New Era of Climate Disclosure for Hong Kong Listed Companies

25 April 2024

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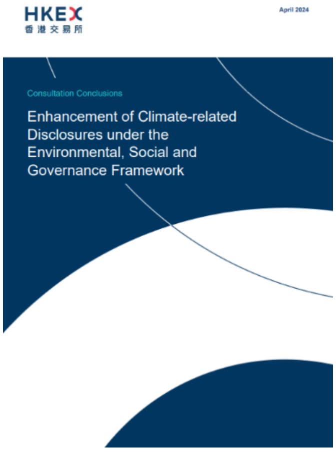

EXECUTIVE SUMMARY

- On 19 April 2024, the Hong Kong Stock Exchange ("HKEX") released the Consultation Conclusions on *Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework* (following on from a Consultation Paper issued in April 2023) laying out new requirements in respect of climate-related disclosures ("New Climate Requirements")
- The requirements are aligned with *IFRS S2 Climate-related Disclosures* ("IFRS S2") to the maximum extent possible
- The HKEX has put in place a phased approach to implementation of the new requirements based on tiers of issuers (large cap issuers, main board issuers other than large cap issuers and GEM issuers) ("Phased Approach")
- A number of different implementation reliefs have been put in place in order to ease the difficulties of compliance for issuers
- HKEX issuers now have final clarity on the New Climate Requirements and will be able to focus efforts on practical steps needed to deal with the challenge of being ready to meet the new reporting requirements

Introduction & background

On 14 April 2023, the HKEX published a Consultation Paper seeking views on proposals to amend its ESG reporting framework, which is predominantly set out in Appendix C2 to the Main Board Listing Rules and GEM Listing Rules, to mandate that listed issuers make climate-related disclosures based on the then proposed IFRS S2 in their ESG reports. Since that date:

- the International Sustainability Standards Board ("ISSB") finalised its proposals with the issuance in June 2023 of *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information* ("IFRS S1") and IFRS S2 aiming to serve as the global baseline of sustainability reporting standards for entities worldwide to prepare consistent, comparable and reliable sustainability disclosures.
- In July 2023, the International Organization of Securities Commissions endorsed the IFRS Sustainability Disclosure Standards ("IFRS SDS") and called on its member jurisdictions to consider ways in which they might adopt, apply or otherwise be informed by the IFRS SDS within the context of their jurisdictional arrangements.
- In February 2024, the IFRS Foundation published the ISSB Adoption Guide Preview, which suggests a focus on publicly accountable entities and allows jurisdictional regulators to classify these entities into different market tiers with reference to thresholds such as an issuer's size, volume of traded securities or liquidity, and consider an accelerated introduction of the requirements of the IFRS SDS for the more advanced market tiers.
- In March 2024, the Hong Kong Government's Financial Services and the Treasury Bureau ("FSTB") published a statement ("Vision Statement") setting out the vision and approach of the Government and financial regulators towards developing a comprehensive ecosystem for sustainability disclosure in Hong Kong. In particular, the Hong Kong Institute of Certified Public Accountants ("HKICPA") will assume the role of the sustainability reporting standard setter in Hong Kong to develop local sustainability reporting standards aligned with the IFRS SDS as well as complementary application and implementation guidance.
- On 12 April 2024, under the auspices of the China Securities Regulatory Commission ("CSRC"), the Shanghai Stock Exchange, the Shenzhen Stock Exchange and the Beijing Stock Exchange issued the guidelines for the sustainability reporting of listed companies

Taking account of these developments and responding to feedback of constituents to the Consultation Paper (which contained strong support for the proposals though with a number of constituents calling for closer alignment with the final IFRS SDS), the HKEX published on 19 April 2024 the Consultation Conclusions which adopt all the proposals in the Consultation with certain modifications to reflect the requirements of IFRS S2 to the maximum extent possible. In addition, concurrently with the publication of the Consultation Conclusions, the HKEX also published an Implementation Guidance which, among other things, contains the conceptual foundations and general requirements of IFRS S1 (see later section "Implementation Guidance and IFRS S1" for details).

Core Content of the climate-related disclosures

The existing requirements of Parts B and C of the ESG Code (formerly ESG Guide) have been largely retained (with exception of the requirements on Scope 1 and 2 greenhouse gas ("GHG") emission being moved to Part D). A new Part D of the ESG Code of Appendix C2 of the Main Board Listing Rules and GEM Listing Rules (however for further details see section below "Effective date and the Phased Approach") sets out the detailed new disclosure requirements across the four core pillars used in the IFRS SDS: governance; strategy; risk management; and metrics and targets. Some key areas of disclosure as per the requirements are listed in the below table:

Governance

• Information about the issuers body(s) or individual(s) responsible for oversight of climate-related risks and opportunities including:
  • how the body/individual determines whether appropriate skills and competencies are available,
  • process and frequency of being informed on climate-related risks and opportunities,
  • consideration of climate-related issues when overseeing strategy, decisions on major transactions and risk management and related processes (including consideration of trade-offs),
  • monitoring of progress towards targets related to climate-related risks and opportunities and linkage of related performance metrics with remuneration policies
• Management's role in the governance processes, controls and procedures used to monitor, manage and oversee climate-related risks and opportunities, including:
  • whether the role is delegated to specific management level position/committee and how oversight is exercised
  • whether management uses controls and procedures to support the oversight of climate-related risks and opportunities and whether these are integrated into other internal functions

Strategy
• Information regarding climate-related risks and opportunities that could reasonably be expected to affect the issuer's cash flows, its access to finance or cost of capital over the short, medium or long term[1] • Information regarding current and anticipated effects of climate-related risks and opportunities on business model and value chain • Information regarding the effects of climate-related risks and opportunities on its strategy and decision-making including how the issuer has responded to, and plans to respond to, climate-related risks and opportunities in its strategy and decision-making, information about its current and anticipated adaptation and mitigation efforts, how it plans to achieve any climate-related targets, any climate-related transition plan as well as progress of such plans disclosed in previous reporting periods • Qualitative and quantitative information about how climate-related risks and opportunities have affected an issuer's financial position, financial performance and cash flows for the reporting period and where in respect of such risks and opportunities there is a significant risk of a material adjustment within the next annual reporting period to the carrying amounts of assets and liabilities • Qualitative and quantitative information about how the issuer expects its financial position, financial performance and cash flows to change over the short, medium and long term, given its strategy to manage climate-related risks and opportunities[1] • Issuers assessment of climate resilience including scenario analysis[1] to show resilience of the issuer's strategy and business model to changes, developments and uncertainties taking into consideration the issuer's identified climate-related risks and opportunities
Risk Management
• Issuer's process and related policies used to identify, assess, prioritise and monitor climate-related risks and opportunities, including whether and how the issuer uses climate-related scenario analysis, the extent to which and how the processes are integrated into overall risk management process
Metrics and Targets
• Scope 1 and 2 GHG emissions • Scope 3 GHG emissions[1] • Further information regarding the measurement and composition of the Scope 1, 2 and 3 GHG emissions, location-based Scope 2 GHG emissions and categories included in Scope 3 GHG emissions • Other cross-industry metrics regarding climate-related transition risks[1], physical risks[1], climate-related opportunities[1] and related capital deployment • Information regarding use of internal carbon prices • Whether and how climate-related considerations are factored into remuneration policy

- Industry-based metrics
- Qualitative and quantitative climate-related targets the issuer has set to monitor progress towards achieving its strategic goals and any targets the issuer is required to meet by law or regulation including any GHG emission targets
- Information about the issuer's approach to setting and reviewing each target and how it monitors progress against each target
- Information about the issuer's performance against each climate-related target and an analysis of trends or changes in the issuer's performance

[1] With implementation reliefs provided (see below section "Implementation Reliefs with respect to specific climate-related disclosures" for more details)

The full text of the amendments to the Listing Rules that implement the New Climate Requirements can be found in Appendix III (with respect to Main Board Listing Rules) and Appendix IV (with respect to GEM Listing Rules) of the Consultation Conclusions.

Implementation Guidance and IFRS S1

In support of the New Climate Requirements, the HKEX has issued Implementation Guidance for Climate Disclosures under HKEX ESG reporting framework ("Implementation Guidance") to assist issuers in understanding, interpreting and implementing the new requirements. The Implementation Guidance:

(a) sets out principles, guidance and illustrative examples for the implementation of the New Climate Requirements,

(b) refers issuers to step-by-step workflows, external frameworks and tools which would be helpful in the preparation of disclosures and

(c) references the IFRS SDS (for example the relevant reporting principles under the IFRS S1 and the IFRS S2 application guidance) insofar as they are relevant/applicable; with respect to this Appendix VI of the Consultation Conclusions sets out the relevant IFRS S1 reporting principles and the location of corresponding discussions in the Implementation Guidance.

While the Implementation Guidance does not constitute part of the Listing Rules, the HKEX does encourage issuers to refer to and apply the Implementation Guidance when preparing their climate-related disclosures under the new requirements. The Implementation Guidance was developed with the intent of assisting issuers to better prepare for the eventual adoption of local Hong Kong Sustainability Reporting Standards (see later section "Future steps by HKEX: local Hong Kong sustainability standards, assurance and other issues").

Effective date and the Phased Approach

The ISSB Adoption Guide Preview published by the IFRS Foundation in February 2024 sets out proportionality and phasing in measures for the application of IFRS SDS with reference to an issuer's size, trading volume and liquidity, allowing jurisdictional regulators to classify issuers into different market tiers and consider an accelerated introduction of the IFRS SDS for more advanced issuers. Taking into account market readiness of HKEX issuers and leveraging on these proportionality and phasing in measures, the HKEX is adopting a Phased Approach that segregates issuers into: Large Cap Issuers, Main Board Issuers (other than Large Cap Issuers) and GEM Issuers with different levels of disclosure required from different effective dates according to such tiered approach. The below table shows a summary of the effective dates for the requirements with differentiation into the various tiers:

New Climate Requirements Effective Date		
	Disclosure on Scope 1 and Scope 2 GHG emissions	Disclosure other than Scope 1 and Scope 2 GHG emissions
LargeCap Issuers[2]	Mandatory disclosure	• **"Comply or explain"**: in financial years commencing on or after 1 January **2025**

	(Financial years commencing on or after 1 January 2025)	• **Mandatory disclosure**: in financial years commencing on or after 1 January **2026**
Main Board Issuers (other than LargeCap Issuers)		**"Comply or explain"** (Financial years commencing on or after 1 January 2025)
GEM Issuers		**Voluntary disclosure** (Financial years commencing on or after 1 January 2025)

[2] Hang Seng Composite LargeCap Index constituents

The table above only summarises issuers' disclosure obligations under Part D of the ESG Code. Non-climate disclosure requirements set out in Parts A to C of the ESG Code will continue to apply. All issuers must continue to report on the relevant provisions in their ESG reports. In particular, GEM issuers shall continue to make climate-related disclosures pursuant to Aspect A4: Climate change of Part C of the ESG Code on a "comply or explain" basis.

Implementation Reliefs with respect to specific climate-related disclosures

The HKEX acknowledged concerns expressed by some constituents regarding the difficulties and challenges of complying with some of the disclosure requirements proposed in the Consultation Paper. In response, the new requirements do contain a number of implementation reliefs originating from the IFRS SDS ("Implementation Reliefs") designed to address concerns over the reporting challenges that some issuers may face by virtue of a lack of resources and/or technical knowledge and expertise/other difficulties. A summary of the Implementation Reliefs is contained in the below table:

Relevant New Climate Requirements	Implementation Relief			
	Reasonable Information Relief	Capabilities Relief	Commercial Sensitivity Relief	Financial Effects Relief
All paragraphs with respect to climate-related opportunities			√	
Identification of climate-related risks and opportunities	√			
Determination of the scope of the value chain	√			
Quantification of current and anticipated financial effects		√ (anticipated financial effects only)		√
Preparation of disclosures on anticipated financial effects	√	√		
Use of climate-related scenario analysis	√	√		
Measurement approach, inputs and assumptions of Scope 3 GHG emissions	√			

Calculation of metrics in particular cross-industry metric categories	√			

Comparing the amended Listing Rules with IFRS S2

The requirements of the new Part D of Appendix C2 to the Main Board Listing Rules reflect the requirements of IFRS S2 (including the reliefs contained in that Standard) to the maximum extent possible. The HKEX has stated that an ESG report prepared in compliance with the IFRS SDS (i.e., both IFRS S1 and IFRS S2) will be considered to have complied with Part D of the ESG Code. Appendix V of the Consultation Conclusions contains a table comparing the requirements of IFRS S2 and the provisions of the HKEX's ESG Code including the New Climate Requirements. In addition to Appendix V, our observations stemming from a comparison of the New Climate Requirements (as per Part D of Appendix C2 of the Main Board Listing Rules) with the requirements of IFRS S2 (operating in conjunction with IFRS S1) are contained in the table below:

Part D of Appendix C2 of Main Board Listing Rules as compared to IFRS S2 (operating in conjunction with IFRS S1)
• Aligned to the requirements of IFRS S2 to the maximum extent possible; with only limited differences remaining including: a) Disclosure of Scope 1 and Scope 2 GHG emissions for the consolidated accounting group and other investees separately is encouraged but not mandatory b) Disclosure of percentage of remuneration linked to climate-related considerations is not required c) Where an issuer's activities include asset management, commercial banking or insurance, the issuer is encouraged to disclose additional information about the issuer's Category 15 GHG emissions or those associated with its investments (financed emissions), but this is not mandatory d) An issuer is encouraged but not required to disclose industry-based metrics that are associated with one or more particular business models, activities or other common features that characterise participation in an industry • Implementation Reliefs are introduced which are largely similar to practical exemptions provided in IFRS SDS, for example, Reasonable Information Relief, Commercial Sensitivity Relief and Capabilities Relief • Materiality: Para 11 within Part A the HKEX ESG Code (which contains general reporting principles applicable to all Parts) continues to define materiality as the threshold at which ESG issues determined by the board are sufficiently important to investors and other stakeholders that they should be reported (with materiality therefore not confined to financial materiality), while IFRS SDS are based on a concept of material information focused on whether information could reasonably be expected to influence decisions that primary users of general purpose financial reports make on the basis of those reports, which include financial statements and sustainability-related financial disclosures (i.e. financial materiality). In the Consultation Conclusions, the HKEX states that the Listing Rules do not prevent the board from applying a financial materiality threshold (as required under the IFRS SDS) in determining disclosure of a climate-related risk or opportunity. Indeed para 11 has been amended to state that for the purpose of Part D of the ESG Code, an issuer must disclose information about climate-related risks and opportunities that could reasonably be expected to affect its cash flows, its access to finance or cost of capital over the short, medium or long term. At the same time, the HKEX makes clear that issuers are allowed to prepare disclosures for the purposes of the New Climate Requirements under the double materiality approach to provide additional disclosures to meet the need of its stakeholders. • Reporting Boundary: Para 15 within Part B of the HKEX ESG Code contains a requirement for narrative explaining the reporting boundaries of the ESG report and describing the process used to identify which entities or operations are included in the ESG report. The HKEX states in the Consultation Conclusions that while it has no intention to change the reporting principles or other requirements (including the reporting boundary) at this juncture, issuers are encouraged to follow the IFRS SDS and align the scope of entities or operations that are included in the ESG report (including the climate-related disclosures) with that of its financial statements. • Effective date is 1 January 2025 and a Phased Approach is introduced; while the effective date of IFRS SDS is 1 January 2024 with limited transition provisions provided

Comparing the amended Listing Rules with the PRC sustainability reporting guidelines for listed companies

On 12 April 2024, under the auspices of the CSRC, the Shanghai Stock Exchange, the Shenzhen Stock Exchange and the Beijing Stock Exchange issued the guidelines for the sustainability reporting of listed companies ("PRC Guidelines for sustainability reporting"), which contain extensive requirements applicable on a mandatory basis to constituents of certain stock indices on certain of those exchanges and available for voluntary adoption by remaining entities listed on those exchanges. Entities listed on one of those exchanges preparing a sustainability report per the guidelines, which are also listed on the HKEX (and therefore subject to the requirements of the Part D of Appendix C2 of the Listing Rules) will need to comply with both sets of requirements in respect of their listings on the respective exchanges. Whilst the mainland stock exchange requirements do draw on international practice and experiences elsewhere there are some differences in the requirements as compared to the HKEX requirements. The following table provides a summary of the most significant commonalities and differences:

PRC Guidelines for sustainability reporting as compared to Part D of Appendix C2 of Main Board Listing Rules
• Similar disclosure requirements across the four core pillars and climate-related disclosures • Disclosure requirements are categorised into mandatory, encouraged and voluntary • Disclosure of climate-related scenario analysis, anticipated financial effects and Scope 3 GHG emissions is not mandatory • Measurement of GHG emissions: The PRC Guidelines for sustainability reporting do not prescribe any measurement method, whereas the GHG Protocol is the default measurement methodology under the IFRS SDS • Other than GHG emissions, the PRC Guidelines for sustainability reporting do not prescribe other cross-industry metrics • Specific disclosure requirements are made for designated topics, such as Resource Utilization and Circular Economy and Rural Revitalization and Social Contributions, and non-designated topics that are considered material in terms of impact • Effective date is 1 May 2024 and listed companies shall publish the first sustainability report (i.e. 2025 report) before 30 April 2026, with early adoption encouraged

Further information in relation to the IFRS SDS and PRC sustainability reporting guidelines for listed companies are available in here and here respectively.

Future steps by HKEX: local Hong Kong sustainability standards, assurance and other issues

As part of the Vision Statement published by the FSTB, the government has targeted the launch in 2024 of a roadmap on the appropriate adoption in Hong Kong of IFRS SDS as appropriate, taking into account Hong Kong's position on the global green finance map, as well as local regulatory expectations and circumstances. Specifically, the HKICPA will assume the role of the sustainability reporting standard setter in Hong Kong to develop local sustainability reporting standards aligned with the IFRS SDS as well as complementary application and implementation guidance. When these are available, the HKEX will consider whether and how to transition towards sustainability reporting in accordance with those local standards, including whether to replace our current ESG regulatory framework with a straightforward Listing Rule requirement directing listed issuers to publish sustainability reports in accordance with those standards (consistent with the approach adopted for financial reporting). When the HKEX consults the market on the implementation of the local standards, it will also consider whether and how to align the non-climate disclosures requirements under the ESG Code with those standards. The HKEX states in the Consultation Conclusions that until that time, the New Climate Requirements serve as an interim step to prepare issuers towards sustainability and climate reporting in accordance with the local standards as contemplated under the roadmap.

Consistent with the proposals in the Consultation Paper, the HKEX will not at present require independent assurance for ESG information as a globally accepted assurance standard has yet to be developed with the International Audit and Assurance Standards Board ("IAASB") working on this. However, the HKEX notes that the Vision Statement expects that local sustainability-related assurance and ethics standards will be developed, taking into account latest global developments, including those from the IAASB. When such local standards are available, the HKEX will assess the readiness of issuers and the local ESG ecosystem, and consider requiring independent assurance for sustainability information in accordance with such local standards. In the meantime, issuers are encouraged to seek independent assurance to strengthen the credibility of ESG information disclosed, and make relevant disclosures when such assurance is obtained (for further information refer to Question 23 of HKEX's Frequently Asked Questions Series 18).

The HKEX has provided, and will continue to provide, training resources and materials via its ESG Academy, a one-stop educational platform, to assist issuers with their ESG reporting. It has also stated that it will provide further guidance and training as appropriate, based on its observations and review of issuers' compliance.

Practical considerations for issuers regarding implementation

Diagnose & Assess	Plan	Communicate
• Assess interactions between HKEX's New Climate Requirements and the applicability of other sustainability-related disclosure requirements and frameworks that the group may be subject to; e.g. US SEC's rules for climate-related disclosures, EU's Corporate Sustainability Reporting Directive, the PRC's Guidelines for sustainability reporting and GRI standards • Clarify reporting requirements and timelines in accordance with the Phased Approach • Seek advice from Deloitte professionals on areas of complexity (e.g. scenario analysis, reporting of financial effects and Scope 3 GHG emissions) • Assess the implications of climate disclosures and how these can be integrated into the governance structure, strategy setting, risk management and internal controls • Identify key gaps and implications for systems, personnel, data and processes, and liaise with key business functions to identify the correct data owners and assess data readiness for the new qualitative and quantitative disclosure requirements • Consider the Implementation Reliefs given the limitation of resources and capability of the issuers • Assess new information (e.g. other cross-industry metrics like percentage of assets vulnerable to transition/physical risks and capital expenditure deployed towards climate risk) to be disclosed under the HKEX's New Climate Requirements	• Consider a phased implementation approach to build capacity for climate-related scenario analysis, quantification of financial impacts of climate-related risks, and measurement of GHG emissions (Scope 1, Scope 2, and Scope 3 emissions) • Develop a plan to operationalise the capture, measurement, review and reporting of climate-related information • Enhance governance and controls related to ESG data and disclosures; document the processes around data collection, review, consolidation and calculation using relevant emission factors • Consider if strategic plans and roadmaps for broader climate mitigation and adaption action need to be updated as part of the climate risk assessment process • Plan for engagement of appropriate external expertise, if needed to help with implementation or assurance over the reported information • Budget and allocate resources for climate-related information disclosures and assurance, if necessary	• Support the C-Suite, Audit Committee and Board to understand the implications of the proposed requirements and upskill the management and the board around strategic ESG priorities • Consider how key stakeholders are kept informed of new information and developments from reviewing, preparing and disclosing against the HKEX's New Climate Requirements and how this can support better strategic decision making and risk review • Build organisational capacity, enhance operating models and strategic change management activities • Communicate data requirements with relevant internal stakeholders and process owners • Connect relevant stakeholders, including financial reporting and sustainability

Indicative implementation Roadmap

Short Term	Mid Term	Long Term
• Conduct a gap analysis against the disclosure requirements • Improve climate-related governance structure and processes • Conduct peer benchmarking and market research on climate-related strategy, risk management and disclosures and assess your readiness • Identify climate-related risks and opportunities and conduct climate scenario analysis • Identify organisational boundaries, map the value chain and assess Scope 3 emissions inventory • Consider setting climate-related targets • Consider integrating climate-related considerations into remuneration policies	• Conduct in-depth climate scenario analysis and quantify the financial impact of physical and transition risks • Collect relevant data and measure Scope 3 emissions • Disclose qualitative cross-industry indicators • Develop climate-related goals and action plans • Integrate climate-related considerations into remuneration policies	• Refine the quantification of the financial impact of physical and transition risks • Incorporate climate-related financial impacts into reporting and integrate climate considerations into business strategy and risk management process • Disclose quantitative cross-industry indicators and industry-specific indicators • Implement key mitigation strategies across the value chain • Monitor and review the process towards, and targets related to climate-related risks and opportunities and make adjustments, if needed

Contact us to continue the conversation

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