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# Hong Kong Stock Exchange Publishes Consultation Conclusions On Environmental, Social And Governance Reporting

## Introduction

The Stock Exchange of Hong Kong (**SEHK** or **Exchange**) published its consultation conclusions (the **Consultation Conclusions**) on its proposed Environmental, Social and Governance Reporting Guide (the **ESG Guide**) on 31 August 2012.

In view of the growing importance of companies’ environmental, social and governance (**ESG**) performance and reporting internationally, the Exchange published a consultation paper (the **Consultation Paper**) on 9 December 2011 to seek comments on its proposed ESG Guide. Noting that most Hong Kong issuers are not actively engaged in ESG performance and reporting, the Exchange proposed to introduce the ESG Guide to raise ESG awareness among Hong Kong issuers and to provide reporting guidance for issuers with limited familiarity with ESG issues.

During the four-month consultation period which ended on 9 April 2012, the Exchange received 106 submissions from respondents including institutional investors, listed companies, business associations, non-governmental/ non-profit organisations as well as unlisted companies. Respondents welcomed the proposed introduction of the ESG Guide. The ESG Guide will be appended as Appendix 27 and Appendix 20 to the Listing Rules and GEM Listing Rules respectively, subject to amendments based on respondents’ comments.

The ESG Guide will be a recommended practice as opposed to a mandatory requirement and will apply to issuers with financial years ending after 31 December 2012. Subject to further consultation, the Exchange plans to increase the obligation level of certain recommended disclosures of the ESG Guide from recommended practice to “comply or explain” by 2015.

The Exchange does not expect listed issuers to report on all their operations and recommended disclosures in the ESG Guide from the start. However, issuers with capability are encouraged to go beyond the ESG Guide to adopt international reporting guidelines.

The Consultation Paper and the Consultation Conclusions are available on the Exchange’s website:

[Consultation Paper](http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201112.pdf)

[Consultation Conclusions](http://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201112cc.pdf)

Charltons’ newsletter on the Consultation Paper is [available here](/newsletters/hklaw/en/2012/144/nl-hklaw-20120203-144.html).

## Key Areas Of The Consultation Conclusions

### The Respondents

Among the 106 responses, 20 responses (19%) were from issuers. The Exchange expressed that while the response rate from issuers was low (approximately 1.3% of Hong Kong issuers), the attendance and feedback from the ESG seminars and workshops held by the Exchange in 2011 indicates that the business community is aware of the growing importance of ESG issues.

Responses from nine institutional investor respondents were received. One investor noted that it invests in over 100 Hong Kong issuers. The Exchange commented that the number of responses reveals that institutional investors are hoping to see more ESG disclosure from Hong Kong issuers.

### Areas and Aspects of ESG under the ESG Guide

The ESG Guide sets out four key subject areas for reporting: (A) Workplace Quality, (B) Environmental Protection, (C) Operating Practices and (D) Community Involvement. Corporate governance is not included as it is dealt with separately by the Code on Corporate Governance, Appendix 14 of the Listing Rules and Appendix 15 of the GEM Listing Rules.

Under each area there are three sections: aspect(s), general disclosure recommendations and Key Performing Indicators (KPIs) to measure ESG performance. The areas and aspects in the ESG Guide are as follows:

**Area A**

**Working Quality**

Aspect A1

Working conditions

Aspect A2

Health and safety

Aspect A3

Development and training

Aspect A4

Labour standards

**Area B**

**Environmental Protection**

Aspect B1

Emissions

Aspect B2

Use of resources

Aspect B3

The environmental and natural resources

**Area C**

**Operating Practices**

Aspect C1

Supply chain management

Aspect C2

Product responsibility

Aspect C3

Anti-corruption

**Area D**

**Community Involvement**

Aspect D1

Community investment

 It is reported that the majority of the respondents supported the ESG areas, although there were comments suggesting that “Operation practices” should not be included as such information could be disclosed elsewhere in corporate reporting. The Exchange responded that the “Operating practices” are not uncommon ESG topics. No amendments will be made to the areas and aspects of ESG.

### Level of Issuers’ Obligation and Effective Date

The majority of the respondents agreed with the Exchange that the ESG Guide should be a recommended practice rather than mandatory at this stage, while approximately 15% of the respondents comprising of individuals and unlisted companies responded that the ESG Guide should be mandatory or at least at a “comply or explain” level.

The Exchange considers it appropriate to introduce the ESG Guide as a recommended practice appended to the Listing Rules as it understands that many issuers do not understand ESG issues well enough yet.

There will be a transition period for the implementation of the ESG Guide and it will apply to issuers with a financial year ending after 31 December 2012. Subject to further future consultation, the Exchange plans to increase the level of obligation of some recommended disclosures to “comply or explain” by 2015.

### Level of Detail and KPIs Disclosure

There are a total of 34 KPIs under the four areas and 11 aspects for ESG reporting. It is reported that some respondents considered that some KPIs are not meaningful or may discourage issuers to report and some considered that the disclosure of KPIs are not objective measures of ESG performance and will encourage unproductive criticism of issuers by the media and special interest groups.

The Exchange considers that such KPIs could provide more guidance to help issuers to focus on the ESG issues that may be of interest to investors and their stakeholders. Moreover, disclosure of quantitative KPIs is in line with international practice. The Exchange opines that what is not measured is not monitored and managed and thus, reporting on KPIs is crucial for issuers to improve their performance on ESG issues.

The Exchange understands that the costs and administrative burden involved are of concern to issuers and suggests that issuers with resource constraints could start reporting on those KPIs that are material and relevant to their major operations. Accordingly, the KPIs have been maintained as part of the ESG Guide.

### International Guidelines and Standards

Some respondents commented that the ESG Guide should refer to, or align with, disclosure guidance under international ESG guidelines such as the Global Reporting Initiative’s Sustainability Report Guidelines, the Carbon Disclosure Project and the Greenhouse Gas Protocol as much as possible. The aim would be to: (1) lower administrative burden to issuers where there are inconsistencies between the KPIs and the other reporting guidelines; and (2) provide further guidance to issuers on how to start reporting by alignment with the international guidelines.

The Exchange indicated that it has referred to various guidelines/ standards when formulating the ESG Guide. However, the Exchange considers it inappropriate to simply refer to external guidelines that it has no control over and issuers who are unfamiliar with ESG reporting may find the international guidelines daunting.

In response to the comments of some of the respondents, the Exchange set out the references in Appendix III of the Consultation Conclusions and will set out useful references to the ESG Guide in the Frequently Asked Questions to be posted on the Exchange’s website.

### Workplace Diversity

Some respondents considered that the ESG Guide should include information on work place diversity, including gender information in the workplace and information specifically on the percentage of females, ethnicity, nationality and age profile of the board directors and senior management.

The Exchange responded that it notes the growing importance of workplace diversity but that this is being considered as a separate exercise and will not be added to the ESG Guide at this stage.

### Assurances

The Exchange is mindful of the additional costs that seeking external assurance on ESG reports may impose and the proposed ESG Guide does not therefore recommend the seeking of external assurance. The majority of the issuer and business association respondents agreed with the Exchange while most of the investor and private practitioner respondents expressed opposite views.

The Exchange agrees with one respondent that the ESG Guide should not leave out the assurance aspect and the Exchange will mention in the ESG Guide that issuers may consider offering assurance on their ESG reports.

### Tone

Some respondents suggested that the ESG Guide could use a stronger tone such as using “encouraged to” rather than “may” in the ESG Guide.

The Exchange considers that normative language is not preferred at this stage and will maintain the overall tone of the ESG Guide except that the Exchange will encourage issuers to:

1. state in the ESG report which entities in the group and/ or which operations have been included for the report to avoid being misleading;
2. continue to report once they start reporting;
3. explain how the KPIs are calculated so that readers can interpret the KPIs which are not defined in the ESG Guide; and
4. prioritise ESG subject areas, aspects and KPIs to show that issuers have carefully considered their ESG strategies and are not using the ESG Guide as a check-list.

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