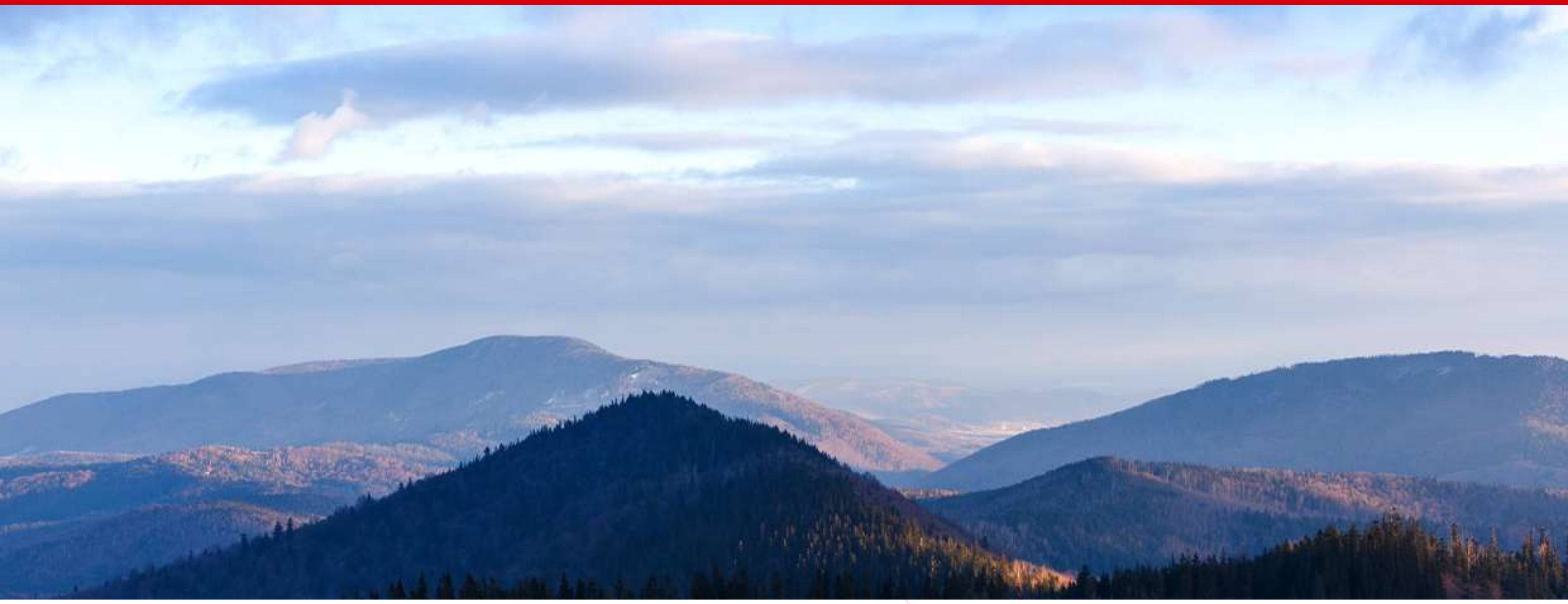


HKEx Updates on Climate Disclosure Standards

On 10 June 2022, the Stock Exchange of Hong Kong (**HKEx**) released its 2022 listing newsletter (**HKEx Listing Newsletter**). This fourth edition primarily focuses on the forthcoming global sustainability reporting standards on climate disclosures that will form the upcoming HKEx review of the environmental, social, and corporate governance reporting framework (**HKEx ESG Reporting Framework**), the relevance of the low-carbon transition of Special Purpose Acquisition Companies (Hong Kong **SPACs**), as well as recent listing developments in the HKEx.

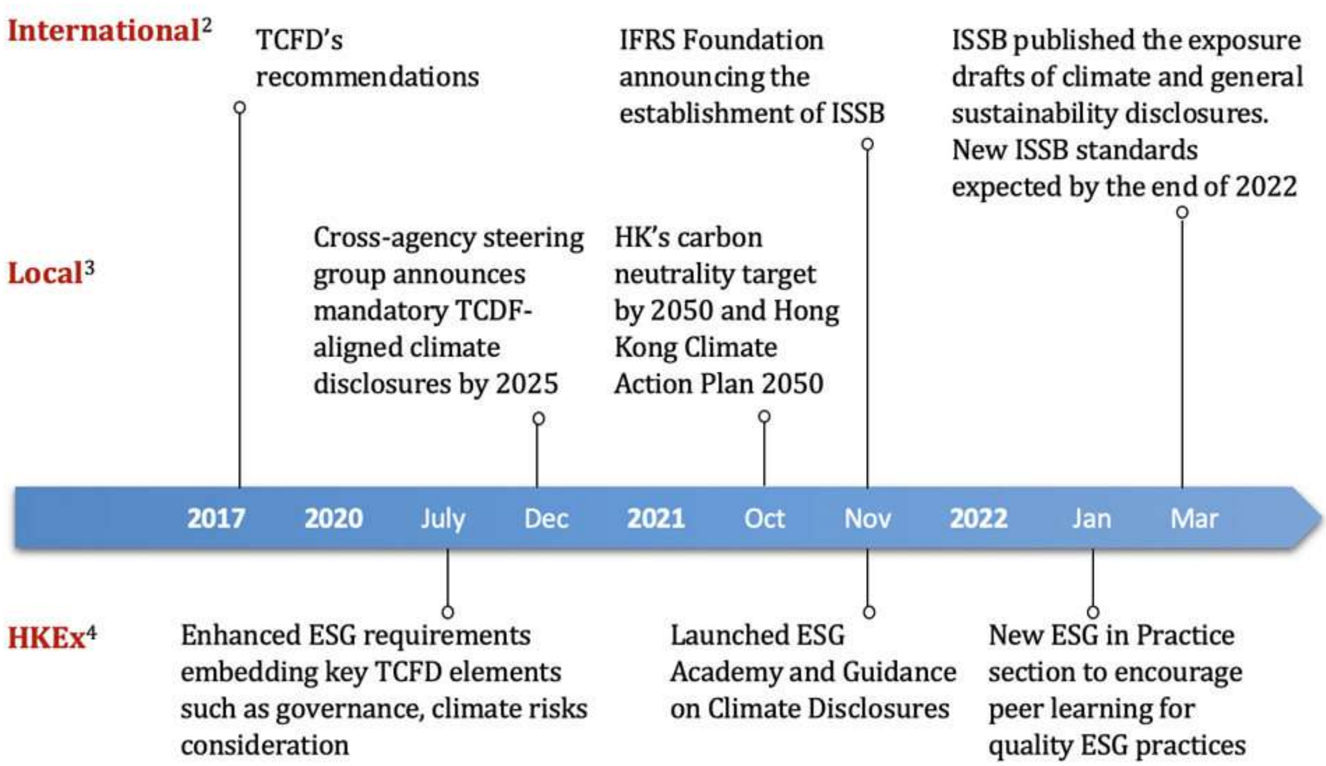
HKEX to Review Improving Standards for Climate Disclosure

With climate change issues increasingly being a pressing issue for people worldwide, coupled with the United Nations' Climate Change Conference (COP26) drawing the world's attention to the issue in November 2021, regulators note that the focus now is on how national policies and regulations can support the transition to a low-carbon and sustainable future. Global investors have shifted to championing environmental footprints over excess profits, social impact over short-term performance, and governance over growth-at-all-costs.

Companies have also noted the increased and varied interests and are progressively conscious of consumers' interests as well as other stakeholders. Many are acknowledging that their commercial interests must also co-exist with a sustainable environment in which they operate.

With a heightened focus on the environment and sustainability, transparent and reliable ESG disclosure will be a key step to prevent greenwashing[1] from stalling the global transition to a low-carbon economy. The HKEx has made steps in creating uniform ESG rules between issuers, investors, exchanges, and regulators, believing it to be essential that collaboration between all parties will lead to a green and sustainable financial ecosystem.

Throughout recent years, there have been efforts to improve climate disclosure. The below chart shows actions on an international level, local level, and from the HKEx in order to improve climate disclosure:



Based on the recommendations by the TCFD, the new global sustainability reporting standards to be developed by the International Sustainability Standards Board (**ISSB**) are expected to require more specific and quantitative climate disclosures with an aim to improve the comparability of data, for example, improving on the use of metrics or measuring the impact on an entity's financial position or performance. With the HKEx on board to align their regulatory requirements with the TCDF's recommendations and reflect the development of the ISSB's standards, the HKEx will review the ESG reporting framework later this year with a focus on climate disclosures.

After reviewing Hong Kong listed companies' ESG practices focusing on changes effective from July 2020, the HKEx will publish its recommendations on areas for improvement. It is expected that the role of education will be particularly important for companies that have less expertise or experience in ESG or climate-related issues. The HKEx will also provide guidance, resources, and other support to assist companies accelerate their environmental, social, and corporate governance and set climate action plans in motion.

When preparing for new climate disclosures, the HKEx Listing Newsletter recommends that Hong Kong listed companies should prioritise the following:

(i) Keeping an eye on latest developments

(a) companies should first refer to the Climate-related Disclosures Exposure Draft published by the IFRS Foundation and identify gaps in internal policies and practices, which will help with planning upgrades, enhancing existing infrastructure or systems in preparation of reporting under the new requirements; and

(b) provide regular training and/or briefings to directors and relevant employees in order to understand the latest requirements.

(ii) Taking action at all levels within the company

(a) the board should integrate consideration of climate risks and opportunities into its strategy and decision-making process, and monitor the progress towards targets set;

(b) finance and sustainability teams should work closely together, with the finance team focusing on the data and financial impact assessments, and the sustainability team working on infrastructure planning and validating the evidence; and

(c) the communications or public relations team should help align the company's sustainability objectives with public affairs goals, which allows stakeholders to better understand and assess the company's climate actions.

(iii) Net-zero plan

(a) companies should employ and provide disclosures on infrastructure and/or technology to help reduce carbon emissions and control climate-related risks in alignment with the Government's carbon neutrality target and Hong Kong's Climate Action Plan.

(iv) Value chain

(a) companies should disclose the impact of climate risks and opportunities on the company's business model, including the effects on its value chain.

HKEx to Follow Greenhouse Gas Protocol Categorisation Greenhouse Gas Emissions

The Greenhouse Gas Protocol categorises greenhouse gas emissions into three scopes:

(i) Scope 1 emissions refer to all direct emissions that occur from the sources or operations that are owned or controlled by the company. For example, emissions from company vehicles or facilities would be classified as Scope 1.

(ii) Scope 2 emissions are indirect emissions that occur from the generation of purchased or acquired electricity, heating, cooling and steam consumed by the company.

(iii) Scope 3 emissions are emissions outside of Scope 2 that occur in the value chain of the company, including upstream with suppliers and downstream with customers. These are emissions that occur from sources not owned or controlled by the company.

Under the current Hong Kong requirements, HKEx listed companies must disclose greenhouse gas Scope 1 and 2 emissions on a "comply or explain" basis in their ESG reports under Appendix 27 to the HKEx Main Board Listing Rules / Appendix 20 to the GEM Listing Rules. With the ISSB Climate Standards contemplating the necessity on reporting all Scope 1, 2, and 3 emissions, listed companies yet to report on Scope 1 and 2 should prepare for making enhanced climate disclosures.

For HKEx listed companies operating in Hong Kong, emission reports for calculating Scope 2 emissions can be found in the latest sustainability reports from the relevant power or utilities companies in Hong Kong, including Hong Kong Electric, CLP, and Towngas. For listed companies with operations outside Hong Kong, emission factors in any overseas countries or territories should be included for calculating their Scope 2 emissions and companies may also contact their energy suppliers for the relevant emission details.

Regarding Scope 3 emissions and all indirect emissions that occur in a company's value chain, the Greenhouse Gas Protocol guidance[5] sorts such activities into 15 categories to facilitate measuring and managing such emissions.[6] The Greenhouse Gas Protocol guidance offers different calculation methods for selection based on criteria such as size of emissions of the activity, the company's business goals, data availability, and quality. In order to calculate Scope 3 emissions, companies may either use (i) primary data (i.e. data collected directly from suppliers for a specific activity via questionnaires or other engagement channels); or (ii) secondary data (i.e. industry-average-data, financial data, or generic data obtained from internationally recognised databases, provided by governments or data that has been peer-reviewed). Further guidance on details such as how to report or calculate emissions can be obtained from the HKEx's How to Prepare an ESG Report – Appendix 2: Reporting Guidance on Environmental KPIs or the Greenhouse Gas Protocol website.

Low Carbon Transition of Hong Kong SPACs

SPACs are a type of shell company with no business operations or assets and are formed to raise funds through initial public offerings for the purpose of conducting an acquisition of an operating company within a pre-defined time period after listing. Hong Kong SPACs are generally established and initially financed by experienced founding shareholders (typically referred to as Hong Kong SPAC Promoters[7]). Charltons has written extensively on SPACs in Hong Kong including an overview of the HKEx's new SPAC listing regime that took effect on 1 January 2022, which can be found *here*.

As of now, there have been 12 SPAC applications in Hong Kong, with 2 listed in March and another in June. The global surge in ESG-Focused SPACs and De-SPAC Transactions[8] is expected to continue, and De-SPAC Targets[9] have been listed from sectors including environmental technology, transportation, industrials, water, and energy in recent years. In Hong Kong, three SPACs (of the ten with current listing applications) and one of the two listed SPACs intend to seek De-SPAC Targets from sectors including climate action, green energy, and green technology.

Efforts by the HKEx to Enhance Listing Developments

Apart from the ESG-related initiatives both planned and already in motion, the HKEx has also provided a platform for the listing of green, social, and sustainability-linked bonds (**HKEx GSS Bonds**). The HKEx saw a larger-than-fivefold increase in the listing of GSS Bonds in 2021, with 95 new GSS Bonds listed on the HKEx, raising a record-breaking HKD281.6 billion. Notable issuers include the HKSAR Government, the Shenzhen Municipal Government, the Malaysian Government (through a wholly-owned SPV), the Bank of China Limited, and China Construction Bank Corporation. For comparison, in 2020 there were 23 new GSS Bonds listed that raised a total of around HKD 50 billion and in 2019 there were 25 new GSS Bonds listed that raised a total of around HKD 55 billion.

Currently, all GSS Bonds are listed under Chapter 37 of the HKEx Listing Rules and offered to professional investors only. As there are no specific requirements governing GSS Bonds, the same HKEx Listing Rules apply to GSS Bonds as all other bonds.

Areas where the HKEx has sought to enhance market development include:

(i) Created a Hong Kong listing framework for SPACs to provide issuers and investors with greater diversity of choice, within appropriate safeguards.

(ii) Enhanced and streamlined the HKEx Listing Rules on the listing regime for overseas issuers to increase the accessibility of our markets for companies listed overseas without compromising protection for shareholders in Hong Kong.

(iii) Proposed changes to extend Chapter 17 of the HKEx Listing Rules to govern share award schemes, due to the increase in number of these schemes.

(iv) Published the Information Paper on Consequential Rule Amendments to reflect new requirements of the SFC Code of Conduct[10] on the conduct of companies and intermediaries involved in bookbuilding and placing activities and the related FAQs. Charltons has also written extensively on this area *here*.

Areas where the HKEx has sought to improve the market quality include:

(i) Revised the Corporate Governance Code and related HKEx Listing Rules to further enhance corporate standards among listed issuers in Hong Kong, specifically in corporate culture, director independence, and diversity.

(ii) Launched a new diversity repository, "Board Diversity & Inclusion in Focus" and introduced an "ESG in Practice" section to the ESG Academy, following the publication of the Guidance on Climate Disclosures.

(iii) Published the Listing Committee Report 2021 to provide an account of the work of the Listing Committee of the Exchange for the year ended 31 December 2021, setting out a policy agenda of matters that the Listing Committee plans to consider in 2022 and beyond.

(iv) Unified the Main Board and GEM websites to align corporate branding.

There has also been development of a series of HKEx Listing Rules e-training courses for listed companies' directors, management and compliance staff, market practitioners, and professionals. These courses deal with topics such as trading halts, continuing obligations, notifiable transactions, connected transactions, equity fundraising rules, and trading arrangements for corporate actions. Further details on such courses are available on the HKEx website *here*.

Looking Forward by the HKEx

The consultation conclusions paper regarding the proposed amendments to the HKEx Listing Rules relating to the share schemes of listed issuers was published by the HKEx on 29 July 2022, and will take effect on 1 January 2023. As a result, the HKEx Listing Rules will be extended to govern all share schemes involving grants of share awards and share options, and there will also be enhanced share schemes regulation to manage dilution of listed shares and provide information disclosure to maintain higher levels of shareholder protection.

With the listed structured products market being a significant component of the cash market (making up an average of 12% of the cash market turnover, or HK$20.1 billion, in 2021), the HKEx has also seen fit to review the structured products regime. With the last review being made in 2006, the HKEx Listing Division is now conducting a review of Chapter 15A of the Main Board Listing Rules to update the rules and bring them in line with market developments. The potential changes include the enhancements of listing standards, facilitation of product issuances and building a more inclusive regime to facilitate new product development.

[1] Greenwashing is a form of marketing where companies deceptively claim or advertise that the company's products or policies are environmentally friendly in an attempt to increase the public's perception of its brand or products

[2] The Task Force on Climate-Related Financial Disclosures (**TCFD**) was established by the Financial Stability Board to improve and increase reporting of climate-related financial information. Its recommendations are structured around four core elements: governance, strategy, risk management, and metrics and targets. The Announcement of issue of exposure drafts on sustainability and climate-related disclosures were proposals published by the International Financial Reporting Standards Foundation (**IFRS**) to develop a comprehensive global baseline of sustainability disclosures.

[3] Hong Kong's own Green and Sustainable Finance Cross-Agency Steering Group was established in May 2020 to co-ordinate the management of climate and environmental risks to the financial sector, accelerate the growth of green and sustainable finance in Hong Kong, and support the Government's climate strategies. The Chief Executive's 2021 Policy Address regarding Hong Kong's carbon neutrality target plan is located here while the Government's Climate Action Plan 2050 is located *here*.

[4] HKEx's ESG Academy seeks to support, guide, and educate listed companies and the broader business community in their sustainability journeys. The Guidance on Climate Disclosures can be found *here* and the ESG in Practice section is located *here*.

[5] https://ghgprotocol.org/sites/default/files/standards/Scope3_Calculation_Guidance_0.pdf

[6] The 15 categories are: Purchased Goods and Services, Capital Goods, Fuel-and Energy-Related Activities Not Included in Scope 1 or Scope 2, Upstream Transportation and Distribution, Waste Generated in Operations, Business Travel, Employee Commuting, Upstream Leased Assets, Downstream Transportation and Distribution, Processing of Sold Products, Use of Sold Products, End-of-Life Treatment of Sold Products, Downstream Leased Assets, Franchises, and Investments

[7] Promoters of SPACs has the meaning in HKEx Listing Rules 18B.10 and 18B.11

[8] A De-SPAC Transaction is an acquisition of, or a business combination with, a De-SPAC Target by a SPAC that rsults in the listing of a successor company (the listed issuer resulting from the completion of a De-SPAC Transaction) (HKEx Listing Rule 18B.01)

[9] A De-SPAC Target refers to the target of a De-SPAC Transaction (HKEx Listing Rule 18B.01)

[10] The Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission

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