



CONSULTATION PAPER ON REVIEW OF THE ENVIRONMENTAL, SOCIAL AND GOVERNANCE REPORTING GUIDE AND RELATED LISTING RULES

The Law Society's Submissions

The Stock Exchange of Hong Kong Limited (the "Exchange") has issued a consultation paper on "Review of the Environmental, Social and Governance Reporting Guide and Related Listing Rules" on 17 May 2019. The Law Society makes the following submissions on the consultation questions posed.

Law Society's general response:

As a general comment, we welcome the Exchange's proposals to enhance board involvement in ESG governance and promote more meaningful ESG disclosures, thereby strengthening issuers' ESG practices. This is important at a time when such issues are increasingly relevant to investment decisions and of concern to the world. We have also raised some specific comments below for the Exchange's consideration, primarily to clarify certain aspects of the proposals so that issuers have a clearer understanding of how to apply the new rules and "comply or explain" obligations.

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?

Law Society's response:

Agreed. Shortening the timeframe for ESG reporting may (i) meet increasing investor demand for more timely ESG disclosures, (ii) potentially encourage a more senior level focus over ESG contents as they review and finalise the non-ESG contents of the annual report and (iii) bring it more in line with the equivalent requirement in the Singapore market (in fact, the proposed time frame would be more aggressive by one month compared to Singapore).

However, issuers must be given sufficient time to adjust, gear up for and implement any changes or improvements to their ESG assessment processes and governance structure, and to set and take steps to achieve the new targets under the environmental KPIs, before the new requirements come into effect. Those 60% of the sample issuers referenced in the consultation paper may continue to early report but other issuers (especially smaller issuers with fewer resources) might find it difficult to compile the ESG reports in accordance with the new requirements in parallel with their annual reports.

For the above reasons, the Exchange should (in a similar manner to the 2016/2017 changes to the ESG guide) consider a phased implementation of the amendments so that issuers can become more familiar with the new requirements in phases and allocate resources accordingly. Further, given the technical nature of the new requirements, the Exchange can consider issuing further guidelines or checklists and provide specific training to those involved in preparing of the ESG report, such as financial department personnel, company secretaries and financial / compliance advisers, in addition to directors.

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?

Law Society's response:

Agreed.

General

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

Law Society's response:

Agreed.

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?*

Law Society's response:

Agreed. In particular, we believe the proposed requirement for the disclosure of how the board reviews progress made against ESG-related targets should result in a higher level of board scrutiny over ESG data and targets.

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?

Law Society's response:

We agree with the substance of the note, but would like to clarify your intention of setting out this requirement in a note instead of in the MDR. Some of the disclosure items within the note do not appear to be an elaboration of the MDR, but are rather separate items.

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?

Law Society's response:

Agreed, except that it may be difficult for issuers to explain (in a meaningful way) how the Reporting Principle relating to "Balance" has been applied. We propose the Exchange issues further guidance to ensure meaningful disclosure in this respect.

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?

Law Society’s response:

We note that the disclosure requirement relating to the Reporting Principle on “materiality” is mandatory, but the wording refers to a disclosure of “the process and results of stakeholder engagement (if any)”. This appears to indicate that it is up to each issuer to decide whether and, if so, how to conduct stakeholder engagement, and a company may decide not to conduct any stakeholder engagement at all (for example, if it considers another method for assessing materiality to be more appropriate).

Please therefore consider if the mandatory disclosure should instead refer to the method for assessing materiality (with stakeholder engagement being a possible method). If the proposed wording is retained as a mandatory disclosure, please clarify whether any negative statement is required if no stakeholder engagement in fact took place during the year. We also suggest the Exchange provide further guidance on how “materiality” may be assessed.

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?*

Law Society’s response:

Agreed. To provide investors with more meaningful comparison of historical data, we suggest providing examples of “comparative data” as disclosure guidance for issuers, e.g. comparing the same data of the issuer in the past three years, comparing the issuer-specific data against industry averages or international standards.

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 report?

Law Society's response:

Agreed, although we suggest adding that the description of the process should require a brief outline of the factors taken into account in determining which entities or operations are included in the ESG report.

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?*

Law Society's response:

Agreed.

However, as the wording is very broad (covering any significant climate-related issues which *may* impact the issuer), please confirm whether an issuer who does not face specific climate-related issues (e.g. beyond a natural disaster of global scale) will be allowed, instead of complying with such disclosure requirements, to explain that there are no such issues specific to it.

We note from the consultation paper that climate-related issues could include change in policies, laws / regulations and market behaviour that increases costs, as well as natural disasters. We suggest the scope of such issues be clarified in an FAQ.

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?

Law Society's response:

Agreed.

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?

Law Society's response:

Agreed.

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

Law Society's response:

Agreed.

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?

Law Society's response:

Agreed. Please also consider including other types of engagement relationship, such as independent contractor.

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?

Law Society's response:

Agreed.

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.*

Law Society's response:

Agreed.

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?

Law Society's response:

Agreed, and it could be categorised into training given to directors / senior management and general staff. In addition, we suggest expanding the scope to include training on money laundering and counter-terrorist financing as these are often considered together with anti-corruption in the context of ESG.

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?

Law Society's response:

Agreed. The Exchange could also consider requiring the disclosure of the name of

the independent party giving the assurance and the assumptions adopted by the independent party.

The Law Society of Hong Kong
2 July 2019