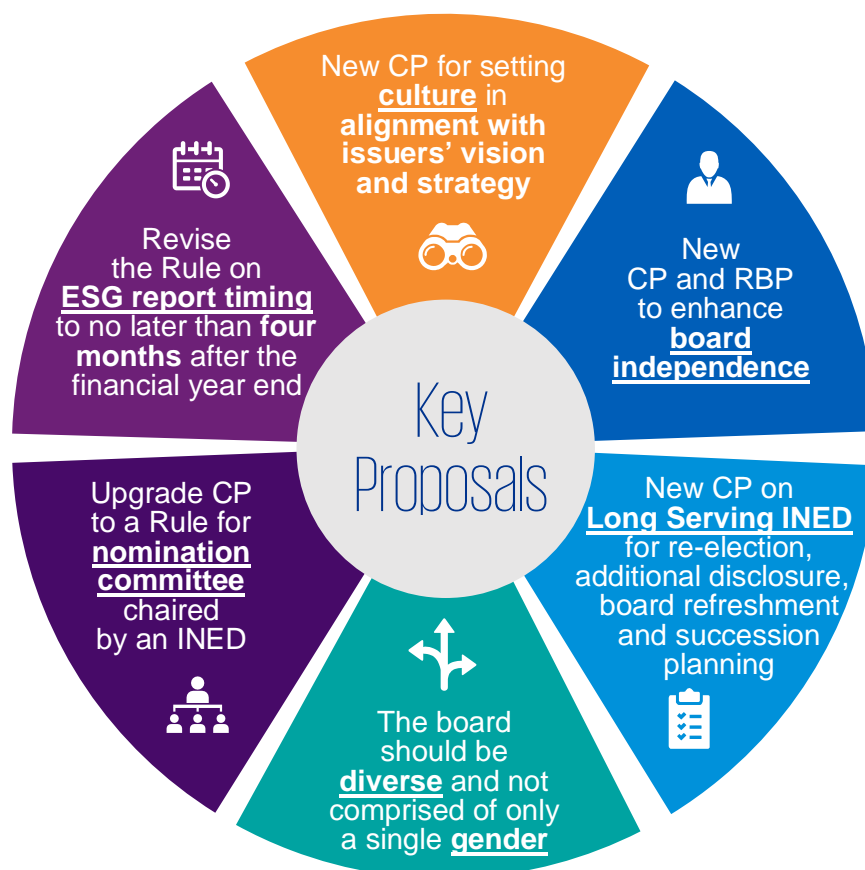


Hong Kong Capital Markets Update

ISSUE 2021-03 | April 2021

HKEX's consultation on review of CG Code

On 16 April 2021, the Stock Exchange of Hong Kong Limited (the "Exchange") published a [consultation paper](#) ("Consultation") seeking views and comments on proposed changes to the Corporate Governance Code ("CG Code"). The deadline for submissions is 18 June 2021.



Background

To ensure the corporate governance framework remains fit for its purpose, continues to promote improvements in the quality of governance and is adequate to maintain investors' confidence in the market, the Exchange conducts reviews from time to time to take into account market developments and observations, as well as the views expressed by professionals, market practitioners and industry groups, including those representing investors.

This Consultation aims to:

- (i) highlight the importance of corporate culture in alignment with vision and strategy to deliver long-term sustainable performance ("**Culture**");
- (ii) enhance board independence, promote board refreshment and succession planning ("**Director's Independence**");
- (iii) further promote board (gender) diversity of listed issuers ("**Diversity**");
- (iv) strengthen the role of the nomination committee ("**Nomination Committee**");
- (v) improve communications with shareholders ("**Communications with Shareholders**");
- (vi) elaborate on the linkage between CG and ESG, and improve the timeliness of ESG reports by aligning the publication timeframe of ESG reports with annual reports ("**ESG Reporting**"); and
- (vii) improve the flow and readability of the Code ("**Code Structure**").

Culture

A healthy culture plays a pivotal role in good governance, and the board should demonstrate good practice in the boardroom and promote governance throughout the business. The company as a whole must demonstrate openness and accountability and should engage constructively with shareholders and wider stakeholders about culture. Therefore, the Exchange proposes introducing a code provision ("CP") to require issuers' boards align the company's culture with its purpose, value and strategy.

Also, anti-corruption and whistleblowing are core to establishing a healthy corporate culture. Hence, the Exchange proposes to: (a) introduce a new CP requiring the establishment of an anticorruption policy; and (b) upgrade a recommended best practice ("RBP") C.3.8 to a CP requiring the establishment of a whistleblowing policy. In fact, issuers are currently required under the ESG Guide in Listing Rules ("Rules") to disclose such policies or information on a "comply or explain" basis subject to materiality.

Director's Independence

It is of utmost importance to ensure that independent non-executive directors ("INEDs") continue to make the expected contribution to the board. Board makeup should change in line with the evolving business environment and challenges. Therefore, it is necessary to refresh the board to avoid entrenchment and to attract new views and perspectives. The board must also put succession planning into practice to ensure its long-term success.

To strengthen board independence, the Exchange proposes introducing a CP requiring disclosure of a policy to ensure independent views and input are available to the board, and an annual review of the implementation and effectiveness of such policy.

To ensure INEDs maintain their objectivity and independence, the Exchange proposes introducing a RBP that an issuer generally should not grant equity-based remuneration (e.g. share options or grants) with performance-related elements to INEDs as this may lead to bias in their decision-making and compromise their objectivity and independence.

To promote board refreshment and succession planning, in respect of re-election of an INED serving more than nine years ("Long Serving INED"), the Exchange proposes revising the existing CP A.4.3 to require (i) such re-election be subject to independent shareholders' approval, and (ii) additional disclosure on the factors considered, the process and the board or nomination committee's discussion in arriving at the determination in the explanation on why such INED is still independent and should be re-elected ("Additional Disclosure").

In circumstances where all the INEDs on the board are Long Serving INEDs, the Exchange proposes introducing a CP requiring issuers to (i) appoint a new INED at the forthcoming annual general meeting ("AGM"), and (ii) disclose the length of the tenure of the Long Serving INEDs on the board on a named basis in the shareholders' circular. In the long run, the Exchange may consider phasing out all Long Serving INEDs gradually.

Diversity

Diversity is an important driver of board effectiveness, creating cognitive diversity in the boardroom and breaking down a tendency towards "group think". To further promote gender diversity, the Exchange proposes to (a) highlight that diversity is not considered to be achieved by a single gender board in the Rule; and (b) introduce a new Mandatory Disclosure Requirement ("MDR") requiring all issuers to set numerical targets and timelines for achieving gender diversity at both (i) board level and (ii) across the workforce (including senior management).

A three-year transition period is proposed by the Exchange allowing existing issuers with single gender boards to appoint at least one director of the absent gender on their boards, while IPO applicants are expected to not have single gender boards, when the revised Rules becomes effective.

The Exchange also proposes introducing a CP requiring the board to review the implementation and effectiveness of its board diversity policy annually.

Nomination Committee

A transparent and independent oversight by the nomination committee of matters relating to board nomination and recruitment, board diversity and succession planning is key to promote better practice and standards. To emphasise the importance of oversight of board nomination and recruitment, diversity and succession planning, the Exchange proposes to upgrade the CP A.5.1 to a Rule requiring issuers to establish a nomination committee chaired by an INED and comprising a majority of INEDs. The Exchange will also set out in the guidance the expected disclosures regarding INED nomination and appointment.

Communications with Shareholders

Effective engagement with shareholders and stakeholders is important for a company to meet its responsibilities to shareholders and stakeholders. To emphasise the importance of two-way communication, the Exchange proposes to upgrade a CP E.1.4 to a MDR requiring disclosure of the issuer's shareholder communication policy.

The policy should include channels for shareholders to communicate their views on various matters affecting the issuer, as well as steps taken to solicit and understand the views of shareholders and stakeholders. Issuers are required to review the effectiveness of the policy on an annual basis.

ESG Reporting

Governance and oversight of ESG matters and management of material ESG risks (including climate-related risks) is an integral part of good corporate governance. Therefore, the Exchange proposes to elaborate on the linkage in the Code by (a) setting out the relationship between CG and ESG in the introductory section in the Code; and (b) including ESG risks in the context of risk management under the Code.

Also, the Exchange proposes revising the Rule and the ESG Guide to require the publication of ESG reports at the same time as publication of annual reports (i.e., no later than four months after the end of the financial year).

Code Structure

Since the market generally refers to all the CG requirements under Appendix 14 as the "Corporate Governance Code". The Exchange therefore proposes to rename Appendix 14 to "Corporate Governance Code" rather than the current name of "Corporate Governance Code and Corporate Governance Report".

The Exchange also proposes to re-arrange the structure of Appendix 14 to enhance the flow and readability by: (a) amending the introductory paragraphs to reflect the CG reporting framework; (b) moving the MDRs upfront in Appendix 14; (c) re-organising the provisions by topics; and (d) making drafting amendments to improve clarity of the requirements (including deleting duplicative requirements). To avoid doubt, the changes to Appendix 14 involve no change in policy direction and will not result in any additional CG requirements.

Other enhancements

To enhance transparency, the Exchange proposes introducing a Rule requiring disclosure of directors' attendance at general meetings in the poll results announcements.

In addition, the Exchange further proposes deleting the CP A.4.1 requiring issuers to appoint NEDs for a specific term as directors are already subject to retirement by rotation and shareholders' approval for re-election.

Proposed Effective Date

The Exchange proposes, subject to the responses to this Consultation, to implement the revised Rules and the Code for financial year commencing on or after 1 January 2022, except for the proposals on Long Serving INEDs which are proposed to be effective for the financial year commencing on or after 1 January 2023 to allow a longer transition period.

If you have any questions about the matters discussed in this publication, please feel free to contact the following capital markets partners and directors.

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