

INTERPRETATION

of the ESG Consultation Conclusions



'The ultimate test of man's conscience may be his willingness to sacrifice something today for future generations whose words of thanks will not be heard.'



On 18 December 2019, The Stock Exchange of Hong Kong Limited (the Exchange) published the conclusions to its consultation on the ‘Review of the Environmental, Social and Governance (ESG) Reporting Guide (ESG Guide) and Related Listing Rules’ (ESG Consultation Conclusions), making revisions on the content of existing ‘Listing Rules’ and the ‘ESG Guide’. The amendments will apply to issuers’ ESG reports for financial years commencing on or after 1 July 2020.

The focuses of this revision by the Exchange were mainly on building the corporate ESG framework, mandating the disclosure of the role the Board plays in its engagement in ESG risks management, encouraging the exploration of the links between climate change and corporate sustainable development, and furthering the application of the principle of Materiality in the disclosure of ESG performance and report preparation.

ESG CONSULTATION CONCLUSIONS

KEY REVISIONS OF THE LISTING RULES

01

A board statement setting out the board’s consideration of ESG issues

Opportunities for Company:

Undoubtedly, ESG related risks have been playing an increasingly pivotal role to enterprises in recent years, which are not only reflected in aspects such as corporate financial performance and compliance management, but in the spotlight of companies that seek long-term healthy and sustainable development. In the market of risks and opportunities being co-existent, the effective corporate sustainability governance structure and board leadership are necessary and believed as an indispensable part of companies avoiding relevant risks and providing stakeholders confidence about the execution of their long-term strategies.

Challenges & Solutions for Directors:

It is the major problem to most enterprises that inadequate skills and knowledge about ESG and ambiguous goals of ESG management are the obstacles ahead of them. To address concerns about global sustainability trends and corporate ESG risks management the board faces, GreenCo suggests that the management and the board of issuers establish a corporate ESG governance structure and goal setting system more efficiently through a comprehensive stakeholder engagement. The provision of ESG training and seminars is of great value as well. This practice will allow companies to implement strategic policies and ESG information management in a transparent and standardised manner.

An explanation of how issuers have applied the Reporting Principles ‘Materiality’, ‘Quantitative’ and ‘Consistency’

02

Opportunities for Companies:

Making the Reporting Principles transparent is conducive to issuers meeting the disclosure requirements and understanding better the purpose and value of ESG reporting. Despite the unnoticeable benefits of revealing the application process of the Reporting Principles to enterprises per se, the profits brought to investors who have conducted objective evaluation and analysis on the non-financial data across different geographic locations, industries over time based on the standardised and harmonised reporting principles would be enormous should enterprises effectively follow the principles of Materiality, Quantitative and Consistency in reporting.

Challenges & Solutions for Directors:

Applying the Reporting Principles seems much easier than disclosing the process in which these principles have been applied to most enterprises. The difficulty of expounding the principles and the attempt to elaborate them in various ways might be the challenge to enterprises. GreenCo suggests that issuers take time to read and comprehend the new requirements listing rules, general disclosure and key performance indicators first. With the basic understanding of the new requirements, issuers need to analyse and categorise the objectives and methods of the application of principles, thereby mastering how to match up the principles with the information that will be disclosed.

An explanation of the reporting boundary and identification process for including specific entities or operations in ESG reports

03

Opportunities for Companies:

Outlining the reporting scope helps readers to gain a clear understanding of and make comparisons of the quantitative and qualitative data in reports, on which investors can see a bigger picture of the extension and limitation of the company's ESG performance. Meanwhile, it allows issuers to grasp the point of disclosed information more flexibly and precisely and lower the uncertainty during data organisation and collection process if boundary issues can be resolved.

Challenges & Solutions for Directors:

More often than not which standard to adopt and how to apply it to the reporting process are questions perplexing enterprises in the boundary setting process. Enterprises usually do not have definite views about what businesses they ought to integrate into the reports. GreenCo suggests that enterprises take into consideration the following three points in the boundary setting process:

- The selected reporting scope does not omit relevant information that substantively influences stakeholder assessments and decisions (e.g. investors, governmental departments, employees, etc.), or that reflects material economic, environmental and social impacts;
- Adopt the standard on which the organisation and reporting boundaries are determined with adequate reasoning (e.g. Equity Share Approach, Control Approach, etc.);
- Provide more relevant information in annual reports, such as the business disclosure in different business segments and geographical locations.



04

Requiring disclosure of significant climate-related issues which have impacted and may impact the issuer. Specifically, it regulates the policies on identification and mitigation of significant climate-related issues which have impacted, and those which may impact, the issuer, and description of the actions taken to manage them

Opportunities for Companies:

Climate change is a topic determining the characteristics of our era. The impacts of global warming on enterprises in certain industries are long-lasting and existent. Along with the increasing demand for environmentally friendly assets by investors, the provision of valid and accurate information around how enterprises tackle climate change-related risks appears to be an unavoidable point in disclosure. To enterprises themselves, the evaluation of the implications of climate change on the value chain and product/service lifecycle scientifically with tools such as scenario-based analysis can assist them to understand and substantially enhance their resilience to climate-related risks in the industry to which they pertain.

Challenges and Solutions for Directors:

In the long run, both physical risks and transition risks may pose threats to the profitability, asset valuation, financial health and brand reputation of an enterprise to varying degrees. If companies do not pay attention to their risk management or look at climate change from a long-term investment perspective, they may be jeopardised by policy changes, climate risks and market fluctuations more likely and seriously. Thus, GreenCo suggests that enterprises carry out a self-examination that facilitates them to garner a deep understanding of the climate-related risks they are confronted with by referring to the TCFD recommendations.

Amend environmental key performance indicators regarding disclosure of relevant targets, including the goal setting in emissions, energy consumption, water efficiency and waste management

05

Opportunities for Companies:

It is helpful for enterprises to transition from 'Disclosure for Compliance' to 'Effective Management' by revising and detailing part of indicators under environmental subject. This also prompts companies to establish a sustainability management system and platform in an incremental manner, on which the environmental performance of the company can be traced and evaluated dynamically. Gradually quantifying corporate environmental policies with forward-looking data, in the long term, drives investors to obtain a better understanding of the corporate vision in sustainable development and the corporate practice echoing the direction of travel of United Nations Sustainable Development Goals.

Challenges and Solutions for Directors:

It goes without saying that mandating the small and medium-sized enterprises and financial institutions, to disclose environmental results, such as greenhouse gas emissions in a scientific way is not easy. The inaccurate result and inappropriate targets set by the companies may indirectly lead to the lower quality of entire reports and lower level of comparability. What GreenCo suggests for enterprises which lack the knowledge in carbon accounting and statistics is to adopt relevant international standards and guidelines, such as ISO14064 and Greenhouse Gas Protocol, or consult qualified experts who can provide professional services in data management.

06

Upgrade the disclosure obligation of all social KPIs to 'comply or explain'

Opportunities for Companies:

In the 'Analysis of Environmental, Social and Governance Practice Disclosure in 2018', a material published together with the ESG Consultation Conclusions, it can be seen that a majority of sample issuers were reporting many key performance indicators under social subject. With the upgrading of the disclosure obligation under social subject to 'comply or explain', the disclosure of aspects such as talent management, supply chain risk control and anti-corruption policy execution can allow enterprises to review their performance and insufficiency in policy implementation and forging sound corporate culture. Investors, in the meantime, would also benefit from being presented with a more comprehensive picture showing the performance of the enterprise's risk management.

Challenges and Solutions for Directors:

The new key performance indicators would add some burden to small and medium-sized enterprises in respect of policy execution and information summarisation and disclosure. GreenCo suggests that issuers provide adequate training to ESG management teams and individuals who are responsible for corporate ESG issues, strengthen internal communication and coordination, and create data management platform that supports companies to collect and organise relevant data systematically. It is time to build your own ESG data management platform and information gathering tool for cost saving and law compliance in the long term.

Shortening the deadline for publication of ESG reports to within five months after the financial year-end

Opportunities for Companies:

The 'Analysis of Environmental, Social and Governance Practice Disclosure in 2018' shows that most sample issuers chose to publish their ESG reports on the same day as they published their annual reports (approximately 63%). To investors, shortening the publication timeframe of ESG reports in line with or as close as possible in time to the publication of annual reports strikes the right balance between improving timeliness and relevance of ESG reporting. Such integration of non-financial information into corporate financial information enables investors to make more informed decisions. Further, it is the new timeframe that ensures that enterprises have sufficient time for data collection and verification while allocating more resources to the optimisation of the Group's sustainability system and efficient implementation of ESG-related policies, a result that pushes enterprises to put more focus on the ESG reports and establish a full process for data collection, submission, verification, summarisation and disclosure.

Challenges and Solutions for Directors:

There is no denying the fact that the upcoming publication timeframe will to some extent influence the ESG reporting management and preparing process of issuers, which may cause the decline of reporting quality due to the short of staff or poor data management. GreenCo's tip is to follow a process of "Organisation, Plan, Boundary Setting, Kick-off Meeting, Research, Compilation, Publication and Summing-up". GreenCo recommends issuers to establish a set of scientific and applicable process for reporting, and highlight the importance of the logic of action and complete ecology in fulfilling corporate social responsibilities.

08 Encouraging issuers to seek independent assurance to strengthen the credibility of ESG information disclosed

Opportunities for Companies:

The purpose of encouraging a third-party quality assurance is to improve the credibility of ESG reports, bridge the gap between issuers and stakeholders in mutual trust, and increase the availability of information disclosed. The information disclosed about an enterprise's sustainable development encompasses a series of quantitative and qualitative performance, which are usually not measured in monetary units. Therefore, their accuracy and representativeness without verification can hardly be guaranteed. With the application of systemic assurance standards, enterprises can achieve:

Increased recognition and credibility; Reduced data quality risks and the opening of a new era of report value management; Improved board and management level involvement; Strengthened internal reporting and management systems; Improved stakeholder communication that facilitates issuers per se a better understanding of national strategy, social needs, positioning in the industry and the company's original intentions.

Challenges & Solutions for Directors:

The primary barriers impeding issuers from seeking a third-party assurance in the future during the preparation of ESG reports are cost and uneven levels of assurance by verifiers. GreenCo suggests that enterprises familiarise themselves with internationally accepted standards for assurance that are suitable to their industries in the first place before performing evaluations of the professional background and service process of independent verifiers and making appropriate arrangements. Moreover, enterprises should build a diligent and efficient working team that takes initiatives to gather information and make contact with external parties, while providing a sound working environment and technical support to third-party verifiers.

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