

Client Alert

December 2019

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Listed company's ESG reporting obligation will be upgraded after 1 July 2020

Summary

On 18 December 2019, The Stock Exchange of Hong Kong Limited (SEHK) published (a) the [Consultation Conclusions on the Review of the Environmental, Social and Governance Reporting Guide \("ESG Guide"\) and related Listing Rules \("Consultation Conclusion"\)](#), and (b) the [Analysis of Environmental, Social and Governance Practice Disclosure in 2018 \("ESG Disclosure Review"\)](#). SEHK adopts the amendments to the Rules Governing the Listing of Securities on the SEHK ("**Listing Rules**") and the ESG Guide proposed in its [Consultation Paper](#) with modifications to reflect market responses. SEHK will implement the amendments to the Listing Rules and the ESG Guide for **financial years commencing on or after 1 July 2020**.

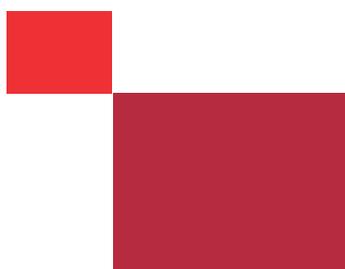
SEHK reminds issuers that it is important for the board to take the lead and get involved in Environmental, Social and Governance (ESG) reporting from the outset. Issuers are recommended to (a) get familiarise with the new requirements set out in the Consultation Conclusions; (b) start the process to implement the necessary reporting infrastructure as early as possible before the commencement of the relevant financial year to allow fine-tuning of the infrastructure based on experience and feedback from stakeholders; (c) consider SEHK's recommendations set out in the ESG Disclosure Review when preparing their ESG Reports; and (d) review [SEHK's ESG resources](#). SEHK will launch a new set of director e-training on ESG reporting, update the step-by-step guide to ESG reporting: "How to Prepare an ESG Report?", the frequently asked questions and links to other resources.

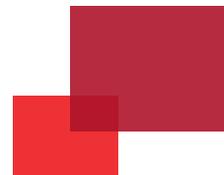
Background

Internationally, various stock exchanges, regulators and supranational organisations (e.g. European Union) have made recommendations and guidelines to enhance listed issuer's reporting of environmental information. Locally, the Securities and Futures Commission (SFC) has recently published the findings of its surveys on integrating ESG factors and climate risks in asset management, which forms part of its initiative mentioned in its paper entitled "Strategic Framework for Green Finance". Under the current trend, SEHK will continue to strengthen the emphasis on ESG for both listing applicants and listed companies.

Key Amendments to the Listing Rules and ESG Guide

Key amendments are summarized below. All references are to the Main Board Listing Rules unless otherwise stated and the amendments apply equally to the GEM Listing Rules.





Part I - Amendments to the Listing Rules

A. Shorten the publication timeframe of ESG Report

Current requirements	New requirements
Rule 13.91 requires an issuer to disclose information set out in the ESG Guide in the annual report, in a separate report or on the issuer's website within three months after publication of the issuer's annual report.	Rule 13.91(5)(d) is amended to encourage issuers to publish the ESG report at the same time as the publication of the annual report. In any event, the issuer should publish the ESG report as close as possible to and no later than <u>five months after the end of the financial year</u> .

B. Paperless ESG Reports and notifications to shareholders

Current requirements	New requirements
No clear guidance on whether issuers are required to send printed form of the ESG reports to shareholders.	Rule 13.91(5) is amended to clarify that irrespective of whether a shareholder has elected to receive the issuer's corporate communication electronically or otherwise, where the ESG report does not form a part of an issuer's annual report, the issuer is <u>not</u> required to provide a printed form of the ESG report to shareholders unless responding to their specific requests. Issuers are required to notify shareholders that the ESG report has been published on SEHK's and the issuer's websites.

Part II - Amendments to the ESG Guide

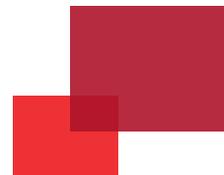
In the ESG Guide, the two levels of disclosure obligations are changed to :

- (a) **Mandatory disclosure requirements** (Part B of the ESG Guide) - An issuer must include such information for the period covered by the ESG report.
- (b) **"Comply or explain" provisions** (Part C of the ESG Guide) - If the issuer does not report on one or more of these "comply or explain" provisions, it must provide considered reasons in its ESG report.

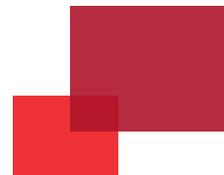
All recommended disclosures (i.e. voluntary disclosures) are upgraded to "comply or explain" provisions. References to "recommended disclosures" are deleted in the amended ESG Guide.

A. Introduce mandatory disclosure requirements

Current requirements	New mandatory disclosure requirements
Governance structure - Paragraphs 8-10 of the ESG Guide states that the board has overall responsibility for	Board statement - New Paragraph 13 of the ESG Guide is introduced to



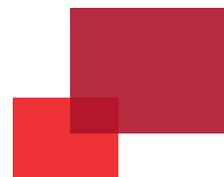
<p>the issuer's ESG strategy and reporting, including evaluating and determining the issuer's ESG related risks. In addition to the requirements of the ESG Guide, issuers are required under the Hong Kong Companies Ordinance to include, in their Directors' Reports, a discussion of their environmental policies and performance including environmental laws and regulations that have a significant impact on them.</p>	<p>require a statement from the board containing the following elements :</p> <ul style="list-style-type: none"> (a) a disclosure of the board's oversight of ESG issues; (b) the board's ESG management approach and strategy, including the process used to evaluate, prioritise 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 with an explanation of how they relate to the issuer's businesses.
<p>Reporting principles - The ESG Guide sets out reporting principles (including materiality and quantitative) that are said to underpin the preparation of an ESG report, informing the content of the report and how information is presented.</p>	<p>New Paragraph 14 of the ESG Guide is introduced to require a description of, or an explanation on, the application of the following Reporting Principles in the preparation of the ESG report :</p> <p>Materiality - The ESG report should disclose: (i) the process to identify and the criteria for the selection of material ESG factors; (ii) if a stakeholder engagement is conducted, a description of significant stakeholders identified, and the process and results of the issuer's stakeholder engagement.</p> <p>Quantitative - 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) should be disclosed.</p> <p>Consistency - The issuer should disclose in the ESG report any changes to the methods or key performance indicators (KPIs) used, or any other relevant factors affecting a meaningful comparison.</p>
<p>Reporting boundary - Paragraph 10 of the ESG Guide provides that an ESG report should state which entities in the issuer's group and/or which operations have been included in the report.</p>	<p>New Paragraph 15 of the ESG Guide is introduced to require a narrative explanation of the reporting boundaries of the ESG report and a description of the process used to identify which entities or operations are included in the ESG report. If there</p>



	is a change in the scope, the issuer should explain the difference and reason for the change.
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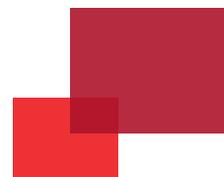
B. Introduce aspect on climate change and revise environmental KPIs

Current requirements	New requirements
<p>Climate change - No requirement to disclose how climate change impacts issuers.</p>	<p>A new Aspect A4 is introduced, which consists of:</p> <ul style="list-style-type: none"> (a) General disclosure - 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. <p>SEHK reiterates that the disclosure obligation under the new Aspect on climate change, like all other Aspects in the ESG Guide, is on a "comply or explain" basis. Accordingly, if an issuer considers that climate change is not material to its business and operations, an explanation of that fact in the ESG report will suffice .</p>
<p>Targets - ESG Guide requires issuers to disclose "results achieved" from their initiatives to reduce emissions/waste, but not targets.</p>	<p>The environmental KPIs are revised to require disclosure of:</p> <ul style="list-style-type: none"> (a) a description on targets set regarding emissions, energy use and water efficiency, waste reduction, etc. and steps taken to achieve them; and (b) Scope 1 and Scope 2 greenhouse gas emissions. <p>SEHK reminds issuers that all Environmental KPIs are subject to "comply or explain" provisions. Issuers are only required to disclose and set targets for Environmental KPIs that are considered material to them.</p>
<p>Emissions - ESG Guide requires issuers to disclose greenhouse gas emissions in total and the intensity. Listing Rules do not require disclosure of emissions by scope types but FAQs encourage issuers to report on emission by scope.</p>	<p>SEHK reminds issuers that all Environmental KPIs are subject to "comply or explain" provisions. Issuers are only required to disclose and set targets for Environmental KPIs that are considered material to them.</p>



C. Upgrade the disclosure obligation of the social KPIs

Current requirements	New requirements
<p>The Social KPIs of the ESG Guide are recommended disclosures (i.e. voluntary disclosures).</p>	<p>Upgrade the disclosure obligation of all Social KPIs to “comply or explain”.</p> <p>If any of the Social KPIs is considered immaterial to an issuer's businesses, the issuer should explain rather than making irrelevant disclosures.</p>
<p>Employment type - Issuers are recommended to disclose total workforce by gender, employment type, age group and geographical region.</p>	<p>Amend KPI B1.1 to clarify that "employment types" should include "full- and part-time" staff. "Full- and part-time staff" are non-exhaustive examples of employment types.</p>
<p>Rate of fatalities - Issuers are recommended to disclose the number and rate of work-related fatalities for the reporting year.</p>	<p>Amend KPI B2.1 to require disclosure of the number and rate of work-related fatalities occurred in each of the past three years including the reporting year.</p>
<p>Supply chain management - Issuers are recommended to describe practices relating to engaging suppliers, number of suppliers where the practices are being implemented and how they are implemented and monitored.</p>	<p>Introduce new KPIs B5.1 - B5.4 to require disclosure of a description of practices used to :</p> <p>(a) Identify the environmental and social risks along the supply chain, and how they are managed and monitored; and</p> <p>(b) Promote environmentally preferable products and services when selecting suppliers, and how these practices are implemented and monitored.</p> <p>Issuers should consider how far down the supply chain the disclosure should encompass in light of materiality and appropriateness in their own circumstances. In some cases, disclosure of issuers' direct suppliers may be sufficient.</p>
<p>Anti-corruption - Issuers are recommended to disclose the following KPIs:</p> <p>(a) Number of concluded legal cases regarding corrupt practices brought against the issuer or its employees during the reporting period and the outcomes of the cases.</p> <p>(b) Description of preventive measures and whistle-blowing procedures, how they are implemented and monitored.</p>	<p>Introduce a new KPI B7.3 to require a description of anti-corruption training provided to directors and staff.</p> <p>The ESG Guide only sets out the minimum parameters for ESG reporting. SEHK encourages issuers to disclose additional information they consider appropriate and material under this KPI, such as the number of directors or staff trained, the content and the outcomes of the anti-corruption training.</p>



D. Encourage independent assurance on ESG Report

Current requirements	New voluntary requirements
Paragraph 7 of the ESG Guide provides that the issuer may consider obtaining assurance on its ESG report.	Introduce a new Paragraph 9 in Section A of the ESG Guide to state that issuers may seek independent assurance to strengthen the credibility of the ESG information disclosed. Where independent assurance is obtained, the issuer should describe the level, scope and processes adopted for assurance given clearly in the ESG report. SEHK reiterates that issuers are encouraged, but not required, to seek independent assurance.

Recommendations in the ESG Disclosure Review

SEHK suggests the following key areas on how issuers can continue to enhance their ESG reporting in the future :

- (a) **Board-level engagement** - Describe (i) the board's oversight of ESG issues; (ii) the board's role in identifying, evaluating and managing material ESG issues; and (iii) how the board reviews progress on ESG issues.
- (b) **Materiality assessments** - Conduct the materiality assessment and demonstrate the existence and thoroughness of the exercise in the ESG report.
- (c) **Considering every provision** - Cover each and every provision in the ESG Guide. If a provision is considered as immaterial, make a statement to that effect with sufficient explanation of its determination of immateriality.
- (d) **"Comply or explain" - both are acceptable options** - If a "comply or explain" provision is not material to an issuer, "explanation" is not a less preferred or secondary option. It is better to say so, and for the issuer to demonstrate that it has fully thought through what applies to them in a material way, and what does not.

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