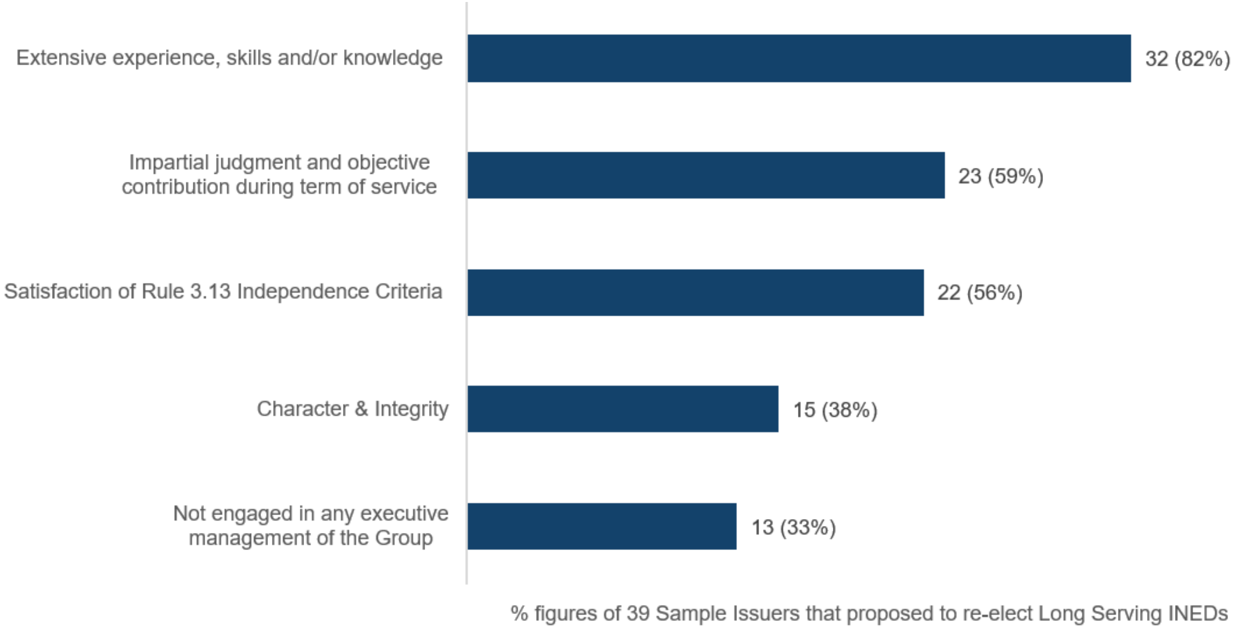
21. Over half of the relevant Sample Issuers whose INEDs were all Long Serving INEDs[9] appointed a new INED prior to their 2023 AGM.

22. In respect of the remaining relevant Sample Issuers with all Long Serving INEDs, all of them disclosed the tenure of each Long Serving INED. However, some issuers did not appoint a new INED at their 2023 AGM and did not provide an explanation as to why they had not done so.

*Issuers with one or more Long Serving INEDs*

23. All the relevant Sample Issuers provided grounds for re-electing Long Serving INEDs in their shareholder circulars and disclosed the factors considered in determining the suitability of such INEDs for re-election. The Exchange reviewed the common explanations given by these issuers[10,11]:

**Chart 1: Reasons for believing that a Long Serving INED is independent (CP B.2.3)**




24. While a number of issuers continued to cite satisfaction of the independence criteria set out in Main Board Rule 3.13 ("**Rule 3.13 Independence Criteria**") as a supporting reason for a Long Serving INED's independence, the percentage was substantially lower compared to our previous corporate governance practice disclosure review.

***Our comments / guidance***

25. Periodic board refreshment, in particular the appointment of new INEDs, can help avoid entrenchment, facilitate board diversity and bring new perspectives to the board. The new requirements introduced in the 2022 Update have served their intended purpose as the Exchange has observed a notable reduction in the number of issuers with all Long Serving INEDs.

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9 Please refer to the sampling method in **Appendix I**.

10 The percentages do not add up to 100% as most issuers referred to more than one reason in their explanations.

11 The figure for "Satisfaction of Rule 3.13 Independence Criteria" includes issuers who referred to i) the annual independence confirmation provided by the INED and/or ii) the board's assessment of the INED's independence with reference to the Rule 3.13 Independence Criteria.

26. If an issuer decides to re-elect a Long Serving INED, it should provide the information necessary to enable the market to assess the rigour of its nomination process, including the steps taken by the nomination committee (for example, how it conducted a review of the Long Serving INED's performance and the INED's ability to contribute objectively to the board) and how the board assessed the nomination committee's recommendation.

27. The Rule 3.13 Independence Criteria primarily focus on a director's actual or potential conflict of interests, and not a director's ability to bring fresh perspective and independent judgment. Therefore, issuers should refer to our previous guidance on quoting the Rule 3.13 Independence Criteria[12] as a reason to justify the re-election of Long Serving INEDs. When assessing a director's continued suitability for the role, the board (or the nomination committee) should focus on the INED's mindset and whether the INED remains capable of continuing to provide an independent and objective contribution. A consideration of the director's actual or potential conflict of interests only is insufficient. Issuers are reminded to provide further details or analysis to support why they have grounds to believe an INED continues to be independent.

28. If an issuer with all Long Serving INEDs chooses not to appoint a new INED and deviates from CP B.2.4(b), it should properly consider and disclose the reasons for retaining its existing Long Serving INEDs.

29. Board evaluations and a board skills matrix are useful tools to help identify a board's existing skillsets and bring any gaps to the board's attention. Issuers may utilize such tools[13] to help inform their decisions on the retention, or not, of Long Serving INEDs and to support board refreshment and succession planning.

30. The Exchange will continue to monitor market progress on Long Serving INEDs, and may consider introducing further measures in this area, as necessary.

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[12] Please refer to paragraph 31 on page 8 of the Exchange's Analysis of 2019 Corporate Governance Practice Disclosure.

[13] For the avoidance of doubt, a board skills matrix should be distinguished from the directors' biographies in the annual report, which are a factual account of each director's educational and professional achievements.

## C. Diversity

**Key takeaways:**

- High level of compliance regarding annual review of board diversity policy and disclosure of workforce gender ratios
- Remember to disclose numerical targets and timelines for achieving board gender diversity
- *Single gender board issuers*: do not wait until the December 2024 deadline to appoint a director of a different gender

***Background***

31. Diversity in the boardroom has a positive effect on board performance and the quality of decision-making by bringing in outside perspectives and reducing the risk of "group think". The Exchange believes in the value of integrating diversity into issuers' strategies and operations and that efforts to promote greater diversity and inclusion should also extend beyond the boardroom to the wider workforce.

32. In January 2022, the Exchange called an end to single gender boards, with a transition period up to 31 December 2024 ("**December 2024 Deadline**")[14]. The 2022 Update also introduced requirements[15] for: an annual review of board diversity policies; the setting of gender diversity targets (with timelines) at the board level; and disclosure of gender ratios within the workforce, together with any plans or measurable objectives for achieving workforce gender diversity.

33. This Review looked at compliance with the above new diversity requirements.

34. The Exchange also tracked the progress that had been made by single gender board issuers that were primarily listed between July 2019 and June 2022 ("**Single Gender Board Newly Listed Issuers**") in achieving board gender diversity ("**2022 Diversity Tracker**").

***Findings***

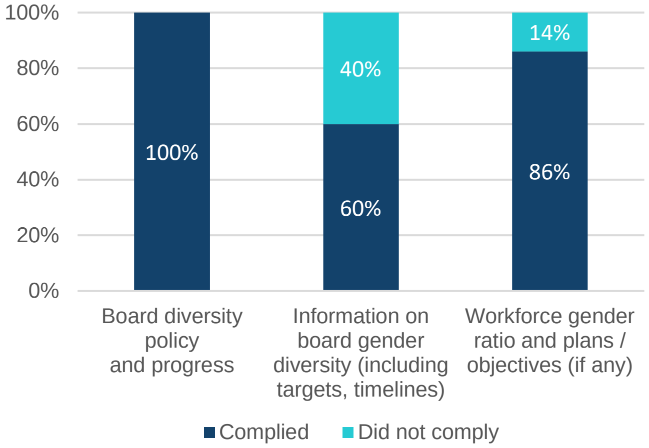
35. As of 31 August 2023, 17.3% of directors on the boards of listed issuers were female (compared to 15.2% prior to the 2022 Update). The percentage of single gender board issuers was 21.4% (compared to 29.6% prior to the 2022 Update). These statistics show positive progress and the Exchange expects such progress to continue.

[14] Main Board Listing Rule 13.92 and GEM Rule 17.104.
[15] Paragraph J of the MDRs and CP B.1.3.

*Compliance with CG Code diversity requirements*

36. Findings from the Sample Issuers' compliance with the new diversity disclosure requirements under the CG Code are summarized below. Generally, there was a high level of compliance, except regarding the requirement to disclose numerical targets and timelines for achieving board gender diversity[16].

**Chart 2: Compliance rate with the new requirements in paragraph J of the MDRs**




*Board gender diversity targets*

(a) Sample Issuers who included a board gender diversity target generally cited a target to appoint one director of a different gender by the December 2024 Deadline (if they had a single gender board) or to maintain the current level of female representation on their board (non-single gender board issuers). Some Sample Issuers stated that they had not set any measurable objectives as they considered their existing board composition to be sufficiently diverse.

(b) Some Sample Issuers went further and articulated a more ambitious target beyond the status quo, with a clear timeline. Good examples included a commitment to have "at least three female directors as an immediate target and a minimum 20% representation by 2025" and to "maintain an appropriate level of female members on the Board, which shall not be less than 20% with immediate effect and 25% by 2025".

*Workforce diversity objectives*

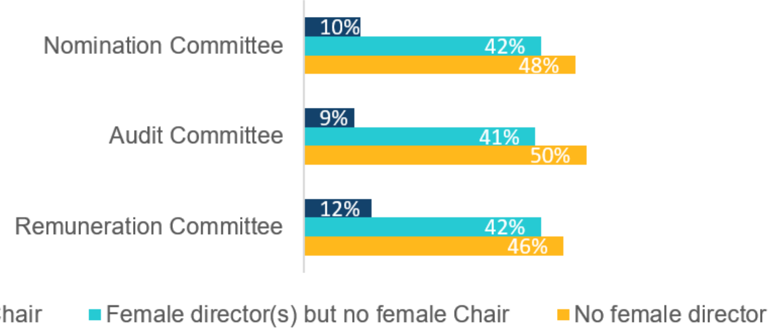
(c) Good examples of better disclosure on workforce diversity objectives included planned actions to cultivate a diverse talent pipeline or a commitment to increase diversity at the management level.

*Gender diversity on mandatory board committees[17]*

37. Around half of the non-single gender board Sample Issuers[18] had one or more female directors on their mandatory board committees. However, the proportion of female chairs remained low:

[16] MDR paragraph J(b).
[17] The Nomination Committee, the Audit Committee and the Remuneration Committee.
[18] 310 out of 400 Sample Issuers.

**Chart 3: Board committee diversity statistics**




*Findings from the 2022 Diversity Tracker*

- The Exchange previously tracked the board diversity progress of Single Gender Board Newly Listed Issuers primarily listed between July 2019 and December 2020 in our Analysis of IPO Applicants' Corporate Governance and ESG Practice Disclosure in 2020/2021 ("**2021 Diversity Tracker**").

- The 2022 Diversity Tracker reviewed the progress of: (i) those Single Gender Board Newly Listed Issuers who had yet to appoint a female director at the time of the 2021 Diversity Tracker; and (ii) Single Gender Board Newly Listed Issuers listed between January 2021 and June 2022.[19]

- The Exchange made the following observations:

    - Around half of the Single Gender Board Newly Listed Issuers had already appointed at least one female director by the end of the financial year 2022.
    - Of the remaining issuers, a number of them revised their original deadlines to align with the December 2024 Deadline. A small number of them had neither appointed a female director nor revised their deadline despite the deadline having lapsed.

***Our comments / guidance***

38. Remaining single gender board issuers should proactively seek to appoint at least one director of a different gender (for example, upon the retirement of an existing director by rotation) and not wait until closer to the December 2024 Deadline to take action.

39. Board composition should reflect a necessary balance of skills, experience and diversity of perspectives. The absence of a prescribed percentage in our Rule does not mean one director of a different gender on the board is sufficient. Issuers should assess their own circumstances and needs, and consider whether to commit to a particular (higher) ratio beyond the present board composition.

40. By setting clear targets and timelines, issuers can demonstrate the concrete steps they will take

[19] This period covers the time from the 2021 Diversity Tracker up until the Exchange ceased to approve listing applications from single gender board listing applicants as a matter of policy in July 2022.

to translate their board gender diversity goals into their broader diversity objectives. Disclosures should include details of: the steps and programmes implemented by the issuer; and a discussion as to whether the issuer is on track to meet its numerical targets and timelines (see Example 2 below), and if not, what additional actions the issuer is taking to enable it to achieve its diversity goals. Such information reflects the issuer's commitment to continually assess its diversity objectives and enables stakeholders to track and assess the issuer's progress. Regular board evaluations and/or a board skills matrix may also assist the board in considering and increasing diversity at the board level.

**Example 2 – Clear disclosure on board gender diversity target and progress – Source: Company in the insurance sector**

The Board's target for female representation on the Board is 40 per cent by the end of 2025, as recommended by the FTSE Women Leaders Review. At 31 December 2022, the role of Chair was held by a woman and the overall representation of women on our Board was 31 per cent. On 1 January 2023 female representation increased to 38 per cent. As previously announced, [male director 1] and [male director 2] will not stand for re-election at the forthcoming AGM, which will further increase the proportion of women on our Board to 45 per cent.

41. Where there is a revision to a diversity target or deadline, or a new circumstance arises that makes it difficult to fulfill their diversity commitments, issuers should provide a reasoned explanation tailored to their individual circumstances.

42. Board committees play a crucial role in overseeing various company functions. The Exchange encourages issuers to also improve diversity on these committees and take proactive steps to cultivate a more diverse talent pipeline (see Example 3 below).

**Example 3 – Disclosure of concrete diversity and inclusion initiatives at the workforce level**
**– Source: Company in the mass transportation industry**

The Company has achieved several D&I related key performance indicators in 2022. For instance, three initiatives aimed at enhancing workforce diversity were organised in collaboration with NGOs and around 230 Diversity, Equity and Inclusion ("DEI") training events for staff were organised. In addition, a review of the DEI clauses in the Code of Conduct and Equal Opportunities Policy has been completed and the revised Code of Conduct was released to all staff in February 2022. Also, 9% of the Company's summer interns recruited were ethnic minorities or persons with disabilities, which is higher than the target of 8%. Meanwhile, workplace inclusiveness has also been enhanced in 2022 through: (1) the establishment of a women's network; and (2) the review of the language requirements for ten job positions.

## D. Risk management and internal controls

**Key takeaways:**

- Full compliance regrading disclosure on Internal Control Systems, with confirmation of systems' effectiveness by most Sample Issuers
- Regular monitoring and at least annual reviews of Internal Control Systems key to effective risk management
- *Good disclosure*: explain in sufficient detail:
  - structure and processes of the Internal Control Systems (responsible persons / departments)
  - particular risks (principal / emerging) including fraud and/or ESG related risks considered
  - process for regular monitoring and reviews

***Background***

43. As an essential component of investor protection and market quality, issuers should have in place an effective risk management and internal control system ("**Internal Control System**"). The CG Code sets out a number of disclosure requirements, including for issuers to confirm that they have reviewed the effectiveness of their Internal Control System, the frequency of such reviews and a confirmation that the Internal Control System is effective and adequate[20]. The CG Code further confirms that it is the duty of the board to: (i) oversee the Internal Control System on an ongoing basis, and (ii) to review its effectiveness at least annually.[21]

44. This Review focused on the quality of disclosures made by the Sample Issuers.

***Findings***

45. All of the Sample Issuers have made substantial disclosures on their Internal Control System. In most cases, the Sample Issuers provided relevant details including on: the risks they identified for their business; an overview of the Internal Control System in place; a summary of that system's review; and a confirmation that the system was found to be effective.

46. Some disclosures, however, lacked specific details to allow for a proper understanding of how the Sample Issuers' Internal Control System was designed to manage specific business risks. Some Sample Issuers referred to ESG-related risks or factors in relation to their Internal Control System but, in most cases, failed to identify which specific ESG-related risks concerned them.

47. In some cases, the confirmations provided on the effectiveness of Internal Control Systems lacked sufficient detail to provide meaningful support for the Sample Issuers' assessment.

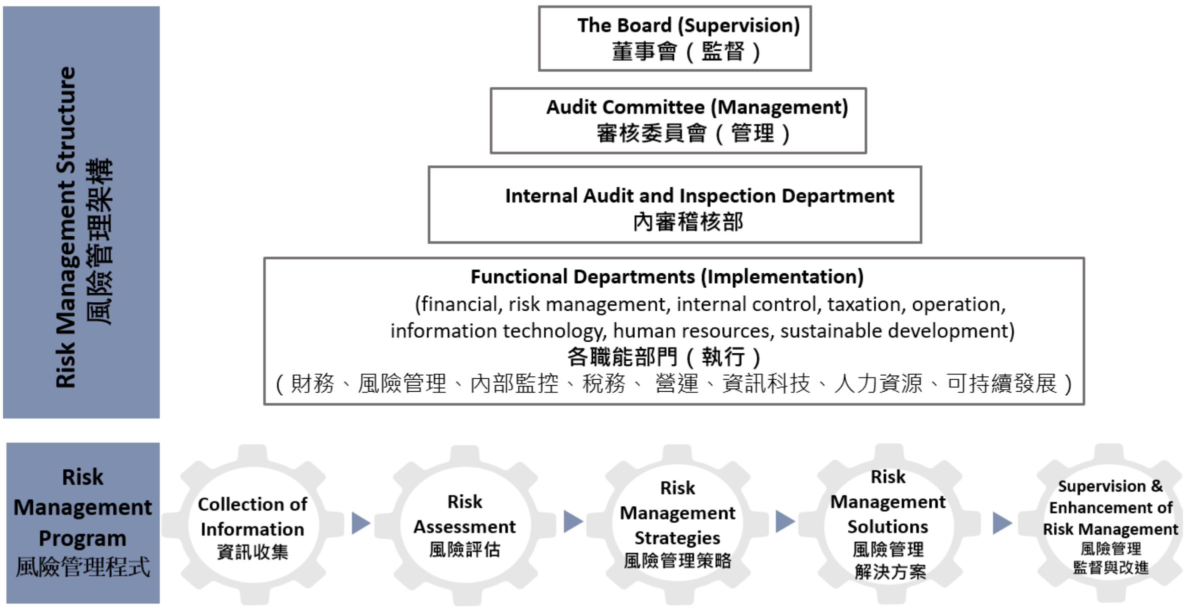
[20] Paragraph H of the MDRs.
[21] CP D.2.1.

***Our comments / guidance***

48. Setting up and maintaining an effective Internal Control System requires issuers to critically assess risks relevant to their business and ensure that the internal controls they have in place are appropriate to effectively manage those risks. The assessment of relevant risks should cover principal and emerging risks and also fraud risks which are prevalent and affect many businesses.

49. With their disclosures on Internal Control Systems in the CG Report, issuers can update the market on the steps they have undertaken to manage specific risks to their business and the effectiveness of the systems they put in place for that purpose. For such disclosures to be effective, there should be sufficient details on the structure of the system in place, including details of the key individuals and departments responsible for such systems, and the processes to regularly review and monitor whether the Internal Control System is operating properly. The use of graphics can help to illustrate the operation of the Internal Control System (see Example 4 below).

**Example 4 – Graphics on structure and process of Internal Control Systems - Source: Issuer in the environmental industry**




50. Issuers are required to conduct (at least) annual reviews of the effectiveness of their Internal Control Systems (which are to be distinguished from regular monitoring of the Internal Control System's operation).[22] For the purpose of demonstrating that the required annual reviews have been conducted, sufficient details should be disclosed to support the issuers' conclusion that the Internal Control System was found to be effective. This would include:

(i) whether the board has confirmed the system's effectiveness;

(ii) which confirmations the board / issuer received in support of its finding that the system

[22] CP D.2.1.

is effective (e.g. from management[23], the audit committee, the internal audit function, other departments and/or external advisers);

(iii) whether any significant areas of concern[24], such as material weaknesses of the system, were identified as part of the review (and if so, how such were remedied); and

(iv) any changes to the system that were implemented over the year (with an explanation what these changes were and the reasons for such changes).

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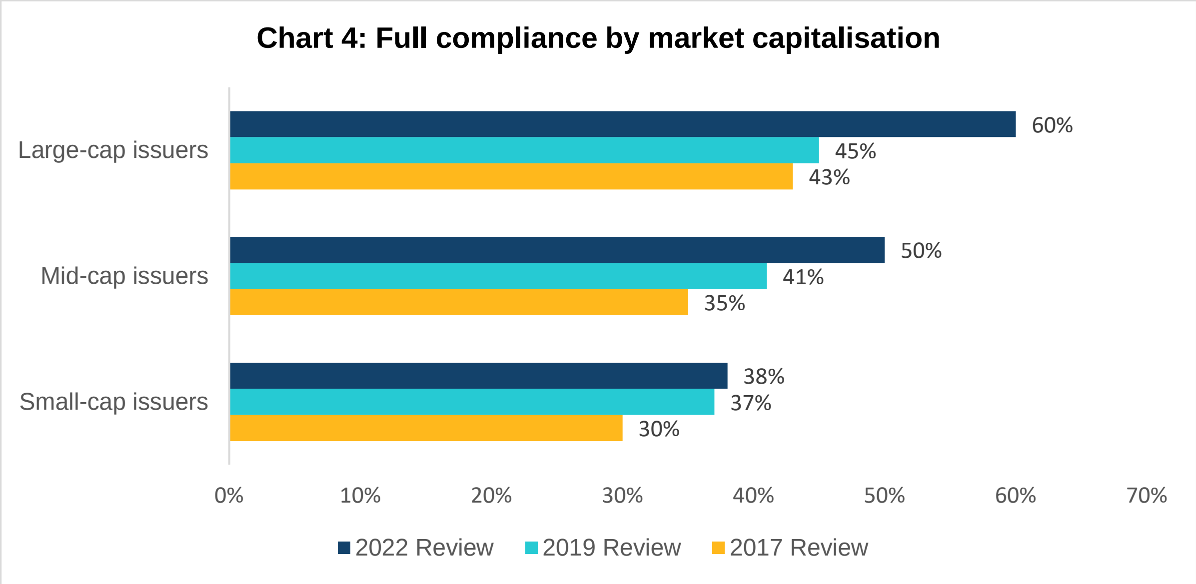
[23] Recommended best practice D.2.8.
[24] Recommended best practice D.2.9.

## A. Key statistics

51. The Exchange is pleased to note that Sample Issuers' compliance with CPs has further improved, continuing the trend observed in the last review period. All Sample Issuers complied with at least 73 out of 78 CPs[25], and 49% of them fully complied with all CPs[26] (2019 Review: 41%, 2017 Review: 36%). Please refer to **Appendix II** for the relevant statistics.

52. Chart 4 below shows the compliance rates of Sample Issuers by reference to their market capitalization. Consistent with previous reviews, large-cap issuers achieved the highest rate of full compliance. However, it was encouraging to note that both mid-cap and small-cap Sample Issuers also achieved meaningful improvements in their overall compliance rate.

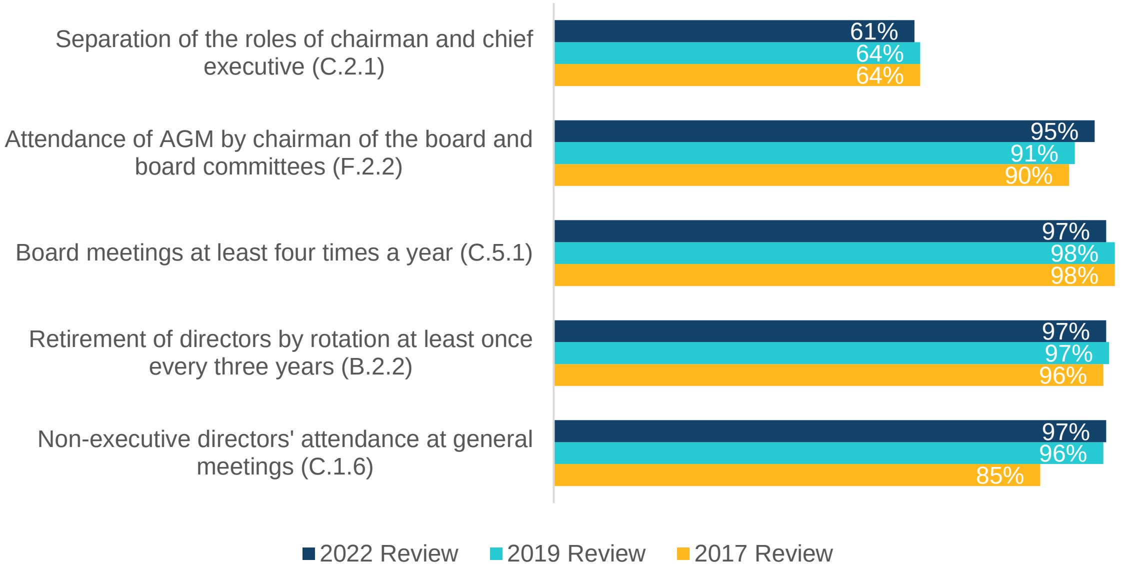



## B. Separation of roles of chairman and chief executive

53. Sample Issuers overall achieved a very high rate of CP compliance (over 90%), except for the CP on the separation of the roles of chairman and chief executive (with a compliance rate of only 61%). The compliance rate on the separation of these roles has remained relatively static over the past three reviews (see Chart 5 below).

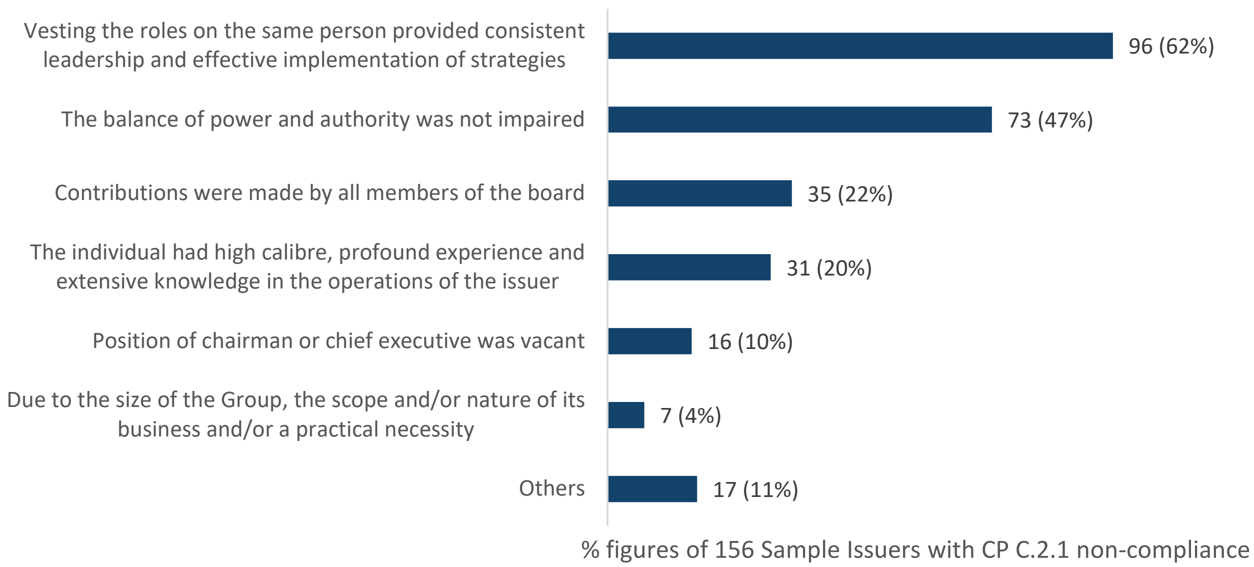
[25] All but two Sample Issuers complied with at least 73 out of 78 CPs. The two Sample Issuers had prolonged vacancies in the positions of chairman and / or chief executive officer as a result of their particular circumstances and were, as such, excluded from the presentation of the relevant statistics.
[26] Statistics are based on self-reporting of Sample Issuers on CP compliance in CG Report.

**Chart 5: Compliance Rate of the Five Least Complied CPs**




54. Chart 6 below summarises the main reasons given by the Sample Issuers for not separating the roles of chairman and chief executive[27]:

**Chart 6: Reasons for non-compliance with CP C.2.1**




55. In a number of instances, the grounds given for not separating the roles (as shown in Chart 6) were provided without any detail or specificity to the issuer's individual circumstances.

***Our Comments***

56. The chairman leads the board and is responsible for its overall effectiveness in directing the company. The chief executive oversees the company's operations. The Exchange believes there should be a clear division of these responsibilities to ensure a balance of power and

[27] The percentages do not add up to 100% as most issuers referred to more than one reason in their explanations.

authority, so that power is not concentrated in any one individual[28]. Having the roles performed by two individuals can help provide a check and balance on the exercise of power.

57. Disclosures for non-compliance with this CP should focus on how the potential governance issue is effectively addressed by alternative arrangements. For example, issuers could explain how the presence of other board members or INEDs, or how the internal control framework assists the issuer in scrutinizing important decisions and monitoring the exercise of power by the chairman cum chief executive[29]

## C. Common pitfalls

*Omission or partial disclosure of MDRs*

58. Certain MDRs were omitted by a portion of Sample Issuers[30], possibly because those MDR(s) were not considered to be relevant or applicable to them. Issuers are reminded that information called for under the MDRs must be disclosed in the CG Report. To comply with the disclosure requirement, issuers should include a negative statement if they consider any of the MDRs not applicable to them.

59. As some MDRs require disclosure on a number of different issues, issuers should carefully examine each paragraph / sub-paragraph of the MDR to ensure that all required information is properly disclosed.

| **MDR** | **Issue spotted / Advice** |
|---|---|
| Relationships between board members, and between chairman and chief executive<br><br>(*Para. B(h)*) | No disclosure is made.<br><br>Issuers should provide a negative statement if this is not applicable or where no discloseable relationships exist. |
| Diversity<br><br>*(Para. J(b))* | Disclosed a summary of board diversity policy, but omitted to state numerical targets and timeline.<br><br>Issuers should state numerical targets and timeline for achieving board gender diversity. |
| Investor Relations (shareholders' communication policy)<br><br>(*Para. L(c)*) | Disclosed a summary of a shareholders' communication policy, but omitted to state the implementation and effectiveness of the policy.<br><br>Issuers should state the review of the implementation and effectiveness of the shareholders' communication policy conducted during the reporting year. |

60. The Exchange also observed that some of the relevant disclosures required by the MDRs are

[28] Principle C.2.

[29] A few Sample Issuers explained their deviation from CP C.2.1 with a resignation from either the chairman or the chief executive with such role remaining vacant temporarily. In such case, issuers should detail the interim measures put in place to safeguard the balance of powers, and indicate the expected duration of such interim arrangement.

[30] For example, 16% of the Sample Issuers failed to either make a positive statement (if applicable) or a negative statement (if not applicable) in respect of any relationships among board members and as between the chairman and the chief executive (paragraph B(h)).

set out within annual reports but not in CG Reports.[31] To improve clarity and readability, issuers should use cross references where appropriate.

*Compliance pitfalls for CPs*

61. The Exchange recognizes that there is no "one size fits all" approach that will achieve effective corporate governance. The Principles in the CG Code set out the overarching direction for issuers to consider but effective application of the Principles may also be achieved by means other than strict compliance with the CPs. The "comply or explain" framework allows issuers to deviate from CPs by adopting alternative means or measures for the purpose of achieving effective corporate governance. This framework, however, also requires that in such cases, issuers disclose considered reasons for the deviation from the CPs in the CG Report and explain how good corporate governance was achieved by means other than strict compliance.[32]

62. The Exchange observed a few occasions where the Sample Issuers did not apply the "comply or explain" framework properly.

| **Issue spotted** | **What should be done** |
|---|---|
| Non-compliance without any explanation[33] | Where non-compliance is reported, issuers must properly explain their reasons for the non-compliance, addressing potential concerns arising from the non-compliance. |
| Full compliance with CPs reported but with non-compliance identified[34] | Where non-compliance exists, issuers must report the non-compliance.[35] |
| Misinterpretation of a CP[36] | Issuers may refer to guidance materials published by the Exchange from time to time. |

63. The Exchange also observed that a small number of the Sample Issuers appeared to have relied on an outdated version of the CG Code in effect prior to the 2022 Update, either by providing outdated CP references or by relying on outdated rules.[37] Issuers must keep up-to-date with the latest changes to the Listing Rules to properly understand and discharge their obligations.

[31] Issuers are reminded that, generally, all disclosures pursuant to the CG Code should be included within their CG Reports (one Sample Issuer referred to the company's website for the disclosure of its diversity policy).
[32] Explanations for a deviation from relevant CPs should also provide a clear rationale for the alternative actions and steps taken by the issuer and their impacts and outcome.
[33] A small number of Sample Issuers reported their non-compliance with certain CPs (pursuant to paragraph A(c) of the MDRs) but did not properly explain, including by failing to identify proper reasons for non-compliance, and/or to address potential concerns arising from the non-compliance.
[34] As an example, a Sample Issuer reported full compliance but upon a closer review of its CG Report, that Issuer may have held less than four board meetings during the reporting period, which would mean the issuer had failed to comply with CP C.5.1.
[35] Issuers must do so pursuant to paragraph A(c) of the MDRs.
[36] A Sample Issuer erroneously interpreted CP C.6.1 as prohibiting external parties from acting as the company secretary. It should be noted that external providers are permitted.
[37] A small number of the Sample Issuers appeared to have relied on the old CG Code in effect prior to the 2022 Update, either by providing outdated CP references or by relying on outdated rules. For example, prior to the 2022 Update, it was (but no longer is) a CP requirement to appoint a non-executive director for a specific term. However, some Sample Issuers appeared to have interpreted CP B.2.2 as still requiring a specific term appointment for a director (and therefore indicating their non-compliance, when under the current CP, directors should be subject to retirement by rotation at regular intervals, advised to be 3 years.

## D. Recommended best practices

64. Notwithstanding the voluntary nature of recommended best practices ("**RBPs**"), we are pleased to note that some Sample Issuers have "gone the extra mile" to disclose against some (if not all) RBPs.

65. The RBPs are practices that should be embedded in issuers' behaviour for achieving the objectives of the Principles set out in the CG Code. Compliance with some of the RBPs is consistent with, and in many cases an extension of, existing MDRs or CPs[38]. They are intended to stimulate the board's thinking as to how they can carry out their role most effectively to enhance the issuer's corporate governance standards. While they may not be mandatory, adopting such practices demonstrates an issuer's commitment to a high level of corporate governance.

[38] For example, RBP D.2.8 which suggests an issuer's board to seek management confirmation of the effectiveness of the Internal Control System. Issuers are therefore encouraged to provide disclosure on confirmation obtained from management as part of the issuer's confirmation of the Internal Control System's effectiveness as required by paragraph H(c) of the MDRs. As another example, for maintenance of INEDs' independence, RBP E.1.9 which provides that remuneration given to INEDs should not contain equity-based or performance-linked components.

## APPENDIX I: SAMPLING METHOD

*Corporate governance report*

66. As at 31 December 2022, there were a total of 2,527 issuers listed on the Exchange. To conduct the 2022 Review, the Exchange excluded long suspended, recently delisted and secondary listed issuers and then randomly selected a sample of 400 of the remaining issuers. It divided the Sample Issuers into three categories of comparable size based on their market capitalization: 134 issuers in the large-cap category ("**Large-cap**") and 133 issuers in each of the mid-cap ("**Mid-cap**") and small-cap ("**Small-cap**") categories. The Sample Issuers represented approximately 15.8% of all listed issuers as at 31 December 2022.

67. Of the 400 Sample Issuers, 314 (78.5%) had a financial year ending on 31 December 2022, 83 (20.8%) had a financial year ending on 31 March 2023 and 3 (0.8%) had other financial year-ends[39].

*Long Serving INEDs*

68. The Exchange reviewed the disclosures made by 39 issuers (selected on a random basis from the Sample Issuers) that had proposed a resolution to re-elect one or more Long Serving INEDs at their 2023 AGM.

*Board diversity progress of Single Gender Board Issuers*

69. The Exchange divided Single Gender Board Newly Listed Issuers into (i) single gender board issuers that were primarily listed on the Exchange between July 2019 and December 2020; and (ii) single gender board issuers that were primarily listed on the Exchange between January 2021 and June 2022:

    (i) The Exchange had previously tracked the post-listing board diversity progress of single gender board issuers that were primarily listed on the Exchange between July 2019 and December 2020 in the 2021 Diversity Tracker. At the time of that review, 39 of these issuers were still single gender board issuers. The Exchange reviewed the board gender diversity disclosures made by 38 of these 39 issuers in their CG Reports for the 2021 financial year and the 2022 financial year. One issuer was excluded on the basis that it had not published its relevant CG Reports at the time of the Review covered in this paper; and

    (ii) Between 1 January 2021 and 30 June 2022, 20 single gender board issuers were primarily listed on the Exchange. The Exchange reviewed the prospectus disclosure made by these issuers and the board gender diversity disclosures in their CG Reports for the 2021 financial year and the 2022 financial year.

[39] The 3 Sample Issuers had financial year-ends on 28 February 2023 or 30 April 2023. Issuers with June financial year-end were not included in the 2022 Review as they had not published their CG Reports at the time of the Exchange's assessment.

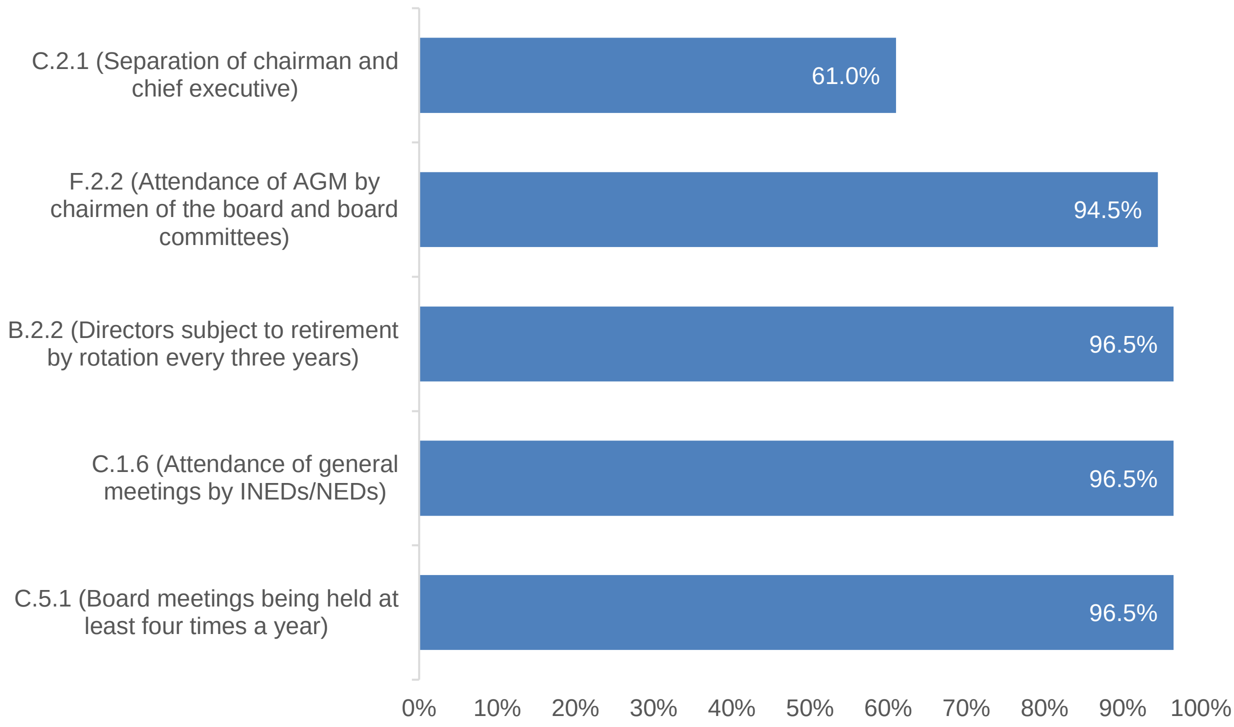
## APPENDIX II: STATISTICS ON CP COMPLIANCE

**Table 1: CP compliance[40] percentage by number of Sample Issuers**

| Number of CPs complied with | 2022 Review | | 2019 Review | | 2017/2018 | |
|---|---|---|---|---|---|---|
| | Number | Percentage | Number | Percentage | Number | Percentage |
| 78 | 197 | 49% | 163 | 41% | 144 | 36% |
| 77 | 161 | 40% | 152 | 38% | 144 | 36% |
| 76 | 25 | 6% | 48 | 12% | 67 | 17% |
| 75 | 7 | 2% | 24 | 6% | 20 | 5% |
| 74 | 6 | 2% | 9 | 2% | 11 | 3% |
| 73 | 2 | 0.5% | 4 | 1% | 5 | 1% |
| 72 | 0 | 0% | 0 | 0% | 5 | 1% |
| 71 | 0 | 0% | 0 | 0% | 2 | 0.5% |
| 70 | 0 | 0% | 0 | 0% | 0 | 0% |
| <70 | 2 | 0.5% | 0 | 0% | 2 | 0.5% |
| **Total** | **400** | **100%** | 400 | 100% | 400 | 100% |

[40] For the purpose of CP compliance rate, a CP is considered "not complied with" if a CG Report contained disclosure in respect of a required disclosure under the CP even if deviation from the CP is explained for. By way of an example, where the Sample Issuer provided explanation for not separating the roles of the chairman and the chief executive in compliance with CP C.2.1, CP C.2.1 is considered "not complied with" for the purpose of compliance rate.

**Table 2: Five CPs with the lowest compliance rates**



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