Climate Change Reporting:

Imminent, Challenging & Mandatory – The Opening Moves

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Contents

Foreword

The fallout from failing to manage climate change is considered as one of the biggest threats to humanity. In fact, in the World Economic Forum's Global Risks Report 2022, climate-related risks account for the three most severe risks affecting people in the next 10 years, with climate action failure considered as the top medium and long-term threat.[1]

Climate change also has a substantial impact on businesses. There is ever-increasing pressure to take actions to slow climate change and reduce carbon emissions. These efforts are expected to continue to intensify over the coming years as the global economy transitions towards a low-carbon model. As revealed in KPMG's 2021 CEO Outlook, 30 percent of surveyed CEOs plan to invest more than 10 percent of their revenues to make their business more sustainable and to address related climate change risks.[2]

Regulators and investors are also demanding increased transparency on how businesses deliver on climate goals and address climate-related issues within a tight time frame. This has resulted in the development of several climate-related disclosure frameworks, the most prominent of which is the recommendations released by the Task Force on Climate-Related Financial Disclosures (TCFD) in 2017. The TCFD was established by the Financial Stability Board, an international body comprising G20 finance ministers and central bank governors, to help identify the information needed by investors, lenders and insurance underwriters to appropriately assess and price climate-related risks and opportunities.

Responding to calls for a more consistent and comparable baseline of investor-focused sustainability standards, the International Financial Reporting Standards (IFRS®) Foundation established the International Sustainability Standards Board (ISSB™ Board) at COP 26 in November 2021, with an initial focus on climate-related financial disclosures. On 31 March 2022, the ISSB Board released proposals for its first two standards, one dealing with general sustainability-related disclosure requirements and the other on climate-related disclosure requirements. These two proposals built upon the TCFD recommendations and are structured around the four pillars that represent core elements of how companies operate, namely: governance, strategy, risk management, as well as metrics and targets.

The ISSB Board expects to finalise the two standards by the end of 2022. In Hong Kong, the Green and Sustainable Finance Cross-Agency Steering Group expressed its support for adopting the ISSB Board's standards.[3] In particular, the Securities and Futures Commission (SFC) and Hong Kong Exchanges and Clearing Limited (HKEX) are engaging with industry practitioners to evaluate how the ISSB Board's proposed requirements can be applied in Hong Kong. It is expected that reporting under the ISSB Board's standards will become mandatory for listed companies.

Companies should prepare themselves for the inevitable ISSB Board's standards. Governance professionals, who serve as the company secretary and governance advisers of listed companies, play a vital role in providing advice and direction about the emerging climate reporting requirements and assisting the board in meeting those requirements.

To help companies better anticipate issues in adopting the proposed ISSB Board's standards, KPMG China has once again collaborated with The Hong Kong Chartered Governance Institute (HKCGI) and CLP Holdings Limited (CLP) to jointly produce this report. This publication will explore the focus areas which may warrant additional attention and resources, together with recommendations about how companies can make their opening moves.

We welcome the opportunity for discussion, and hope you find the insights within this publication useful as your company embarks on its climate journey.

[1] 'The Global Risks Report 2022', World Economic Forum, 2022, https://www3.weforum.org/docs/WEF_The_Global_Risks_Report_2022.pdf
[2] 'KPMG 2021 CEO Outlook', KPMG International, 2021, https://assets.kpmg/content/dam/kpmg/xx/pdf/2021/09/kpmg-2021-ceo-outlook.pdf
[3] 'Green and Sustainable Finance Cross-Agency Steering Group welcomes publication of International Sustainability Standards Board proposed standards for public consultation', Hong Kong SAR Government, accessed on 6 May 2022, https://www.info.gov.hk/gia/general/202203/31/P2022033100606.htm

> ***The development of global baseline standards by the International Sustainability Standards Board is a significant milestone in the effort to retool the financial system to deal with climate change. Hong Kong's potential adoption of these standards has enormous significance. Incorporating them into local requirements will establish a framework for disclosures which provide investors with key information about the impact of climate risks on corporate performance. This report presents a timely perspective on the key issues listed companies will need to consider.***

Ashley Alder
Chief Executive Officer, Securities and Futures Commission,
and Chair of the Board, International Organization of Securities Commissions

Executive summary

Climate change is a strategic issue requiring board oversight. Failure to take appropriate steps can expose a company to material business risks. By the same token, companies and directors are also exposed to climate-related litigation risks for failure to consider and manage climate-related risks. Companies preparing climate reporting under the ISSB Board's climate proposal to address climate-related disclosures should adopt a strategic lens and ensure their reporting serves as an appropriate risk mitigation.

This report identifies five focus areas relating to the adoption of the imminent climate reporting regime by the ISSB Board. These areas are either different from or not fully aligned with the HKEX's ESG Reporting Guide, and may therefore be relatively new to companies in Hong Kong. They are:

1. Adopting the 'Enterprise Value' approach to materiality
2. Quantifying the current and anticipated financial effects of climate issues
3. Conducting climate-related scenario analysis
4. Formulating the climate transition plan and setting the targets
5. Determining and reporting on the metrics, such as scope 3 emissions

> ***The IFRS Sustainability Disclosure Standards signal a seismic change in global corporate reporting as it aims to share an entity's sustainability information in a relevant, timely and comparable manner. It may not be easy to achieve this and management will need to put the governance in place to adapt. At KPMG, we have a relentless focus on our Environmental, Social and Governance (ESG) commitments, which we set out in Our Impact Plan (OIP). This allows us to reaffirm our commitments and share our journey to become a better business to all our stakeholders. I truly believe that the development of the global baseline standards can provide a solid foundation for the business community to help shape a more sustainable future — one that is aligned with purpose.***

Andrew Weir
Senior Partner, Hong Kong
KPMG China

In implementing the processes underpinning the ISSB Board's climate reporting regime, common areas of concern include: availability of data, selection of methodology and use of assumptions, coordination of organisational support, and availability of appropriate human and other resources.

Regardless of these concerns, climate change reporting is pressing ahead as it helps drive business performance and create resilience. Regulators and investors are also demanding increased disclosures on how a company's strategy and business model address climate-related risks and opportunities. For example, in Hong Kong, it is expected that mandatory regulatory reporting based on the ISSB Board reporting regime will be in place. Nevertheless, it appears that many listed companies are ill-equipped to deal with these new disclosures and face many challenges with climate change reporting.

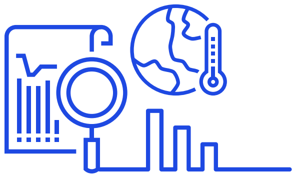
During a webinar hosted by HKCGI on 5 May 2022, featuring speakers from KPMG and CLP, a survey was held to understand how prepared companies in Hong Kong are for climate change reporting. The survey was taken by around 125 respondents, primarily comprising governance professionals from Hong Kong, with key findings summarised on the next page.

> ***The governance professional which our Institute represents is at the forefront of providing governance advice to listed companies and other industry players. This includes reporting on climate change, a most pressing issue of our times. Accordingly, our Institute is proud of our thought leadership position on the emerging international reporting standards and promoting the related best practices to see them through.***

Ernest Lee FCG HKFCG(PE)
President, HKCGI

Climate change reporting by surveyed companies in Hong Kong

Only **17%** have performed a climate-related scenario analysis



Top three challenges to reporting scope 3 emissions are:

37% Hard to get relevant data

23% Lack of internal expertise/resources

17% The selection and application of methodologies

Companies are using a variety of approaches to identify climate-related risks and opportunities*

- Internal management review – 22%
- Stakeholder engagement (excl. with investors and lenders) – 19%
- Engagement with investors and lenders – 16%
- Industry review – 14%
- Peer benchmarking – 13%

86% of respondents stated that their companies have not set a climate transition plan

47% consider that their companies are unlikely to set one

Support needed to adopt ISSB Board's climate proposal*

24% Resources and expertise (both internal and external)

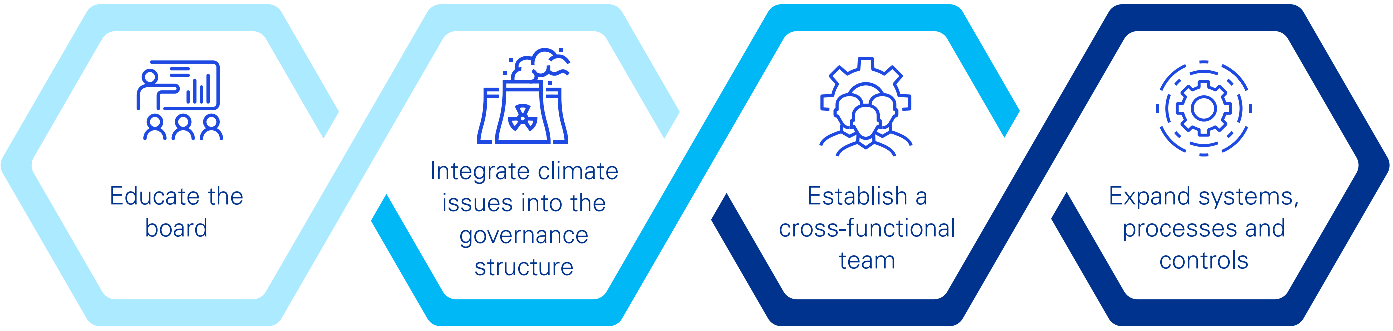
21% Further industry guidance

21% More practical guidance (e.g. case studies)

Results based on a survey held among 125 governance professionals based in Hong Kong

*Respondents could select more than one answer

Recognising that climate change-related disclosures will likely become mandatory and the processes behind the scenes are complex and time-consuming, companies that have not yet started on their climate risk disclosure and net zero planning should do so soon. In addition, this report will consider the necessary opening moves to be adopted by companies, namely the need to:



Governance professionals play a vital role in providing advice and direction on emerging climate reporting requirements and assisting the board in taking the actions to meet those requirements. This report is intended to provide thought leadership from the applied governance perspective on this top of the agenda global issue. The time for action on climate change reporting will be imminent, challenging and likely, mandatory.

> ***Increasing requirements for climate reporting and climate action is the clear direction of travel which no business can ignore and this report contains a host of timely, valuable and practical recommendations for all business in tackling these issues.***

David Simmonds FCG HKFCG

Chief Strategy, Sustainability and Governance Officer, CLP Holdings Limited;
Vice-President and Chairman of the Membership Committee, HKCGI

The International Sustainability Standards Board and its proposals

Before turning to the five focus areas, we recap, for companies and governance professionals, that the International Sustainability Standards Board (ISSB™ Board) is a standard-setting body established under the IFRS Foundation in November 2021. The ISSB Board aims to deliver a comprehensive and global baseline of sustainability-related disclosure standards that meet the information demands of investors and other capital market participants in respect of companies' sustainability-related risks and opportunities.

The ISSB Board works closely with the IFRS's International Accounting Standards Board (IASB® Board) to ensure that the sustainability standards developed by the ISSB Board establish a strong connection with financial statements.

The ISSB Board aims to consolidate and build on the work of existing investor-focused reporting initiatives to create a global baseline for sustainability reporting. Specifically, the ISSB Board has consolidated the Climate Disclosure Standards Board (CDSB) and is expected to consolidate the Value Reporting Foundation, which houses the Integrated Reporting Framework and the Sustainability Accounting Standards Board (SASB), by August 2022.

On 31 March 2022, the ISSB Board released its first two exposure drafts: one outlining general sustainability-related financial disclosures requirements, and another specifically in relation to climate-related disclosures. These two proposals are designed to be applied together for climate reporting. There will be further exposure drafts over time, meaning we are only at the initial stages of developing the ISSB Board's reporting regime. Companies are likely to be impacted by sustainability-related risks and opportunities, in addition to those related to climate change, e.g. biodiversity and human capital. They are advised to monitor the development of future standards as this will affect their disclosures of other sustainability-related risks and opportunities.

> ***We can take a leadership position in Asia if the global baseline standards developed by ISSB are adopted in Hong Kong, starting with climate-related disclosures. Listed companies are encouraged to take early action to integrate climate-related impact into their systems, processes and governance to facilitate reporting under the proposed ISSB framework. This should help reduce reporting burdens against multiple standards and facilitate global comparability of impact of climate-related risks on corporate performance and global efforts to tackle greenwashing. A top-down and bottom-up retuning of mindset from each organisation is needed to tackle the many challenges ahead – to make this once-in-a-generation opportunity a reality.***

Teresa Ko JP BBS
Senior Partner, Hong Kong and China Chairman,
Freshfields Bruckhaus Deringer;
Co-Vice Chair, IFRS Foundation

Proposal 1: Draft IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information

The first proposal relates to the general requirements for disclosure of sustainability-related financial information, including definitions and requirements that are consistent with the IASB Board's Conceptual Framework for Financial Reporting, IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.

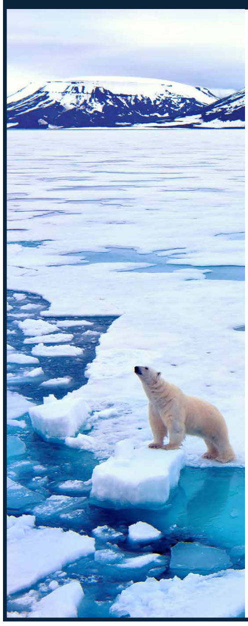
In a nutshell, the proposal requires a company to disclose material information about all the significant sustainability-related risks and opportunities to which it is exposed. It is designed to enable primary users to assess enterprise value.

The proposal builds on the TCFD recommendations and requires disclosure of information on the four core pillars of how a company operates, namely: governance, strategy, risk management, and metrics and targets. It also incorporates the industry-based requirements from the SASB Standards from which a company selects industry-based metrics, among other metrics that are required by the proposal. The SASB Standards are a set of 77 industry-specific standards designed to help companies disclose material and useful information to investors.

The proposal also requires a company to explain the connections between different pieces of information, including the linking of various sustainability-related risks and opportunities to information in the company's financial statements.

The sustainability-related financial information must cover the same reporting entity as the financial statements, and it must be published as part of the company's general-purpose financial reporting. It should also be made available at the same time as the company's financial statements.

Proposal 2: Draft IFRS S2 Climate-related Disclosures



The second proposal focuses on climate-related disclosures and requires a company to disclose information about its exposure to significant climate-related risks and opportunities. The objective of this information is to enable investors and other providers of other financial capital to:

- Assess the effects of significant climate-related risks and opportunities on the company's enterprise value
- Understand how the company's use of resources, and corresponding inputs, activities, outputs, and outcomes support its response to and strategy for managing its significant climate-related risks and opportunities, and
- Evaluate the company's ability to adapt its planning, business model and operations to significant climate-related risks and opportunities.

The proposal incorporates recommendations and guidance from the TCFD and again requires a company to provide information on all four pillars (governance, strategy, risk management, and metrics and targets).

Next steps for the ISSB Board

The ISSB Board is seeking feedback on the proposals by 29 July 2022. It will review the feedback in the second half of 2022 and aims to issue the new standards by the end of 2022. The new standards will become the IFRS Sustainability Disclosure Standards.

At present, the IFRS Sustainability Disclosure Standards are only in their infancy. As noted above, the ISSB Board will issue other topic-specific standards in the future.

As currently worded in the proposals, if a company would like to assert compliance with the IFRS Sustainability Disclosure Standards, for sustainability topics other than climate, it will need to exercise its judgment in identifying disclosures that are relevant to the decision-making needs of the primary users and faithfully represent the company's risks and opportunities in relation to the specific sustainability-related risk or opportunity. In making such judgements, the proposal requires companies to consider the following sources:

- Disclosure topics in the industry-based SASB Standards
- The ISSB Board's non-mandatory guidance (such as the CDSB Framework application guidance for water- and biodiversity-related disclosures)
- The most recent pronouncements of other standard-setting bodies whose requirements are designed to meet the needs of primary users of general-purpose financial reporting
- Sustainability-related risks and opportunities identified by companies that operate in the same industries or geographies

If a company decides to prepare its climate-related disclosures in accordance with the ISSB Board's proposals, but not for other sustainability-related risks and opportunities, then the company cannot assert compliance with the IFRS Sustainability Disclosure Standards, which is likely to be predominantly required by investors over time.

For further details on the two proposals, please refer to the ISSB Board's proposals and KPMG ISG's New on the Horizon publication on sustainability reporting.

"As Asia's largest listed exchange operator and market regulator, HKEX is committed to pioneering and promoting ESG excellence, and will continue to lead our issuers in their sustainability journeys. We strive to create a sustainable framework underpinned by robust ESG standards and regulations. HKEX will review our Rules to further enhance climate disclosures, taking into account the state-of-readiness and capabilities of our issuers. Climate action is no longer a "nice-to-have". Companies must put purpose into practice by setting actionable plans for a low-carbon resilient future."

Bonnie Y Chan
Head of Listing, HKEX

Focus areas

This next section examines the five focus areas that are either different from or are not fully aligned with the HKEX's ESG Reporting Guide. Therefore, we expect preparation work will be needed for those areas as companies look to implement the IFRS Sustainability Disclosure Standards on climate-related information.

Focus area 1: Adopting the 'Enterprise Value' approach to materiality

Materiality is the foundation for reporting under the IFRS Sustainability Disclosure Standards, as it underpins the topics and information that is to be reported. In practice, identifying materiality is a challenging topic for most companies and one that changes over time. The ISSB Board's proposals allow companies not to disclose a specific piece of required information if that information is determined to be not material. On the other hand, a company should consider providing more than the required information if such additional information is considered material.

The ISSB Board's proposals define materiality based on the materiality concept used in the International Financial Reporting Standards (IFRS) Accounting Standards. Information is determined to be material if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that the 'primary users' of general-purpose financial reports make on the basis of those reports. This is an important useful working principle that companies need to consider when in doubt on the issue of materiality.

These primary users are existing and potential investors, lenders and other creditors. The general-purpose financial reporting includes a company's financial statements and sustainability-related financial information. It provides information that is useful to the primary users in making decisions relating to providing resources to the company.

The proposals further explain that sustainability-related financial information is material if it influences primary users' assessments of the company's enterprise value. Enterprise value is defined as the total value of the company and is the sum of the value of the entity's equity (market capitalisation) and the value of the company's net debt. Enterprise value reflects expectations of the amount, timing and certainty of future cash flows over the short, medium and long term and the value of those cash flows in light of the company's risk profile, its access to finance and cost of capital.

The materiality assessment also affects the reporting boundary. While the proposals define the reporting boundary to be the same as the financial statements, they also require the disclosure of information about parties outside of the company when such information affects the primary users' assessment of enterprise value. For instance, a company may determine that information about sustainability risks and opportunities arising from its supplier is material to investors' assessment of its enterprise value.

In addition, the materiality assessment also affects the determination of the completeness of the sustainability topics or information to be reported. The proposals require companies to report on a "complete set" of sustainability-related risks and opportunities. Even if there is no relevant topic-specific IFRS Sustainability Disclosure Standard, a company would need to disclose the topic if the information is determined to be material.

Material sustainability-related financial information disclosed by a company may change from one reporting period to another, as circumstances and assumptions change. Therefore, the proposals require the company to reassess its materiality judgements at each reporting date.

The 'Enterprise Value' approach to materiality adopted by the ISSB Board differs from other sustainability reporting frameworks, which adopt a broader definition of materiality based on the needs of other stakeholders in addition to the providers of financial capital.

In addition, other sustainability reporting frameworks, e.g. GRI, require disclosure of sustainability matters that reflect the significant impacts of a company on the environment and society. This is different from the materiality definition of the ISSB Board's proposals, which focuses on the impacts of sustainability-related matters on the company.

Given the difference in the definition of materiality between the ISSB Board's proposals and broader sustainability reporting frameworks, a company may identify different topics or information that needs to be reported for the existing sustainability reports and the sustainability report prepared under IFRS Sustainability Disclosure Standards. For instance, under the ISSB Board's general requirements proposal, a company does not need to consider all its significant impacts on the environment and society, but only those impacts that could reasonably be expected to affect primary users' assessment of the company's enterprise value.

For example:

- The HKEX defines materiality as "the threshold at which ESG issues determined by the board are sufficiently important to investors and other stakeholders that they should be reported"[4]
- The Global Reporting Initiative (GRI) requires the reporting of matters that reflect a company's significant economic, environmental and social impacts or those that would substantively influence the assessments and decisions of stakeholders.[5]

The 'Enterprise Value' approach to materiality under the proposals may be new to companies that have been preparing ESG reports for wider stakeholders. Meanwhile, the proposals do not specify the process for assessing materiality. A company may find the current process for assessing materiality under the broader sustainability reporting frameworks to be a good starting point and adapt this process to align with the ISSB Board's focus on enterprise value. Regardless, it is best for companies to get up to speed on materiality, including the necessary reporting to primary users and other stakeholders under other sustainability reporting frameworks.

[4] 'How to Prepare An ESG Report', HKEX, 2020, https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/step_by_step.pdf

[5] 'GRI 101: Foundation', GRI, 2016, https://www.globalreporting.org/standards/media/1036/gri-101-foundation-2016.pdf

Focus area 2: Quantifying the current and anticipated financial effects of climate issues

The financial effects of climate-related risks and opportunities provide useful information to investors. As revealed in the TCFD 2021 status report, over nine out of ten users of such information find the disclosure of actual and potential financial impacts useful. Investors leverage such disclosure for financial impact assessments, while rating agencies consider such information as an increasingly important input for the rating process.[6]

The ISSB Board's climate proposal requires a company to disclose quantitative information, expressed as single amounts or a range, about the effects of significant climate-related risks and opportunities on its financial position, financial performance and cash flows for the reporting period, as well as the anticipated effects over the short, medium, and long term. If the company is unable to provide quantitative information of the above matters, it will need to explain why this is the case and provide qualitative information.

Specifically, a company is required to disclose the following, which go outside the realms of traditional reporting:

Subject	Information to be disclosed
Actual financial effects	How significant climate-related risks and opportunities have affected its most recently reported financial position, financial performance and cash flows.
Potential financial effects within the next financial year	Information about climate-related risks and opportunities for which there is a significant risk that there will be a material adjustment to the carrying amounts of assets and liabilities reported in the financial statements within the next financial year.
Potential financial effects over time	How the company expects its financial position and financial performance to change over time, given its strategy to address significant climate-related risks and opportunities. Impacts on the financial position include disclosing: • the company's current and committed investment plans (for example, capital expenditure, major acquisitions and divestments, joint ventures, business transformation, innovation, new business areas and asset retirements), and • its planned sources of funding to implement its strategy. Examples of impacts on the financial performance may include the following: • increased revenue from or costs of products and services aligned with a lower-carbon economy, consistent with the latest international agreement on climate change • physical damage to assets from climate events, and • the costs of climate adaptation or mitigation.
Financial planning	How climate-related risks and opportunities are included in the company's financial planning.

6 'Task Force on Climate-related Financial Disclosures: 2021 Status Report', TCFD, 2021, https://assets.bbhub.io/company/sites/60/2021/07/2021-TCFD-Status_Report.pdf

In its 2021 status report, the TCFD describes several challenges and lessons learnt by preparers, including companies, around effectively assessing and disclosing the financial impact of their climate-related risks and opportunities. These include:[7]

Coordinating organisational support and resources: In view of the wide range of climate-related impacts that can affect a company, financial impact analysis is a multi-disciplinary process that involves personnel and resources from strategy, risk, finance, legal, R&D and sustainability teams, among others. A lack of collaboration can result in difficulties in identifying assumptions and assessing business implications of climate-related risks and opportunities.

Obtaining relevant data: Considering the complexity of estimating financial impacts, it may be difficult to obtain relevant data, examples of which include data from suppliers and granular, asset-level data which serve as inputs to financial impact analysis. Companies will need to consider what the required data are and how to obtain those.

Determining actual financial impacts: This process often includes attributing specific financial effects to climate events, while financial effects can be attributed to a number of factors in addition to climate. It likely involves companies making judgments, which may be subjective in nature, to identify and disaggregate the financial effects driven by climate-related factors from those that are influenced by other factors.

Estimating potential financial impacts: Estimating forward-looking financial impacts involves the selection of a methodology and the use of assumptions. In this regard, climate-related scenario analysis can be a useful tool that helps companies understand and estimate the potential financial effects of climate-related risks and opportunities.

Many TCFD reporters use recognised third-party scenarios, such as those developed by the International Energy Agency (IEA) or Network for Greening the Financial System (NGFS), which contain predetermined methodologies and facilitate comparison of the results. However, these scenarios are not often at the appropriate level of granularity needed for company-level use. Companies that are considering adapting third-party scenarios will likely need support in translating the scenarios to the company or business level.

In addition, climate-related scenarios cover a longer time horizon which goes beyond typical business planning timelines. Companies will need to develop a baseline forecast from which to attribute quantified financial effects and estimate scenario impacts.

Obtaining buy-in to disclose the information: Companies will need to obtain buy-in and approvals from a range of functions, such as legal, corporate communications, finance, and strategy teams. These functions may have concerns about disclosing financial impacts for a variety of reasons, such as concerns about disclosing confidential information about the company's strategy, potential legal liability associated with disclosure of forward-looking information which may vary from actual results, and lack of confidence in data, methodology and assumptions.

Understanding that many companies are in an early stage of quantifying the financial effects of climate-related risks and opportunities, the ISSB Board allows disclosure of qualitative information if a company is unable to provide quantitative information.

Companies preparing themselves for the proposals can refer to the guidance developed by the TCFD and lessons learnt by the TCFD reporters as set out in its 2021 status report.[8]

[7-8] 'Task Force on Climate-related Financial Disclosures: 2021 Status Report', TCFD, 2021, https://assets.bbhub.io/company/sites/60/2021/07/2021-TCFD-Status_Report.pdf

Focus area 3: Conducting climate-related scenario analysis

Climate-related scenario analysis is a process for identifying and assessing a potential range of outcomes of future events under conditions of uncertainty. This is likely to be most challenging to companies. For example, the financial impact of the flooding of waterfront properties owned by a company will depend on the projected rise of sea levels based on a different range of temperature changes. In this case, a scenario analysis will be most useful for primary users' investment decisions. Such an analysis allows a company to explore and develop an understanding of how climate-related risks and opportunities may impact its business, strategies and financial performance over time.

Climate-related scenario analysis can be a useful tool to assess potential financial impacts, as mentioned before. It is also the preferred approach to enable primary users to understand the resilience of a company's business model and strategy to climate change. In this regard, the ISSB Board's climate proposal has built on the TCFD recommendations and incorporated the requirement to apply climate-related scenario analysis – unless a company is unable to do so.

The proposal has also added information to be disclosed regarding significant areas of uncertainty for strategy resilience, a company's capacity to adjust and adapt its strategy over time, and details on how scenario analysis or other assessments have been conducted.

Specifically, the climate proposal requires the disclosure of the following information regarding climate resilience:

<table>
<tr><th>Subject</th><th colspan="2">Information to be disclosed</th></tr>
<tr><td>Results of the analysis</td><td colspan="2">• The implications of the findings for the company's strategy
• Significant areas of uncertainty considered in the analysis
• The company's capacity to adjust or adapt its strategy or business over the short, medium, or long term in terms of:
- The availability of, and flexibility in, existing financial resources to address climate-related risks, and/or to be redirected to take advantage of climate-related opportunities
- The ability to redeploy, repurpose, upgrade, or decommission existing assets, and
- The effect of current or planned investments in climate-related mitigation, adaptation, or opportunities.</td></tr>
<tr><td></td><td>When using climate-related scenario analysis</td><td>When using other assessments rather than climate-related scenario analysis</td></tr>
<tr><td>Overview of the analysis</td><td>• Which scenarios are used and the sources thereof
• Whether a diverse range of scenarios have been compared
• Whether the scenarios are associated with transition risks or physical risks
• Whether a scenario used aligns with the latest international agreement on climate change, and
• An explanation of why the chosen scenarios are relevant to the analysis.</td><td>• An explanation of the methods/ techniques used
• The climate-related assumptions used in the analysis
• An explanation of why those assumptions are relevant to the assessment, and
• An explanation of why the company was unable to use climate-related scenario analysis.</td></tr>
<tr><td>Horizons, inputs and assumptions</td><td>• The time horizons used in the analysis
• The inputs used, including the scope of risks, the scope of operations covered and details of the assumptions, and
• Assumptions about the way the transition to a lower carbon economy will affect the company, including policy assumptions, assumptions about macroeconomic trends, energy usage and mix, and technology.</td><td>• Same as that when scenario analysis is used.</td></tr>
</table>

For companies, climate-related scenario analysis can be a demanding task due to the following:[9]

- Difficulties in developing scenarios that are relevant to the business/company
- Gaps in availability of sufficiently granular, business-relevant data and support tools
- Difficulties in understanding the results of the modelling and translating them into strategic decisions, and
- Concerns about disclosing the results of scenario analysis, which are forward-looking and may be perceived as speculative in nature.

The 2018 to 2021 TCFD Status Reports identified that the percentage of companies disclosing the resilience of their strategies under different climate-related scenarios has been the lowest among all recommended disclosures for all those years.[10]

The ISSB Board also understands that many companies may still be at an early stage of exploring the use of climate-related scenario analysis. As a result, the ISSB Board's proposal allows companies to use an alternative approach if they are unable to conduct climate-related scenario analysis, provided that they disclose information that is similar to that resulting from climate-related scenario analysis and an explanation of why they are unable to conduct the analysis. Examples of alternative approaches include qualitative analysis, single-point forecasts, sensitivity analysis and stress tests.

Various guidance has been issued in recent years to assist companies in exploring the use of climate-related scenario analysis. For instance, TCFD released guidance on how to conduct scenario analysis in 2020.[11] HKEX also issued its guidance on climate disclosures in 2021.[12] The World Business Council for Sustainable Development (WBCSD) also developed business-relevant approaches to climate-related scenario analysis.[13]

[9] 'Task Force on Climate-related Financial Disclosures: Guidance on Scenario Analysis for Non-Financial Companies', TCFD, 2020, https://assets.bbhub.io/company/sites/60/2020/09/2020-TCFD_Guidance-Scenario-Analysis-Guidance.pdf

[10] 'Task Force on Climate-related Financial Disclosures: 2021 Status Report', TCFD, 2021, https://assets.bbhub.io/company/sites/60/2021/07/2021-TCFD-Status_Report.pdf

[11] 'Task Force on Climate-related Financial Disclosures: Guidance on Scenario Analysis for Non-Financial Companies', TCFD, 2020, https://assets.bbhub.io/company/sites/60/2020/09/2020-TCFD_Guidance-Scenario-Analysis-Guidance.pdf

[12] 'HKEX Guidance on Climate Disclosures', HKEX, 2021, https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/guidance_climate_disclosures.pdf?la=en

[13] 'Climate Scenario Analysis Reference Approach: For Companies in the Energy System', WBCSD, 2022, https://www.wbcsd.org/Programs/Redefining-Value/TCFD/Resources/Climate-Scenario-Analysis-Reference-Approach

Focus area 4: Formulating the climate transition plan and setting the targets

A transition plan is an aspect of an entity's overall strategy that outlines the company's targets and actions for its transition towards a lower carbon business model, including actions such as reducing its greenhouse gas emissions. It can be a challenge for companies to put together a strategy on how they intend to reduce their carbon footprint.

China aims to reach peak carbon emissions by 2030 and is committed to being carbon neutral by 2060.[14] Meanwhile, the Hong Kong SAR Government has pledged to achieve carbon neutrality by 2050, and set out its strategy to achieve this in its Climate Action Plan 2050.[15] To align with these goals and help achieve the carbon reduction commitments, reporting companies will need to prepare themselves to transition to a lower carbon economy.

Disclosing a company's transition plan is important. This disclosure not only enhances the credibility of the company's climate change commitments, but also provides information on how the company will adjust its strategies or business models to reduce climate-related risks and capture climate-related opportunities, which in turn may affect its enterprise value.

The ISSB Board's climate proposal requires a range of disclosures about a company's transition plan:

Subject	Information to be disclosed
Current and anticipated changes to its business model	• Changes in strategy and resource allocation to address climate-related risks and opportunities, including plans and critical assumptions for legacy assets • Direct and indirect adaptation and mitigation efforts, and • How these plans will be resourced.
Climate-related targets	• Process for review of the targets • Amount of the emissions target to be achieved through emissions reductions, and • Carbon offsets: the extent of usage; whether the carbon offsets are subject to third-party offset verification or certification schemes, and if yes, which schemes; type of carbon offsets; and any other factors relating to the credibility and integrity of the offsets.
Progress	• Quantitative and qualitative information about the progress of plans disclosed in prior reporting periods.

As the climate transition plan is about how a company responds to climate-related risks and opportunities, the transition plan should align with the company's overall strategy.

In addition, the transition plan describes the metrics the company will monitor to track progress against its plans and targets. Those metrics should be aligned with cross-industry metrics, industry-based metrics, company-specific metrics and related targets required by the ISSB Board's climate proposal (refer to page 20 of this report for details).

In light of the complexities and uncertainties around climate change, companies may need support in terms of identifying and implementing mitigation and adaptation efforts, estimating the effects or outcomes of these efforts, which can impact the setting of targets and reviews of progress. As companies will need to disclose metrics, targets and progress compared with prior periods, they may struggle to set targets that are achievable and demonstrate improvements each year. In this regard, companies can refer to guidance on transition plans and targets developed by the TCFD[16] as a starting point.

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[14] 'China Maps Path to Carbon Peak Neutrality under New Development Philosophy', Xinhua, 2021, http://english.www.gov.cn/policies/latestreleases/202110/24/content_WS61755fe9c6d0df57f98e3bed.html

[15] 'Hong Kong's Climate Action Plan 2050', Hong Kong SAR Government, 2021, https://www.climateready.gov.hk/files/pdf/CAP2050_booklet_en.pdf

[16] 'Task Force on Climate-related Financial Disclosures: Guidance on Metrics, Targets and Transition Plans', TCFD, 2021, https://assets.bbhub.io/company/sites/60/2021/07/2021-Metrics_Targets_Guidance-1.pdf

Focus area 5: Determining and reporting on the metrics

Climate-related metrics support the measurement of risk exposures and inform primary users about how the company tracks and manages climate-related risks and opportunities. The metrics required by the climate proposal may be relatively new to companies in Hong Kong and therefore, much preparation work is required.

The ISSB Board's proposals require disclosure of the following metrics and targets:

Table A

Type of metrics	Metrics to be disclosed
1. Cross-industry metrics	The climate proposal requires the same categories of cross-industry metrics as in the TCFD guidance. Please refer to table B for details.
2. Industry-based metrics	Companies select the applicable industry-based metrics from Appendix B of the proposed standard; these metrics are derived from the SASB Standards.[17] For companies which operate in multiple sectors, more than one set of industry-based metrics may be required.
3. Other metrics	When a metric has been developed internally, the general requirements proposal requires the disclosure of: • How the metric is defined, and any sources used to construct the metric • Whether the measurement of the metric is validated by an external body and if so, which body, and • Explanations of the method used to calculate the targets and inputs to the calculation, including significant assumptions and limitations.
4. Targets	For each climate-related target, the following information must be disclosed: • Metrics used to assess progress • The specific target set • Whether the target is an absolute or intensity target • The objective of the target (e.g. mitigation, adaptation or conformance with sector or science-based initiatives) • How the target compares with those created in the latest international agreement on climate change and whether it has been validated by a third party • Whether the target was derived using a sectoral decarbonisation approach • The period over which the target applies • The base period from which progress is measured, and • Any milestones or interim targets.

[17] 'Appendix B – Industry-based disclosure requirements', IFRS Foundation, accessed on 8 May 2022, https://www.ifrs.org/projects/work-plan/climate-related-disclosures/appendix-b-industry-based-disclosure-requirements/

Target-setting is closely associated with the formulation of the climate transition plan as it is discussed at the beginning of transition planning.

With respect to cross-industry metrics, the climate proposal prescribes that the following metrics be disclosed:

Table B

Categories of metrics	Metrics to be disclosed
1. Greenhouse gas emissions	Consistent with the TCFD guidelines, the climate proposal requires the use of the Greenhouse Gas Protocol and disclosure of emissions on an absolute and intensity basis. However, the proposal requires that additional details be disclosed. For scope 1 and scope 2 emissions: • Emissions for the consolidated group, and • Emissions for associates, joint ventures, unconsolidated subsidiaries or affiliates; the approach used to include emissions; and the reasons for the choice of approach. For scope 3 emissions: • Include upstream and downstream emissions in the measurement • Disclose the categories included within the measurement to show which scope 3 activities have been included or excluded • Explain the basis for measurement when including information provided by entities in the value chain, and • State the reason for omitting emissions from the measurement.
2. Transition risks	The amount and percentage of assets or business activities vulnerable to transition risks.
3. Physical risks	The amount and percentage of assets or business activities vulnerable to physical risks.
4. Climate-related opportunities	The amount and percentage of assets or business activities aligned with climate-related opportunities.
5. Capital deployment	The amount of capital expenditure, financing or investment deployed towards climate-related risks and opportunities.
6. Internal carbon prices	The price for each metric tonne of greenhouse gas emissions that a company uses to assess the cost of its emissions. An explanation of how the company is applying carbon prices in decision-making.
7. Remuneration	The percentage of executive management remuneration recognised in the current period that is linked to climate-related considerations. A description of how climate-related considerations are factored into executive remuneration.

If a metric or target is revised, the company is required to explain the changes and the reasons therefor, and to provide restated comparative figures unless it is impracticable to do so. For metrics two to seven in Table B, the climate proposal requires companies to consider the relationship between these metrics and the amounts recognised and disclosed in the financial statements.

Scope 3 emissions

In view of the increasing recognition that scope 3 emissions are a critical component of a company's carbon footprint, the ISSB Board's climate proposal goes beyond the TCFD recommendations and requires the disclosure of scope 3 emissions. This aligns with the demands from investor initiatives for the disclosure of such information. In addition, as various jurisdictions announce their net-zero pledges, they may require comprehensive carbon reporting from companies to track their carbon emission reduction commitments.

Despite the importance of scope 3 emissions, the disclosure of such information involves challenges around data access and methodology selection as mentioned by respondents in the TCFD's 2021 survey:[18,19]

Data access: Difficulties arise from collecting reliable and sufficiently granular primary data over the value chain and in managing the volume of such data. Overcoming these difficulties requires significant resources and data management solutions.

Companies may use secondary data or industry-average emissions factors where available. However, using such data presents challenges due to inadequate transparency around data quality and the potential for uneven distribution of greenhouse gas emissions within an industry.

Methodology selection: Methodological challenges occur when estimating greenhouse gas emissions of activities across the value chain including the unavailability of relevant data, defining an appropriate calculation approach for all scope 3 activities, and addressing the potential risk of double counting when greenhouse gas emissions are aggregated across entities.

Industry-led initiatives may help resolve these issues by compiling relevant data, enhancing transparency and developing better practices.

Other cross-industry metrics

With the exception of emissions metrics, other cross-industry metrics are not currently required by the HKEX ESG Reporting Guide and may be relatively new to Hong Kong companies. As a result, companies should define the metrics, set up processes and controls to collect data that is relevant, reliable, and consistent with financial statements, and determine the methodologies and assumptions to use where appropriate.

Industry-based metrics

The industry-based metrics in the ISSB Board's proposals are derived from the SASB Standards. In 2021, nearly half of SASB reporters (48 percent) were domiciled in the US, and only 10.4 percent of SASB reporters were domiciled in Asia Pacific.[20] Therefore, the SASB Standards may be relatively new to Hong Kong companies. In the proposals, the industry-based metrics are referenced to international standards and definitions in order to improve their international applicability. Companies adopting the ISSB Board's proposals will need to understand the industry-based metrics, apply materiality judgements to the metrics, and adapt their existing data compilation processes to the metrics and/or set up new processes.

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18 'Metrics, Targets and Transitional Plans Consultation: Summary of Responses', TCFD, 2021, https://assets.bbhub.io/company/sites/60/2021/08/Summary-of-June-2021-Public-Consultation.pdf

19 'Task Force on Climate-related Financial Disclosures: Guidance on Metrics, Targets and Transition Plans', TCFD, 2021, https://assets.bbhub.io/company/sites/60/2021/07/2021-Metrics_Targets_Guidance-1.pdf

20 'Investor and Market Support', SASB, accessed on 19 April 2022, https://www.sasb.org/about/global-use/#investor-market-support

Readiness of surveyed Hong Kong companies

On 5 May 2022, HKCGI hosted a webinar, featuring speakers from KPMG and CLP, to raise awareness of the ISSB Board proposals and gather feedback from the 125 participants on their companies' readiness in adopting ISSB Board's proposals. The participants primarily comprised governance professionals from Hong Kong.

The results of the polling questions confirm that Hong Kong companies are facing similar challenges as outlined in this report.

Only **7%** and **4%** of respondents **adopted TCFD recommendations and SASB standards**, respectively. This implies that many companies are likely to experience a significant gap between current climate reporting and the ISSB Board's climate proposal, which builds on TCFD recommendations and SASB standards.

The results of the survey also show that a variety of approaches to **identifying climate-related risks and opportunities** are being taken by companies in Hong Kong. Nearly a quarter **(22%)** reported that their companies currently identify these through an internal management review, but this was closely followed by stakeholder engagement (excluding investors and lenders) **(19%)**, engagement with investors and lenders **(16%)**, industry review **(14%)** and peer benchmarking **(13%)**.

Just **over a third** of respondents **(34%) did not have a plan to conduct a scenario analysis**, while **25%** have plans to prepare one within one to two years. Only **17%** of respondents advised that their companies had already prepared a scenario analysis, while **11%** are currently preparing one.

Key challenges in performing a scenario analysis were found to be sourcing relevant data **(29%)**, lack of expertise resources **(25%)**, selection and application of methodologies **(21%)**, development of relevant scenarios **(19%)** and lack of internal buy in **(6%)**.

A large majority **(86%)** confirmed that their companies have not set a **climate transition plan**, while **47%** onsider that their companies are **unlikely to set one**.

Meanwhile, **around a third** of respondents **(37%)** have not determined what **climate related metrics** are to be reported on, with **28%** expressing concerns about how the company will compare with its peers.

The **top three challenges** arising from the reporting of scope 3 emissions are: hard to get relevant data **(37%)**, lack of internal expertise/resources **(23%)**, followed by the selection and application of methodologies **(17%)**.

In terms of **support**, respondents identified internal and external resources and expertise **(24%)**, further industry guidance **(21%)** and more practical guidance, e.g. case studies **(21%)**, as their most pressing needs.

Conclusion and next steps for companies

Climate change is a board-level strategic issue and a failure to take appropriate steps exposes a company to material business risks. Companies preparing climate reporting under the ISSB Board's climate proposal need to take a strategic lens and let the reporting follow from that. They should not treat this as a box-ticking exercise, but as a framework to guide business and investment decisions.

As discussed in this report, the processes underpinning the ISSB Board's climate reporting involve significant efforts. Serious implementation of these processes requires commitment from leadership and others across the company, as well as appropriate resources. A light touch approach will not provide investors with useful information and could result in substantial risk management issues if a company fails to fully understand and act on the impacts of climate change on its business.

The disclosure landscape is evolving rapidly and the pressure to disclose more is growing. Regulators and investors are demanding increased disclosures on how a company's strategy and business model is responding to climate-related risks and opportunities. Recognising that such disclosure is likely to become mandatory, and that the processes behind the scenes are complex and time-consuming, companies that have not yet started compiling these disclosures and net zero planning should do so without delay.

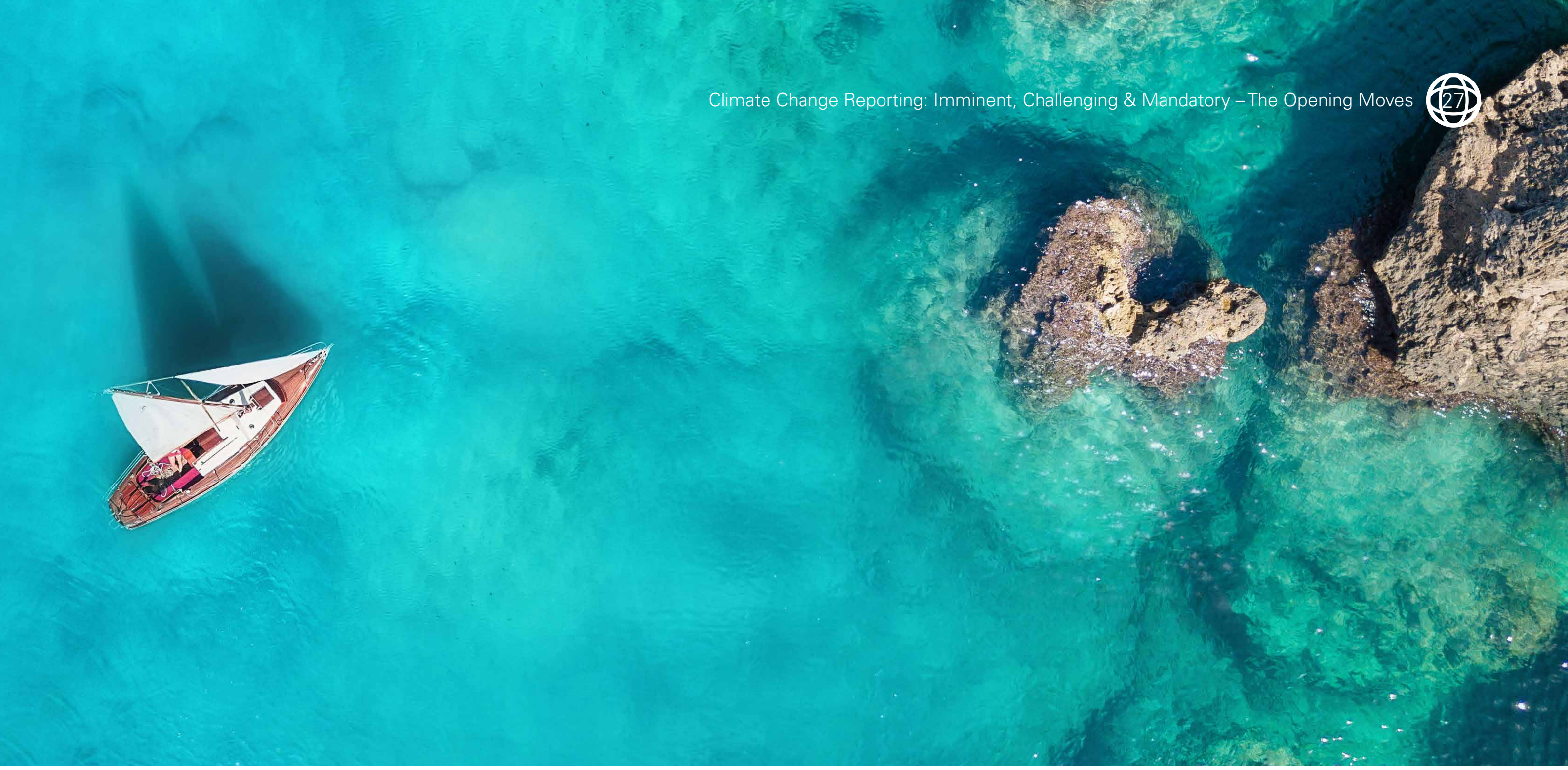
As closing thoughts for companies starting out on the journey, we recommend the following:

Educate the board: As the board takes accountability for monitoring and managing climate-related risks and opportunities, it should understand the latest developments in climate issues and the related reporting landscape, the company's potential exposure to climate-related risks and opportunities, and the potential implications on the company's strategy and business model.

Governance professionals should educate the board about the emerging climate reporting requirements and the potential impacts and challenges. Various platforms such as HKEX's ESG Academy and TCFD Knowledge Hub provide useful resources in this regard.

Integrate climate issues into governance structure: The board should integrate climate-related issues into strategy and decision-making processes and enhance board-level oversight over monitoring and management of climate-related risks and opportunities. This helps to secure commitment and support from the leadership.

Governance professionals may assist the board in enhancing the current governance structure, including the roles of the board and management.



Establish a cross-functional team: A cross-functional team is important to both act on climate issues and report on the company's climate responses. A diverse team helps to obtain buy-in and support from across the organisation. It also brings together different skill sets.

For instance, Sustainability professionals have an understanding of climate issues. Strategy professionals and risk management experts can advise on the impacts on strategy and business models. Finance professionals can help understand and quantify the financial effects and connect climate and financial reporting.

Governance professionals may assist the board in establishing the multi-disciplinary team to implement the needed processes and tackle the challenges described in this report.

Expand systems, processes and controls: Companies will need processes and controls to quantify financial effects of climate issues, conduct climate-related scenario analysis and report on metrics. Companies should engage with current process owners to understand how information is being defined, captured and reported and where there are data gaps and control gaps.

The cross-functional team may need to assist the board in identifying these gaps and expanding existing systems, processes and controls to ensure data integrity and avoid duplication between different types of reporting.

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About HKCGI

(Incorporated in Hong Kong with limited liability by guarantee)

The Hong Kong Chartered Governance Institute (HKCGI), formerly known as The Hong Kong Institute of Chartered Secretaries (HKICS), is the only qualifying institution in Hong Kong and the Mainland of China for the internationally recognised Chartered Secretary and Chartered Governance Professional qualifications.

With over 70 years of history and as the Hong Kong/China Division of The Chartered Governance Institute (CGI), the Institute's reach and professional recognition extends to all of CGI's nine divisions, with more than 40,000 members and students worldwide. HKCGI is one the fastest growing divisions of CGI, with a current membership of over 6,800, 300 graduates and 3,000 students with significant representations within listed companies and other cross-industry governance functions.

Believing that better governance leads to a better future, HKCGI's mission is to promote good governance in an increasingly complex world and to advance leadership in the effective governance and efficient administration of commerce, industry and public affairs. As recognised thought leaders in our field, the Institute educates and advocates for the highest standards in governance and promotes an expansive approach which takes account of the interests of all stakeholders.

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About CLP

The CLP Group is one of the largest investor-owned power businesses in Asia Pacific with investments across Hong Kong, Mainland China, Australia, India, Southeast Asia and Taiwan. Hong Kong-listed CLP Holdings Limited is the holding company for the CLP Group, which has a diversified portfolio of generating assets that uses a wide range of fuels including coal, gas, nuclear and renewable sources.

Through CLP Power Hong Kong Limited, the Group operates a vertically integrated electricity supply business that provides a highly reliable supply of electricity to 80% of Hong Kong's population. In Mainland China, the CLP Group is the largest external independent power producer with a focus on low-carbon energy. In Australia, the Group's wholly-owned subsidiary EnergyAustralia is a leading integrated energy company, providing gas and electricity to about 2.44 million households and businesses. Apraava Energy (formerly known as CLP India) is one of India's biggest renewable energy producers with operations in power generation and transmission.

CLP Holdings is included in the Global Dow – a 150-stock index of the world's leading blue chip companies, the Dow Jones Sustainability Asia Pacific Index (DJSI Asia Pacific), the Dow Jones Sustainability Asia Pacific 40 Index (DJSI Asia Pacific 40), the Hang Seng Corporate Sustainability Index Series and the FTSE4Good Index series.

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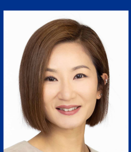

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