CFA Institute

CFA Society Hong Kong

By Email (consultationsupport@hkex.com.hk)

14 July 2023

8/F, Two Exchange Square,
8 Connaught Place, Central,
Hong Kong

Dear Sir/Madam,

RE: CONSULTATION PAPER - ENHANCEMENT OF CLIMATE-RELATED DISCLOSURES UNDER THE ENVIRONMENTAL, SOCIAL AND GOVERNANCE FRAMEWORK

Covering letter

CFA Institute[1] and CFA Society Hong Kong[2] appreciate the opportunity to respond to the Hong Kong Exchanges and Clearing ('HKEX')'s proposal on Enhancement of Climate Disclosure Under Its ESG Framework (the 'Proposal'). We are providing comments in line with our missions of promoting fair and transparent capital markets and safeguarding investors' interests. An integral part of our efforts is to ensure that corporate financial disclosures – and the related assurance – intended for investors and other stakeholders are of high quality. Our advocacy position and standard of reporting are informed by our global membership, which invests both locally and globally.

Overall, we support the spirit of the Proposal. Investors want to expand the scope of value-relevant information to include climate-related risks and opportunities for investment decision-making. We know from 60-plus years of advocating on behalf of investors that what gets disclosed gets monitored, measured, and managed — not only by investors but also by management. This Proposal rightly brings climate-related risks into the sphere of improved information for investment decision-making, the perspective from which we respond. We also specifically draw upon the perspectives outlined in the 2022 CFA Institute response to the US Securities and Exchange Commission's The Enhancement and Standardization of Climate-Related Disclosures for Investors.

We applaud HKEX for developing this extensive Proposal, including its prior efforts to engage with end users of the Proposal and understand market-specific needs, which enables Hong Kong to be

[1] CFA Institute is a global, not-for-profit professional association of more than 181,000 members, as well as 160 member societies around the world. Members include investment analysts, advisers, portfolio managers, and other investment professionals. CFA Institute administers the Chartered Financial Analyst® (CFA®) Program.

[2] CFA Society Hong Kong (the 'Society') is a non-profit organization founded in 1992 as the Hong Kong Society of Financial Analysts by a group of CFA Charterholders. The Society shares the mission of CFA Institute in raising the professional and ethical standards of financial analysts and investment practitioners through our advocacy and continuing education efforts. In addition to promoting the CFA designation in Hong Kong, the Society aims to provide a forum for our members, CFA Institute, other investment practitioners and regulators for networking and the exchange of industry insights and best practices.

an early adopter – and adapter – of the International Sustainability Standards Board ('ISSB') baseline. We note HKEX is adopting a market-focused approach with standard-setter thinking and technical methodology. This allows flexibility for issuers in more challenging areas, such as climate-related targets, industry-based metrics, and alternative disclosure during interim periods. With that, we acknowledge the HKEX has localized ISSB in certain areas to incorporate Hong Kong-relevant nuances, in order to stay competitive as a financial hub and attract capital raising, keeping in mind that other markets in the region are working in a similar timeline.

HKEX has also advanced the conversation and discourse of climate-related disclosures in Hong Kong and other markets, especially in the Asia-Pacific region. This also includes the impact of climate-related disclosures on securities analysis and investment decision-making — among all the stakeholders who invest in, participate as public companies, and support global companies in accessing the Hong Kong capital market. The proposed enhancement from comply-or-explain to mandatory disclosure, coupled with a comment period following the issuance of exposure drafts ('Exposure Draft') of the ISSB's IFRS S2 Climate-related Disclosures ('IFRS S2'), has captured the attention of market participants and provided them with the opportunity to deliberate. The HKEX has unequivocally improved the understanding regarding the integration of climate-related disclosures in the investment decision-making process, and irrespective of the outcome of this Proposal, this is a valuable outcome for those who have engaged in the process.

The questions presented in the Proposal are relatively broad and are path-dependent. As such, responses to each question may depend, for example, on whether the HKEX undertakes rulemaking or delegates its authority to an independent standard-setting body, and where the information is located, and therefore the degree to which it can be assured. Additionally, we highlight our core perspectives below:

Perspectives that inform our response

i. Securities Analysis and Selection

Our response to the Proposal aligns with the approach to all corporate disclosure consultations — which stems from the perspective of an analyst or buy-side value-driven investor. In this vein, we advocate standard setters give more weight to studies that shed light on value relevance from the perspective of investors, who are a key group of financial report users.

The history of CFA Institute and the CFA Program is rooted in the provision of information for investment decision-making. Specifically, our foundational principles with respect to ESG disclosures, borrowed from the CFA Institute response to Accountancy Europe's publication/consultation Interconnected Standard Setting for Corporate Reporting, are:

- Long-Term Value Creation and Integrated Reporting

- We note that the intended audience of the information are investors and other stakeholders. Also, the objective of the report is to enable value-driven decision-making and long-term value discovery.
- Non-financial Information May Need Clarification or Rebranding
    - For instance, while we support the spirit of Question 12 of the Proposal to link the discussion of climate-related risks to their financial impacts, the non-financial nature of GHG emission metrics — with no required disclosure to quantify the cost of reducing them — may reduce the practicality and resulting effectiveness.
- Reporting Is Communication: Know Your Audience (Investors) and Communication Objective (Financial Value Creation)
    - We understand that entities with smaller scale and lesser resources, such as GEM (Growth Enterprise Market) Board issuers, would take a longer time to reach that level of reporting in full compliance. Thus, as we commented in Question 29, we suggest a disclosure framework with consideration for the diverse capabilities and the resulting resource gaps between the issuers of the Main Board and GEM Board.
- Materiality
    - This informs our responses to the Proposal, especially Questions 3 and 12, which we will explain later. While we understand the relative priority of HKEX (i.e., climate-related risk elements come first), we believe climate-related risks and opportunities should be measured and disclosed so long as they are material.
- Location of Information Matters
    - We note that this Proposal is concerned with general-purpose reports.
- Funding
- Where to Start: Investors

ii. Value- vs Values-based investors

Meanwhile, we also note that investors are not monolithic on ESG and climate issues, and their views are contingent upon whether they prioritize value or values-based investing objectives. Given this dynamic, investors must need and seek information, especially when managing funds on behalf of others, that is sufficiently disciplined to discern the difference and evaluate the trade-offs, between value and values, that may arise in this context. Our responses to this Proposal are not developed from a public policy or civil society objective, but rather from investors' demand on value-relevant information and fiduciary responsibility of our members to their clients.

iii. Global Convergence of Climate-Related Disclosures

We have long expressed support for efforts to achieve global accounting standards, and we support the Proposal to extend this effort to climate reporting standards, given that investing is global, and comparability is the lifeblood of investment analysis. Similarly, we have supported the creation of the ISSB for the same reasons.

While we highlight our support for the intention of HKEX to substantially incorporate the ISSB's IFRS S2 to its Proposal, we also address the challenges associated with such an approach, such as knowing the audience for, as well as the objective, location, and materiality of, ESG and climate disclosures. In addition, we support the disclosure of common metrics across industries, complemented by industry-specific metrics.

iv. Use of Third-Party Frameworks and Standard Setters

As an investor organization, we have spent decades advocating for the creation of accounting standards that are useful to investors. We believe these standards should be issued by independent organizations that are adequate in their funding; have a fair board composition that takes into account the interests of all stakeholders; focus on investors (users) as the primary audience for such information; and have a transparent and fair agenda setting and due process, including public meetings, consultations, as well as active engagement with users and investors of the information in the standard-setting process.

As we consider the leveraging of these standards, the current snapshot approach brings about a few practical implications regarding the development of the framework (i.e., in a manner consistent with independent standard-setting to serve the interests of investors, not prudential regulators) and how Task Force on Climate-Related Financial Disclosures ('TCFD') is maintained as the requirements may evolve over time. Said differently, will the TCFD framework shift while the HKEX rule remains static, because it is currently anchored on the TCFD framework? We believe the HKEX should consider whether the Proposal will require ongoing updates as it is taking a snapshot of these standards at this moment in time, and there is no mechanism for updating outside of changes in the HKEX's requirements, relative to the scrutiny and interpretation that will inevitably arise alongside a wider adoption of the underlying standards in the Hong Kong capital market.

v. Evolutionary vs. Revolutionary Approach

We recommend the HKEX adopt an evolutionary approach rather than a revolutionary approach, considering also other financial reporting priorities for investors. It is important for issuers and investors to recognize the evolving nature of the disclosures to meet investors' needs, as information becomes available and investors become more aware of ESG risks, including their measurement metrics and integration to investment decision-making. "ESG is not a stable molecule," and thus the need for rulemaking will not likely be once and done. We will continue to refine our thinking globally — through a review of these proposals, engagement with investors, and possibly a member survey on ESG matters[3] — and to mitigate lingering skepticism around climate-related disclosures. Overall, we recommend HKEX adopt an evolutionary approach to constantly reflect the changing dynamics and needs of the market.

[3] CFA Institute conducted a survey to collect members' views on ESG matters in November 2021. chrome-extension://efaidnbmnnnibpcajpcglclefindmkaj/https://www.cfainstitute.org/-/media/documents/survey/cfa-esg-survey-web.pdfCFA Institute conducted a survey to collect members' views on ESG matters in November 2021. chrome-extension://efaidnbmnnnibpcajpcglclefindmkaj/https://www.cfainstitute.org/-/media/documents/survey/cfa-esg-survey-web.pdf

vi. Relevance vs. Reliability

What we have learned from decades of engaging with investors is that relevance always takes precedence over perfect reliability. Investors do not want to forego timely and relevant information in favor of waiting for perfectly reliable information. This is why investors support fair value over amortized cost, the latter of which is highly reliable but lacks relevance in investment decision-making. Our message here is that while reliability is important, it is not to the degree at which it deters the provision of relevant information. This informs our support for Scope 3 emission disclosures, which should be expressed as ranges and provided even without verification.

Conclusion

We believe our responses have balanced investors' immediate needs for relevance over reliability, with issuers' needs to develop systems and controls to gather information and ensure that appropriate safe harbors protect their ability to provide relevant information. We also support the adoption of global baseline, while addressing Hong Kong-relevant nuances, to make the work of issuers and investors easier so that the allocation of capital and investment decision-making process can happen with the least amount of friction and regulatory arbitrage possible.

Thank you for your consideration of our views and perspectives. We welcome and appreciate the opportunity to meet and provide you with more details on our letter. If you have any questions or seek further elaboration on our responses, please contact Matthew Chan at matthew.chan@cfahk.org or Sivananth Ramachandran, CFA, CIPM at sivananth.ramachandran@cfainstitute.org. CFA Institute and members of CFA Society Hong Kong contributed to the content of this letter.

Sincerely,

For an on behalf of CFA Institute

Sivananth Ramachandran, CFA, CIPM
Director, Capital Markets Policy,
CFA Institute

For and on behalf of CFA Society Hong Kong

Matthew Chan
Managing Director,
CFA Society Hong Kong

Response to specific question

Question 1: Do you agree to upgrade climate-related disclosures to mandatory from "comply or explain"? Please provide reasons for your views.

We recognize the urgency of addressing climate change and the global commitment to this endeavor. As such, we support the proposal to make climate-related disclosures mandatory for issuers, which will provide investors with the necessary information, regarding the climate-related risks and climate resilience of issuers, to make informed decisions. In addition, this would promote climate awareness and contribute to our shared goal of achieving carbon neutrality.

CFA Institute strongly supports this, as issuers will be less likely to comply but more likely to explain otherwise[4]. Generally, the assessment of materiality is not to be fully made under the "comply or explain" regime, and the explanation remains highly generic. It is our long-standing view that what gets disclosed gets measured.

However, as we transition to mandatory disclosure, it is essential to ensure that the disclosure is accurate, reliable, and relevant. Based on our experience, this may be achieved through a mechanism driven by market forces and/or regulatory authority. Unfortunately, from a market-driven perspective, carbon markets and sustainable investing are still in their nascent stages. Therefore, relying solely on market forces may not be sufficient to incentivize issuers to diligently disclose climate-related risks, opportunities, and goals. As such, the issue of greenwashing, low-quality disclosures, and enforcement remains a challenge.

Considering that climate change affects not only investors, but also a wide range of stakeholders, we urge HKEX and relevant authorities to examine possible mechanisms, including a comprehensive regulatory framework, for ensuring accountability and enforcement. This will help maintain the quality of disclosures and mitigate agency problems.

As a step forward or as an interim measure, we suggest that HKEX leverage the existing financial reporting mechanism and regulatory framework to require the issuers to also disclose the material climate-related risks and opportunities and related material financial information contained in the ESG report in their audited financial statements. This can provide a safeguard and audit assurance for the quality and reliability of the relevant climate-related risks and opportunities disclosures.

By integrating the disclosure of climate-related risks and opportunities into the financial statements of issuers, it would establish a link between disclosures inside and outside financial statements. Such that investors can have a more comprehensive understanding of the risks and opportunities

[4] In the "survey of CFA Institute members on latest ESG matters" in 2021, as a baseline question, we asked our investors/members whether sustainability (ESG) reporting should be mandatory or voluntary for public companies. By a wide majority (54%), respondents wanted minimum disclosures pursuant to formal regulatory standards of sustainability reporting with the flexibility to supplement with voluntary disclosures, and we believe the trend will continue.

exposure of the issuers to support their investment decisions. In addition, with the review by the auditors, this will help improve the consistency and quality of disclosures among issuers.

Overall, we believe that the inclusion of climate-related information in financial statements is a positive step or an effective interim measure towards the purpose of climate-related disclosures, particularly given the absence of adequate market- or regulatory-driven mechanisms at this stage.

(A) GOVERNANCE

Question 2: Do you agree to introduce new governance disclosures focusing on climate-related issues as set out in paragraph 1 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. It is crucial that issuers have a robust corporate governance framework to oversee their progress on climate-related targets and management of climate-related risks.

We suggest that issuers should disclose the identity of the designated key individual or chairman of the committee responsible for climate-related matters.

Paragraph 1 of Part D of the Proposed Appendix 27 only requires the disclosure of the board committee or board members responsible for overseeing climate-related risks and opportunities, without specifying the chairman or key individual with that responsibility. This may weaken accountability on climate-related matters. Also, such a disclosure requirement is inconsistent with the requirement in Appendix 14E (b) of the Corporate Governance Code that issuers are required to disclose the identity of the chairman of the committee of the corporate governance function.

In addition, issuers should disclose the identity and qualifications of external experts who have given opinions or advice in the ESG Report. While the board has ultimate responsibility for ESG matters, it is important that investors have a clear understanding of the expertise and credentials of external experts who have contributed to the ESG Report.

This approach is similar to the existing disclosure requirement in relation to an expert's opinion or advice in transaction or listing documents and is a way to enhance accountability and transparency in ESG reporting.

While we support disclosure requirements on board oversight, we would like to highlight the following referenced from CFA Institute Climate Letter to SEC[i]:

- Quality of compliance: TCFD has observed little compliance with the relevant disclosures. This raises concerns about enforcement.
- Need for board authorship: we recommend board authorship (on top of oversight) for this section to ensure this includes a sufficient level of detail by those responsible and in attendance at such meetings.

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- Proportionality of needed expertise: We think the need for climate expertise is industry- and company-dependent and that these provisions, or their application, need to consider this proportionally.

(B) STRATEGY

Question 3: Do you agree to require disclosure of climate-related risks as set out in paragraph 2 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. Even issuers can now legitimately say investor demand for information has reached critical mass[5], investors have told us that this is a climate risk they seek to price, and they would like the information to do so. Among all, we believe disclosures should be made if there will be impacts or significant changes to business operations. Hence, we support disclosure of material climate-related risks, by location if possible, considering time horizons.

In accordance with paragraph 2 of Part D of the Proposed Appendix 27, issuers are required to disclose material climate-related risks. Materiality can be interpreted in different ways, such as financial materiality, double materiality, or dynamic materiality. The definition of materiality provided in paragraph 11(i) of Part A of Appendix 27 states that it is the threshold at which ESG issues determined by the board are sufficiently important to investors and other stakeholders that they should be reported. On the other hand, HKEX has recommended that issuers consider the "double materiality perspective" and "level of impact the activities have on the environment and society" when assessing materiality in its "How to prepare an ESG Report" and "Appendix 1: Toolkit – materiality and relevance." However, the examples provided in paragraph 56 of the Proposal appear to focus on financial materiality.

Given the above, we are concerned that the materiality concept of the Proposed Appendix 27 is ambiguous and inconsistent. To enable investors to make informed decisions, we suggest HKEX clarify the materiality interpretation they are referring to in the Proposed Appendix 27, and whether financial materiality, double materiality, or dynamic materiality should be applied in determining disclosure requirements throughout the Proposed Appendix 27.

Paragraph 2 of Part D of the Proposed Appendix 27 also requires issuers to disclose information regarding their time horizon. We support this requirement as it aids in year-on-year and competitor comparisons, as well as assisting investors in estimating future cash flow prospects.

However, given the varying business models and life cycles across industries, we suggest that HKEX provides guidance on the definition of short-term, medium-term, and long-term. In the context of climate-related disclosures, the time horizons are generally very long-term, and providing broad parameters would be useful for investors to assess related uncertainties over these time horizons. We suggest that ranges of short-term (1–3 years), medium-term (4–5 years), and long-term (6–10 years) would be appropriate. Issuers requiring more long-term capital expenditure plans (e.g.,

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[5] The 2020 climate-specific survey included within the Climate Change Analysis in the Investment Process report highlighted more specifically the investors' desire and request, but lack of information, to incorporate climate-related risks into the investment decision-making process.

utilities or transportation industries) can define their own horizons with proper disclosure of the basis. This would enable investors to better understand the time horizons applicable to the business and assess the related uncertainties.

Meanwhile, we seek clarification on the definition of 'Transition risk', which will be further explained in Question 20 (a) of the response. For instance, it could be changes in the expected useful life of assets across time horizons. Issuers should also describe the nature of the risk, including whether it relates to regulatory, technological, market (including changing consumer, business counterparty, and investor preferences), liability, reputational, or other transition-related factors[6].

We note that Appendix A of the IFRS S2 provides guidance on acute and chronic climate-related physical risks. In order to facilitate better understanding for investors and preparation for issuers, we suggest HKEX consider offering similar guidance.

Going forward, we also recommend making disclosure of climate-related risks within an issuer's value chain, i.e., where in its value chain risks are concentrated. However, obtaining such information and verifying its veracity is likely to be challenging. Investors need to understand that the nature of such information may be substantially less reliable than the information controlled by the company. Like Scope 3 emissions and impacts from suppliers (i.e., cost implications), this information is likely significant but difficult to capture and of varying degrees of quality.

Question 4: Do you agree that issuers may opt to disclose the actual and potential effects of climate-related opportunities they may have identified in response to climate-related risks disclosed as set out in paragraph 3 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Disagreed. We believe, from the investors' perspective, it is the "materiality" of impacts that matters rather than the "types" of impacts (risks or opportunities). We refer the scope of climate-related opportunities to those that are material and already embedded in a visible plan.

In particular, if the issuer is promoting its stock in venues, forums, publications, and investor pitches by highlighting its climate-related opportunities, then the disclosure of these opportunities should be required in the issuer's ESG report. This would ensure that investors have access to the same information about climate-related opportunities that the issuer is using to promote itself and make informed investment decisions.

[6] HKEX: How to prepare an ESG Report.
HKEX: Appendix 1: Toolkit – materiality and relevance.
Appendix of CFA Institute's Comment Letter to ISSB.

Question 5: Do you agree that an issuer shall consider the applicability of and disclose the metrics when assessing and making disclosure of climate-related risks and opportunities as set out in paragraph 4 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

We suggest that HKEX consider mandating the disclosure of cross-industry and industry-based metrics in paragraph 4 of Part D of the Proposed Appendix 27.

The proposed seven cross-industry metric categories, aligned with the TCFD's Guidance on Metrics, Targets, and Transition Plans, offer a standardized set of climate-related disclosures that are applicable to most types of companies. We support the adoption of greater comparability of disclosures across industries and business models. We suggest that HKEX provide implementation guidance with examples of the types of information that would be relevant for each category, to help issuers meet the requirements of the cross-industry metric categories.

We note that HKEX's proposal does not mandate the disclosure of industry-based metrics but instead encourages issuers to consider the industry-based disclosure requirements under other international ESG reporting frameworks and make disclosures as they see fit. Investors typically make asset allocation decisions and organize their portfolios by industry, and climate risks impact industries differently. Therefore, applying and disclosing industry-based metrics can result in greater comparability of disclosures both within and across industries, leading to similar judgments regarding the most material risks and opportunities within an industry. Therefore, we suggest HKEX consider mandating the disclosure of industry-based metrics for climate-related disclosures to be most meaningful. We discuss additional nuances on this topic in our response to Question 26.

In addition, we suggest HKEX consider requiring issuers to disclose metrics – other than those mentioned by Paragraphs 13 to 22 of Part D of the Proposed Appendix 27 – that the governance body or the issuer uses to measure, monitor, and manage climate-related risks and opportunities, if they are material. This would provide investors with more transparency.

Question 6: Do you agree to require disclosure of how the issuer is responding to climate-related risks and, where an issuer chooses to, any climate-related opportunities as set out in paragraph 5 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. The required disclosure will facilitate investors' understanding of whether the issuer has a plan and whether it may be effective in the short, medium, and long term in achieving the transition. Presently, many companies have made net-zero commitments by 2050 but have made little, if any, disclosures regarding how they plan to get there. This requirement would necessitate that they do so. Possible angles include policies that restrict GHG emissions and the imposition of a carbon price.

To enhance the comparability and consistency of issuers' disclosure about their climate-related transition risk, we suggest HKEX incorporate the IFRS S2 requirement for the issuer to disclose the assumptions it made in developing its climate-related transition plan and the dependencies on which the plan's achievement relies. Investors need to understand the assumptions and dependencies of the transition plan in order to assess its credibility and be able to make comparisons among issuers.

It would be best to commence with a section relevant to climate-related risk disclosures, with a cross-reference to other sections regarding strategies, responses, and implementation plans, to enhance the connectivity of the reported information.

Question 7: Do you agree to require disclosure of climate-related targets set by the issuer as set out in paragraph 6 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. The Hong Kong SAR government has pledged to achieve carbon neutrality by 2050, while Mainland China aims to have CO2 emissions peak before 2030 and achieve carbon neutrality before 2060. Therefore, it is essential for all issuers to set climate targets as soon as possible to mitigate the transition risk ahead.

We believe that the proposed disclosure requirement of qualitative and quantitative targets for plans set by the issuer and those required by local law is important because it will give investors the information they need to judge the validity of the issuer's claims and plans related to climate change. Such commitments elucidate information for investors with respect to

1) the management's intent and strategy in reducing GHG emissions,
2) the associated cost, and
3) more quantifiable progress towards achieving the milestones.

Additionally, we support the requirement for disclosing gross emission targets, intended use of carbon credits, and net emission targets separately, and whether the credits will be subject to a third-party credit verification or certification scheme. This enables investors to gain insight into the issuer's approach to reducing GHG emissions and the role of carbon credits in the issuer's net GHG emissions targets. We suggest HKEX require issuers to disclose the third-party scheme(s) responsible for verifying or certifying carbon credits, as best practices.

We noted that for each GHG emissions target disclosed, IFRS S2 requires an entity to disclose the type of GHG and the scope (Scope 1, Scope 2, or Scope 3) covered. We suggest HKEX adopt similar disclosure requirements to enhance transparency and consistency across greenhouse gas emissions reporting.

We acknowledge the challenges in deciding and, therefore, disclosing climate-related targets. This will take a longer time, especially for issuers whose headquarters located in jurisdictions with weak climate awareness. The same challenge goes to GEM Board issuers which are without sufficient resources and skill sets on climate matters, even at the board level. On top of that, supply chain emission data collection is complicated (e.g., supply chain issues, need for non-public company data, estimations, delays in reporting, and materiality application questions), which poses practical difficulties to issuers in setting climate-related goals and targets. Meanwhile, we believe there should be no material incremental disclosure costs incurred by issuers, as HKEX does not mandate issuers to have climate-related targets (including GHG emissions targets) at this stage.

Question 8: Do you agree that where an issuer has yet to disclose climate-related targets, it should make alternative disclosures as set out in note 2 to paragraph 6 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. Although there are gaps to be filled in as we compare the Proposed Appendix 27 to the IFRS S2, we understand the practical challenges stated in Question 7. Therefore, we support not putting up a penalty but allowing alternative disclosure, subject to a governance system, at this stage.

For issuers yet to disclose climate-related targets, at minimum, they should be able to disclose softer aspects of deliverables at the operation level. We agree with the proposed requirements, i.e., the work plan, progress, and timetable for setting the targets.

Question 9: Do you agree to require disclosure of progress made in the most recent reporting year in respect of plans disclosed as set out in paragraph 7 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

We support HKEX's requirement that issuers disclose information about the progress in the current reporting period with respect to plans that have been previously disclosed, as this is crucial for establishing accountability and verifiability over time. However, we worry that disclosure will be boilerplate and general, without tracking the progress. We need metrics – not simply when or if management has them – that effectively guide investors' judgement. An extra benefit is that, with metrics and measurable indicators, issuers can evaluate timely whether the working level can cope with the targets and revise their plans accordingly.

We do not oppose making the first reporting period a grace period. Our ultimate goal is to achieve quality disclosures, which set the foundations for evolution going forward. However, we suggest adding language that requires more frequent updates if there are significant changes in laws, regulations, or business drivers in the longer term.

To further enhance transparency, we suggest that such progress should be reported both quantitatively and qualitatively, in order to provide investors with a more comprehensive understanding of the issuer's performance, including whether the issuers are making progress towards their stated plans, and help them make informed investment decisions.

Question 10: Do you agree to require discussion of the issuer's climate resilience as set out in paragraph 8 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. We support HKEX to require disclosure of the assessment of resilience (in paragraph 8 of Part D of the Proposed Appendix 27) based on the scenario analysis (in paragraph 9 of part D of the Proposed Appendix 27), which provide both quantitative and qualitative information for investors to assess the resilience of the issuer's strategy.

We suggest HKEX require issuers to provide separate disclosures regarding their ability to adjust or adopt their business model over different time horizons, such as short, medium, or long-term. This will enable investors to gain a better understanding of the issuer's strategic flexibility and its potential to adapt to changing market conditions.

Question 11: Do you agree to require issuers to apply a climate-related scenario analysis that is commensurate with the issuer's circumstances, and to require disclosure of information on climate-related scenario analysis as set out in paragraph 9 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

We support HKEX's decision to incorporate relevant IFRS S2 requirements on climate-related scenario analysis into Appendix 27, but we are concerned that the Proposal is ambiguous. For the sake of clarity and to ensure consistency and quality of disclosure, we suggest the following:

a) An interim provision for quantitative climate-related scenario analysis

We suggest that HKEX set out an interim provision outlining the expected timeline for issuers to disclose climate-related scenario analysis based on quantitative models. Recognizing the complexity of the scenario analysis, we appreciate HKEX's reference to Rounsevell's research[7] in paragraph 86 of the Proposal, which suggests that issuers may initially adopt qualitative scenario narratives or storylines to explore the range of climate change implications before transitioning to climate-related scenario analysis based on quantitative models.

However, despite acknowledging the learning curve associated with scenario analysis, the Proposed Appendix 27 is silent on the expected quality, granularity, and timetable for quantitative scenario analysis. We are concerned that this oversight may reduce the comparability and relevance of climate-related scenario analysis among issuers, as they vary in their learning cycles, resources, and commitment to climate-related disclosures.

In addition, we observe that HKEX provides several interim provisions allowing issuers to postpone disclosures, such as setting climate-related targets (note 2 of paragraph 6 of Part D of the Proposed Appendix 27) and the anticipated effects of climate-related risks and opportunities (paragraph 11 of Part D of the Proposed Appendix 27). Curiously, no corresponding interim provision exists for climate-related scenario analysis, even though the aforementioned elements are one of the key inputs for scenario analysis. This inconsistency in the Proposal could cause confusion and practical difficulties for issuers.

Given the above, we urge HKEX to include an interim provision specifying the expected timetable for a quantitative climate-related scenario analysis. This will promote clarity and consistency in disclosure practices, facilitating more relevant and comparable climate-related scenario analyses for investors.

[7] Rounsevell, Mark D. and Marc J. Metzger (2010). Developing qualitative scenario storylines for environmental change assessment. WIREs Climate Change, 1: 606-619.

b) Specification of the time horizon used in climate-related scenario analysis

We note that HKEX currently does not require a specific time horizon used in climate-related scenario analysis, and we are concerned that this may lead to a lack of comparability and consistency among issuer disclosures.

Empirical research has shown that most entities conduct scenario analysis by looking at the whole business impact, depending on the nature of the business. However, the scenarios used, including the timeframe used for the analyses, are often inconsistent across entities. This can make it difficult for investors to understand the disclosures. (Chua et al., 2022[8]). In light of the above, we believe that a standard time horizon for climate-related scenario analysis is warranted.

As such, we suggest that HKEX specify the time horizon used in climate-related scenario analysis, which would enhance comparability and consistency among disclosures.

Question 12: Do you agree to require disclosure of the current financial effects of climate-related risks, and where applicable, climate-related opportunities as set out in paragraph 10 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

We note that the Proposed Appendix 27 requires issuers to disclose only the current financial effect of climate-related risks and, if any, opportunities that are material to the financial statements. We are concerned that this may create confusion and result in inadequate disclosures.

Notably, under the IFRS (as outlined in paragraph 94 of the Proposal), issuers are already required to recognize and/or disclose material financial effects (both current and anticipated) arising from climate-related matters in their financial statements. However, in practice, we note that issuers rarely recognize climate-related matters in their financial statements unless there is an exceptional or direct environmental disaster or event. As such, the Proposal which requires disclosure for matters that are material solely in terms of the financial statements, may result in no or minimal disclosures on climate-related risks and, if any, opportunities.

Given the above, we suggest HKEX adopt the wording of paragraph 15 of IFRS S2 that an issuer shall disclose in ESG Report *"the effects of climate-related risks and opportunities on the entity's financial position"; and "the anticipated effects of climate-related risks and opportunities on the entity's financial position, financial performance"*. This enables investors to understand the financial impacts of climate-related risks and opportunities that may not be adequately reflected by their financial statements otherwise.

In addition, as we commented on Question 3, the materiality interpretation in the Proposal is ambiguous. To ensure consistent disclosure of climate-related matters, clearly defined materiality should be used. As such, we urge HKEX to provide a clear materiality interpretation.

[8] Chua, W.F., James, R., King, A., Lee, E. and Soderstrom, N. (2022), Task Force on Climate-related Financial Disclosures (TCFD) Implementation: An Overview and Insights from the Australian Accounting Standards Board Dialogue Series. Australian Accounting Review, 32: 396-405. https://doi.org/10.1111/auar.12388

Question 13: Do you agree that during the Interim Period, where an issuer has yet to provide quantitative disclosures pursuant to paragraph 10(a) of Part D of the Proposed Appendix 27, it should make the interim disclosures as set out in the paragraph immediately following paragraph 10 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Disagreed. We note that the accounting standard (i.e. IAS 37) already mandates issuers to disclose qualitative information in the financial statements for events such as contingent liabilities or assets that cannot be reliably measured. As such, material climate-related matters that cannot be quantified, should be disclosed qualitatively under the accounting standard.

In addition, relaxing the requirement to disclose quantitative effects during the Interim Period may lead to a situation where most of the disclosures will be generic and boilerplate. Therefore, we believe that the proposed interim provision is redundant and unnecessary.

Question 14: Do you agree to require disclosure of anticipated financial effects of climate-related risks and, where applicable, climate-related opportunities as set out in paragraph 11 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. The future-oriented paradigm is important given the focus on climate risk going forward. Investors need metrics that are forward-looking and predictive, as they primarily focus on the prospective impacts of climate-related risks and opportunities.

We observe that, in Part D of the Proposed Appendix 27, HKEX requires disclosure of current financial effects on financial position, financial performance, and cash flows in paragraph 10. However, there is no related disclosure requirement to explain how cash flows will change over time in paragraph 11. This is a significant missing element in our view, as what investors ultimately need are changes in anticipated cash flows over time.

As such, we suggest HKEX require issuers to disclose the anticipated effects of climate-related risks and opportunities on cash flows over time, as outlined in paragraph 15(b) of IFRS S2. Meanwhile, the quantification of time horizons matters as it will affect cash flow estimations. We suggest that issuers should clearly define this.

Separately, we note that, unlike current financial effect disclosure in paragraph 10(b), HKEX did not specify the materiality concept (‘material adjustment’) in paragraph 11. In this regard, we urge HKEX to clarify the required level of materiality for the disclosures under paragraphs 10(b) and 11, respectively, to avoid confusion. This will also facilitate issuers to disclose what is material first, given proportionality to the company’s size and complexity.

Question 15: Do you agree that during the Interim Period, where an issuer has yet to provide information required in paragraph 11 of Part D of the Proposed Appendix 27, it should make the interim disclosures as set out in the paragraph immediately following paragraph 11 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

We suggest the inclusion of a comply or explain element in this interim provision. While we support the requirement for issuers to disclose available information on the aspects of the financial statements most affected by climate matters, and the relevant work plan and timetable, we believe that a comply or explain element will ensure that issuers make reasonable efforts to meet this disclosure requirement.

By requiring issuers to explain the reasons for any non-disclosure of the items outlined in paragraph 11 in Part D of the Proposed Appendix 27, investors can have a better understanding of why certain information has not been disclosed and whether issuers have made a genuine effort to obtain and disclose such information. In addition, this will enhance the transparency and accountability of disclosure on material climate-related matters.

Question 16: Do you agree to require disclosure of the process an issuer uses to identify, assess and manage climate-related risks as set out in paragraph 12(a) of Part D of the Proposed Appendix 27? Please provide reasons for your views.

As an investor organization, we agree and appreciate the importance of a description on how climate-related risks are identified and managed. While the list of requirements is fairly comprehensive and checking multiple boxes, please note the following observations referenced from CFA Institute Climate Letter to SEC[ii]::

- Materiality — This requirement to describe how the materiality (likelihood and effects) of climate-related risks was determined is, in our view, precedent-setting. Further, we suggest disclosure of magnitude and probability over the short, medium, and long term. Requiring management to consider time horizons — and the dynamic nature of materiality — more explicitly adds a different, or at least more explicit, consideration of the qualitative, and possibly quantitative, elements of materiality.

- Relative Importance — we agree with the disclosure of the basis for risk prioritization. As a result of these proposals, climate risks would garner significantly more disclosure than other risks. The HKEX itself may need to demonstrate the proportionality of the requirements and the need to prioritize other disclosures.

- Qualitative vs. Quantitative: Risk of Boilerplate, Unless Quantitative Metrics and Active Enforcement — In terms of assessment methodology, we worry that the disclosure runs the risk of being qualitative, high-level, and boilerplate. To ensure this is not the case, the disclosure will require vigorous enforcement mechanism (as commented in Question 1) to ensure the discussion is meaningful. We believe that metrics or key performance indicators that highlight the drivers of customer or supplier preferences, technological changes, and market prices by industry are the decision-useful disclosures investors need. This is where we believe metrics should be considered.

- Regulatory Reforms by Geography — The Proposal asks issuers to monitor climate-related risks. One of the risks may be those arising from regulations. In our view, investors need an analysis of regulatory risk by geography/region — including GHG emission disclosures, if, for example, the regulation requires their reduction. A high-level discussion of the regulatory risks by region will not suffice. Investors need to link GHG emissions to climate-related regulatory risks and segment results by region.

- Integration of Climate and Overall Risk Management — We believe the requirement to disclose the interaction between climate and overall risk management framework is particularly important as climate will touch all aspects of the business. We think it is important to describe precisely the separate and joint responsibilities of management and the board as they relate to climate risk and their interaction with other aspects of risk management.

Question 17: Do you agree that issuers may opt to disclose the process used to identify, assess and manage climate-related opportunities as set out in paragraph 12(b) of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Disagreed. As discussed in Question 4, we believe it is the "materiality" of impacts that matters rather than the "types" of impacts, be it risks or opportunities. As a result, issuers should be mandated to disclose the process. From an investor protection perspective, we believe the disclosure should demonstrate that the process to identify and assess climate-related opportunities — especially when the opportunities are announced by company management elsewhere as part of marketing company stock (e.g., roadshows and pitches to new investors) — are sufficient and robust.

Question 18 (a): Do you agree with the proposed approach for the disclosure of scope 1 and scope 2 emissions and the related information as set out in paragraphs 13 to 14 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. We support disclosure of Scope 1 and 2 emissions. As we described in the opening section of this letter, "Perspectives That Inform Our Response," investors are increasingly interested in climate-related risks to better inform their decisions around voting and investing. GHG emissions may be a non-financial metric, but they serve as an impact barometer for investors to understand the current transition exposure and how progress (financially and non-financially) can be, or is being, made in reducing emissions. From our discussions with investors, their request for additional information includes Scope 1 and 2 emissions.

We believe it makes sense to use GHGs as defined by the Greenhouse Gas Protocol, as it helps garner comparability across issuers and provides issuers of different sizes with diverse calculation tools. Going forward, GHG emissions need context[9] (i.e., industry drivers, company strategy, and cost of reduction) to be most meaningful to investors. An entity is recommended to disclose the following:

- Industry-based metrics (as required by IFRS S2)
- Approach used to include emissions and reasons for the choice of approach
- Comparative period information

While we suggest the adoption of the GHG protocol as the baseline standard, we have concerns over the long term when interpretive issues arise — given the many application considerations, and influence from other stakeholders on the development of GHG emission standards. This is especially important since the GHG Protocol will be the standard under which companies, in the future, will seek attestation from auditors on their GHG emissions.

On another note, regarding the consolidation approach, we suggest HKEX consider adding a requirement for issuers to separately disclose GHG emissions for unconsolidated investees, particularly jointly controlled entities. We believe if these entities emit significant amounts of GHGs — i.e., material from a double materiality perspective, apart from financial materiality — and if their financial information is not consolidated, their GHG emissions should be separately disclosed as well by the issuer.

This is particularly relevant in industries where companies collaborate on projects through jointly controlled entities (project companies) to reduce balance sheet pressure and financial risk, resulting in unconsolidated financial information. Real estate is an example. The current GHG emissions consolidation approach used to report GHG emissions, such as equity share, financial control, or operational control, may not fully reflect the GHG emissions of these project companies which engage in property development and construction. Requiring separate disclosure of GHG emissions for these entities would provide investors with a more comprehensive understanding of the issuer's climate-related risks and opportunities. This would also encourage issuers to take responsibility for their indirect emissions and collaborate with their unconsolidated investees to mitigate their climate impacts.

Question 18 (b): Do you agree with the proposed approach for the disclosure of scope 3 emissions and the related information as set out in paragraphs 13 to 15 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. Our support is informed by investors' advice that Scope 3 emissions will likely be the most significant emission category for many companies (i.e., because companies need only outsource activities to move emissions to Scope 3 to avoid disclosure). As such, excluding them will not appropriately convey the transition risk faced by an issuer.

[9] Context here refers to (1) the company's climate strategy and its path to transitioning to lower emissions and a lower or low-carbon economy, as this provides context to this barometer; (2) industry-based drivers of future performance that explain how such a transition will impact revenues, expenses, and enterprise value; and (3) the cost of reducing such emissions. Referenced from CFA Institute Climate Letter to SEC.

Recognizing the many challenges associated — including data collection, high degree of estimation, as well as different reporting periods among entities in the value chain — we still strongly support mandatory disclosure of Scope 3, given that its relevance supersedes perfect reliability. Otherwise, this will always be a stated hurdle to disclosure and will be less likely to improve over time. We believe these disclosures will be a standard practice in jurisdictions worldwide, with many large private companies being required to furnish such disclosures already.

Meanwhile, we would be supportive of an industry-based and size-based transition approach, expressed as ranges and with appropriate safe harbors. Such an approach would likely garner support from investors, as it would entail the largest and most significant Scope 3 emitters to implement disclosures first, while other issuers are allowed a grace period of two years.

Disaggregation of GHG emissions by scope, type of GHG, location, geography, segment, and upstream and downstream category is essential to understanding the risks by industry, region, and supply chain. Visual representation, under the principles of communication (e.g., use of tables for quantitative information, cross-referencing, and effective signposting), helps investors better process risk-related information.

Question 19: Do you agree with the proposed approach for the interim disclosures in respect of scope 3 emissions during the Interim Period as set out in the paragraph immediately following paragraph 15 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. The key is to start reporting, even in an evolutionary approach without perfect information. However, clarification from HKEX is needed for the interim provision, which requires "information to the extent reasonably available." For instance, HKEX can consider referencing the GHG Protocol Scope 3 Standard[10] which identifies the minimum boundaries of each scope 3 category, before ultimately proceeding to full boundaries.

Question 20 (a): Do you agree to require disclosure of the amount and percentage of assets or business activities vulnerable to transition risks as set out in paragraph 16 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. Linking transition risk reporting with financial performance could help investors compare underlying profitability across issuers following different risk strategies. Without this quantitative metric, the analysis is not as useful as it could be for understanding the issuer's exposure and projecting future cash flows. We suggest disclosure of the properties, processes, or operations subject to transition risks by location. For instance, to include a cross-reference to the definition of location, meaning postal code or equivalent, to ensure that connection to that level of detail is obvious. Otherwise, we would not expect issuers to provide such information.

10 GHG Protocol Scope 3 Standard identifies the minimum boundaries of each scope 3 category.

However, as mentioned by our response to Question 3, we believe efforts are needed for a more prescriptive and granular definition of 'transition risk' in advance, to ensure the disclosure of this derived metric is meaningful.

In the event that an issuer has significant operations within a jurisdiction that has made a GHG emissions reduction commitment, it may be exposed to transition risks (and hence regulatory risks) related to the implementation of the commitment. Consequently, we recommend HKEX require a description, by geography, of the link between GHG emissions reduction and transition costs, and its impact on enterprise value. This underscores the need to emphasize that changes in legislation or regulations and international accords or agreements may have differing impacts; hence, disclosure on impacts of transition risks related to GHG emission reduction by geographic regions. Investors require more than just information on GHG emissions; they also need to know the source and location, as regulations and international agreements may change unevenly across the globe and present different risks and business outcomes.

Question 20 (b): Do you agree with the proposed interim disclosures during the Interim Period in respect of the metric regarding transition risks as set out in the paragraph immediately following paragraph 16 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

We acknowledge the need for interim disclosures in Hong Kong.

However, we seek HKEX's clarification on this. According to the Proposal, instead of voluntary disclosure, an entity will be mandated to describe the assets or business activities being affected by transition risks otherwise, at a granular level down to its nature, location, and the level of risk involved at minimum. We wonder if this set of information itself would already suffice to determine the quantitative metric (i.e., amount and percentage of assets or business activities vulnerable to transition risks) as requested by Question 20 (a).

Question 21 (a): Do you agree to require disclosure of the amount and percentage of assets or business activities vulnerable to physical risks as set out in paragraph 17 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed, as it is one of the improvements in financial reporting that investors have been seeking for at least the past decade. Again, similar to our response to Question 20 (a), we suggest disclosure of this metric by location of the properties, processes, or operations subject to physical risks.

Specifically, for flood-hazard and high-water stress areas, replacement value is likely a more important measure than book value[iii], as is the impact on financial performance (revenues and expenses) of this risk should it emerge. For example, there could be property with very little book value (as fully depreciated), which could be very costly to replace and have very significant impacts on an issuer's operating results, if not usable.

We also support HKEX's proposed separation of physical risks from transition risks when it comes to climate-related risk disclosures. Having said that, they may not be as easily separable as the definitions may suggest. Physical risks may manifest financially as transition risks, and therefore, clarification from HKEX is needed. We believe it is important to explore the interconnectedness of the two kinds of risks and consider whether a caption is needed for those that have key elements of both. Any plans the company has to transit away from these properties (i.e., which demonstrate the interrelationship between physical and transition risk) would also be useful.

Question 21 (b): Do you agree with the proposed interim disclosures during the Interim Period in respect of the metric regarding physical risks as set out in the paragraph immediately following paragraph 17 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Again, we acknowledge the need for interim disclosures in Hong Kong. However, we have the same inquiry as put forward in Question 20 (b), except for a different type of risk.

Question 22 (a): Do you agree to require disclosure of the amount and percentage of assets or business activities aligned with climate-related opportunities as set out in paragraph 18 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed, as it provides insights into a company's position relative to its peers, allowing investors to understand the likely transition pathways and potential changes in profitability over time.

However, it appears that issuers may opt to disclose the actual and potential effects of climate-related opportunities, as stated in our response to Question 4. We are concerned about inconsistency among the levels of reporting required against climate-related opportunities throughout the Proposal, which will affect general perceptions of the importance of the topic.

While we support disclosure of material climate-related opportunities, and so do its associated assets or business activities, we anticipate greater degree of variation in terms of opportunities within specific business lines or asset classes. For example, automobile manufacturers may report sales of electric vehicles relative to total vehicle sales, while utilities companies may report renewable generation as a fraction of their total electricity generation.

Question 22 (b): Do you agree with the proposed interim disclosures during the Interim Period in respect of metrics regarding climate-related opportunities as set out in the paragraph immediately following paragraph 18 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed with interim disclosures, but only when the climate-related opportunities are material, and are already embedded in a visible plan, so as to avoid boilerplate disclosure and potential manipulation of company stock performance.

Question 23 (a): Do you agree to require disclosure of the amount of capital expenditure, financing or investment deployed towards climate related risks and opportunities as set out in paragraph 19 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. This would serve as a significant step to bring profitability focus to the extensive balance sheet risks and opportunities now being reported.

However, again, it appears that the issuer's disclosure against responses (i.e., including resource deployment) towards climate-related opportunities is made voluntary by our response to Question 6. We are, again, concerned about the inconsistency among the levels of reporting required.

Question 23 (b): Do you agree with the proposed interim disclosures during the Interim Period in respect of the metric regarding capital deployment as set out in the paragraph immediately following paragraph 19 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed, but we have the same concerns as stated in Question 20 (b), and if qualitative disclosure is allowed, it would serve a similar purpose as that served by Question 6.

Question 24: Do you agree that where an issuer maintains an internal carbon price, it should disclose the information as set out in paragraph 20 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. As far as pricing the externalities of climate change, a carbon price would be most helpful in this endeavor, and the disclosure is iterative to understand its impacts on entity operations. We do not anticipate many difficulties disclosing the price if entities already have maintained one.

We understand that different pricing methods and the fact that some issuers operate in various regions may result in a lack of comparability, and it could be too early to require the use of a particular carbon-pricing methodology. It would, however, serve as a useful reference for investors to make their own estimation that links carbon emissions to their impact on enterprise value.

We note that some companies may simply fail to maintain an internal carbon price to avoid disclosing a potentially negative outlook on enterprise value, operating results, or liquidity[iv]. We also acknowledge the difficulty of ascertaining an internal carbon price in the absence of a mature carbon market. Hence, going forward, we advocate for a carbon market that is liquid and allows efficient price discovery, which will benefit issuers in making informed strategic plans and scenario analysis exercises.

Question 25: Do you agree with the proposed approach for the disclosure of how climate-related considerations are factored into remuneration policy as set out in paragraph 21 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. We support management accountability and the linkage of risk management to compensation from a governance perspective. We are informed by investors and our experience that what gets measured (and compensated) is what gets monitored, and without a link to compensation, there may not be the progress that is needed. With such information, investors can begin to frame risks, exposures, and necessary management actions from which linkage to compensation can evolve and be included in their annual AGM proxy.

Question 26: Do you agree with the proposed approach for the industry-based disclosure requirements prescribed under other international ESG reporting frameworks such as the SASB Standards and the GRI Standards as set out in paragraph 22 of Part D of the Proposed Appendix 27? Please provide reasons for your views.

Agreed. We acknowledge the balance to be achieved between standard disclosures that are comparable across industries and disclosures within an industry so that the most material climate-related issues can be identified for a particular industry. At the same time, care must be taken not to rely too heavily on a sector model that looks to fit every company into a neatly defined category. Many companies operate in diverse business lines and defy easy classification, also taking into account the evolving nature of industry-specific metrics. We note that companies need the capacity to communicate their exposures, and investors need the tools to engage with those companies and promote best practices. Therefore, we agree with a complementary disclosure of sector-specific information at this stage, while the HKEX should consider mandating industry-based disclosure requirement going forward. This will enable a system that establishes effective cross-industry disclosure while not stifling the ability to introduce resolutions that have the effect of increasing engagement.

As for industry-specific references, we believe the future-oriented SASB and GRI standards are likely expected elements and illustrative of future performance drivers. They may also earn higher credibility to global investors and multi-national corporations. We understand the constraints on referencing the SASB standards, but like with other standards upon which this Proposal is based, we believe there will be a means for the industry-based standards to be included, as these are essential to a global baseline.

Question 27: Do you have any comments regarding whether the manner in which the proposed consequential amendments are drafted will give rise to any ambiguities or unintended consequences? Please elaborate.

On the note of consistency among levels of reporting required for climate-related opportunities, please refer to our responses to Questions 22 and 23.

Question 28: Do you have any comments regarding the topics/matters that we intend to give guidance on? Is there any particular topic/matter you consider further guidance to be helpful? Please elaborate.

On disclosure assurance and attestation — While our investor members have told us they desire assurance over sustainability disclosures, we recognize challenges on data availability and human capital.

For instance, ESG information is different in that it is not typically based on accounting information but rather on climate science, human capital, and other areas of expertise, and such information can be more forward-looking than auditors are traditionally comfortable assuring. Therefore, issuers should engage with experts in the preparation of climate disclosures, if the management sees a lack of relevant capability. Such that, on the basis of the expert work, auditors should wear the hat of a gatekeeper, evaluate the appropriateness and reasonableness of the methodology, and assumptions underlying the climate disclosures in accordance with ISA 500 – Audit Evidence or ISA 620 - Using the Work of an Auditor's Expert[11]. This provides assurance and control on the quality of climate disclosures, particularly regarding material impacts of climate-related risks and opportunities. Separately, we are seeking more guidance on verification or attestation against disclosure under such Proposal, especially for GHG emissions, from an independent third party.

Besides, we note that many small and medium-sized issuers tend to publish ESG reports that are primarily narrative and lack sufficient quantitative information on their environmental and social performance. This may prevent investors from analyzing the issuers' environmental and social performance. According to the Proposal, Part C (i.e., KPIs) is not mandatory, instead more qualitative disclosure for strategies and plans is required. While we support the Proposal to require more disclosure on strategies and plans, we are concerned that this may further reduce comparability and consistency of information between issuers and make it more challenging for investors to evaluate issuer's actual performance. To address this issue, we suggest that HKEX provide guidelines requiring issuers to have a separate section in their ESG report that summarizes and highlights key quantitative information, key targets, and any material changes from the previous year. This will facilitate investors to access essential information on issuers' ESG performance and improve the comparability of the ESG information.

We also suggest more guidance/clarification on the definition of the below concepts:

- 'Materiality', specifically Questions 3 and 12
- 'Time horizons', specifically Questions 3 and 14
- 'Information to the extent reasonably available', specifically Question 19
- 'Transition risk', specifically related to Questions 3 and 20.

[11] ISA 500 and ISA 620 deal with the auditor's use of the work of a person or entity possessing expertise in a field other than accounting or auditing, employed or engaged by the management or auditor to assist the auditor to obtain sufficient appropriate audit evidence.

Question 29: Do you have any feedback on the new developments announced by the ISSB subsequent to the publication of this paper that may impact on the proposals in this paper? Please share your views with us.

1) Define the users of ESG Report

While the proposed code largely mirrors the disclosure requirements of IFRS S2, we are concerned that the target audience for the proposed ESG code and IFRS S2 do not appear to be identical, and we believe that clarifying the target audience and defining the term "stakeholder" will reduce confusion among issuers.

As stated in the conclusion paper of IFRS S2 (BC16), the IFRS S2 aims to establish a baseline for sustainability-related financial disclosures that are relevant to the users of general-purpose financial reports, defined as investors, lenders, and other creditors (see appendix A of the IFRS S2). The disclosure requirements are therefore from the perspective of these parties and are intended to provide information about how a company's financial performance and position will be affected by climate change, but not vice versa. There is no concept of "stakeholders" in IFRS S2.

Unlikely IFRS S2, the proposed Appendix 27 does not explicitly define the users of ESG report. Instead, it introduces the concept of stakeholders and encourages issuers to engage them on an ongoing basis (e.g., paragraphs 7 and 14 of the proposed ESG Code).

To avoid confusion and ensure ESG report is appropriately addressed, we suggest that HKEX:

I. Clarify the intended users of ESG report: Aligning the ESG report's target audience with that of the IFRS S2 will provide consistency in disclosure requirements and help issuers better understand the scope and purpose of their disclosures.

II. Define "stakeholder" within the proposed code: Providing a clear definition of stakeholders will enhance transparency and accountability, enabling issuers to effectively engage with relevant parties and address their concerns and expectations.

2) Mitigate the proportionality challenges

We suggest that HKEX review the proposed ESG Code with consideration for the diverse capabilities and resources among issuers. We are concerned that applying the same standards to issuers of both the Main Board and GEM Board, without regard to their size and resources may result in inconsistent quality of disclosure among issuers, ultimately undermining the confidence of users in ESG Reports. As highlighted in the conclusion paper (BC14), most respondents urged the ISSB to consider the diverse capabilities and preparedness of entities in applying the standards. They recognized that issuers may face limitations in terms of resource constraints, data and specialist availability. In response, the ISSB has added a proportionality mechanism in the IFRS S2, which stipulates "an approach that is commensurate with the skills, capabilities and resources that are available to the entity for preparing those disclosures." This is to address the potential disparities among issuers, particularly in relation to climate-related scenario analysis, measurement of GHG emissions, and calculation of metrics.

Given the above and the gap between the size of issuers of the Main Board and GEM Board, we suggest that the HKEX adjust the disclosure requirements according to the size of the issuer's operations to mitigate proportionality challenges, such as allowing GEM Board issuers to take a "comply or explain" approach to complex disclosures, like scenario analysis, GHG emissions, and metrics. Such that the proposed Code is commensurate with issuers' skills, capabilities and resources, promoting a fair reporting standard while maintaining the comparability and reliability of ESG Reports.

Concluding Remarks

CFA Institute and CFA Society Hong Kong support disclosures based upon the global baselines ISSB and TCFD, which provide a useful framework for communicating how a company thinks about climate risks from a strategic perspective and its plans for managing climate risks. We view IFRS S1 and S2 as important frameworks going in parallel for multi-period and multi-jurisdictional efforts towards improving the quality of climate-related disclosures. We encourage the HKEX to place priority on aligning with IFRS S1, following the integration of S2 into Appendix 27.

We acknowledge and support the HKEX's balanced approach to be adopted in Hong Kong SAR as a more natural starting point, considering the constituents of the HKEX, the maturity and ESG literacy of issuers, and HKEX's long-standing practice. The quality and usefulness of the disclosures, however, will be highly dependent upon implementation. The disclosures, other than GHG emissions and certain metrics disclosures, will likely be qualitative. The TCFD's own study of the application of its guidance also suggested weak compliance. With HKEX's enhanced requirements, this will naturally improve, given the liability concerns that should be commensurate with the evolving nature of climate-related disclosure. However, to be decision-useful, the compliance element of the Proposal will require persistent enforcement from HKEX and relevant authorities, while there is meaningful protection from legal liability for disclosures provided in good faith.

Going forward, we encourage the HKEX to continue its efforts in broader engagement and assisting issuers with capacity building. Apart from engaging with issuers to raise awareness and collect their feedback on implementation learnings, investor engagement is equally important – given they are the audience of the reports and users of the proposed standards with respect to stewardship. We also encourage the HKEX to continue providing best practice guidance and incentives for upskilling on climate-related matters, while connecting with other markets in the region to participate in the global conversation and transition journey.

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[i] Please see CFA Institute's response to The Enhancement and Standardization of Climate-Related Disclosures for Investors in 2022.
[ii] Same as above.
[iii] Same as above.
[iv] Same as above.