New Climate-Related ESG Disclosures for Hong Kong-Listed Issuers

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The Stock Exchange of Hong Kong Limited (the "HKEx") has published consultation conclusions on the new climate-related disclosure requirements (the "New Climate Requirements") for issuers in their environmental, social and governance ("ESG") reports for financial years commencing on or after 1 January, 2025.

The New Climate Requirements closely align with the IFRS S2 climate-related disclosures published by the International Sustainability Standards Board (the "ISSB"). They form part of the Hong Kong roadmap for the local adoption of the ISSB Standards to prepare issuers for internationally recognised sustainability reporting.

The HKEx previously postponed the implementation date to ease undue burdens on issuers. To ensure a reasonable timeframe for compliance, the HKEx will adopt a phased implementation: certain disclosures will be "comply or explain" for the first financial reporting year, and implementation relief is available for issuers preparing to make disclosures.

This In Depth explains the New Climate Requirements, compares Hong Kong's progress with its counterparts in the Asia Pacific and suggests practical tips for preparing to make disclosures, manage risks and meet regulatory expectations.

Background

Currently, listed companies in Hong Kong are subject to the Environmental, Social and Governance Reporting Guide (the "ESG Reporting Guide") requirements,[1] and the Corporate Governance Code. This framework has two levels of reporting requirements: mandatory disclosure and "comply or explain", where issuers either disclose the required information or explain the reasons for not doing so.

Main Board issuers are required to make climate-related disclosures on a "comply or explain" basis in their ESG reports, but board directors are mandated to provide a

[1] Appendix 27 to the Main Board Listing Rules; Appendix 20 to the GEM Listing Rules.

statement on the board's oversight of ESG issues, ESG management approach and strategy; ESG progress reviews; and a description of how ESG-related goals and targets relate to the business.

The HKEx has undertaken extensive efforts in recent years to enhance its ESG-reporting framework. In July 2020, the HKEx incorporated elements of the Task Force on Climate-related Financial Disclosures (the "TCFD") recommendations in an updated version of the ESG Reporting Guide. The Hong Kong Green and Sustainable Finance Cross-Agency Steering Group (the "Group"), established in 2020, is co-chaired by the Hong Kong Monetary Authority and the Securities and Futures Commission. The Group is committed to coordinating with the financial sector to address climate and environmental risks, accelerating the growth of green and sustainable finance and facilitating the implementation of Hong Kong's Climate Action Plan 2050.

New Climate Disclosure Requirements

The New Climate Requirements were developed based on IFRS S2. These are part of the ISSB Standards, which serve as the global baseline of sustainability reporting standards with the aim of aligning the sustainability disclosures made by entities worldwide.

The New Climate Requirements introduce enhanced climate-related disclosures through a new Part D to Appendix C2 of the HKEx Listing Rules. The ESG Reporting Guide will be renamed the ESG Code (the "ESG Code").

Closely mirroring the ISSB Standards, the New Climate Requirements are consistent with the four core TCFD recommendations, which are fully incorporated into the ISSB Standards: governance; strategy; risk management; and metrics and target.

- *Governance*: Issuers will be required to disclose information about the body(ies) or individual(s) responsible for oversight of climate-related risks and opportunities. This includes management's role in the governance processes, controls and procedures.

- *Strategy*: The ESG Reporting Guide already requires issuers to provide general disclosures about board management of ESG considerations. The New Climate Requirements require issuers to specifically consider the different nature and types of climate-related risks and opportunities and make appropriate assessments on a short-, medium- or long-term basis. Issuers will need to identify and disclose their assessment of material climate-related risks and opportunities and the impact on their business operations, business model and strategy transition plans; climate-related targets; climate resilience; and any related financial effects.

- *Risk Management*: The ESG Reporting Guide does not require any disclosure of specific risk management processes on climate-related risks. The New Climate Requirements mandate that issuers disclose their risk management process used to identify, assess, monitor and manage climate-related risks and opportunities.

- *Metrics and Targets*: The ESG Reporting Guide requires issuers to disclose emissions and other environmental KPIs on a "comply or explain" basis. The New Climate Requirements will require issuers to disclose Scope 1 (direct emissions), Scope 2 (emissions associated with purchased electricity) and, for certain issuers, Scope 3 (emissions from a company's value chain) greenhouse gas ("GHG") emissions and other cross-industry climate metrics applicable to all organisations, including the internal carbon price on each metric tonne of GHG emissions used and whether and how executive remuneration is linked to climate considerations.

By requiring issuers to provide broader and anticipatory disclosures, the New Climate Requirements are likely to drive a paradigm shift away from the traditional corporate sustainability reporting of emissions or energy consumption data. Issuers will be required to:

- incorporate sustainability considerations into their corporate strategy planning;
- actively identify climate-related risks and opportunities;
- develop action plans and targets to tackle these; and
- consider any necessary changes to business models and strategies.

Overall, companies should be incentivised to develop innovative, sustainable and resilient products and services that will move Hong Kong closer towards the goal of reaching net zero by 2050.

Implementation Timeline and Interim Reliefs

The HKEx will adopt a phased approach to implement the New Climate Requirements to provide issuers with sufficient time to prepare for the changes. The implementation timeline varies for different types of issuers. To assist issuers preparing to make disclosures, the HKEx has published implementation guidance that sets out principles, guidelines, tools and illustrative examples for preparing for disclosures.[2]

The ESG Code divides issuers into three categories: (i) issuers in the Hang Seng Composite LargeCap Index immediately prior to the reporting year ("LargeCap Issuers"); (ii) Main Board issuers other than LargeCap Issuers ("Main Board Issuers"); and (iii) GEM issuers ("GEM Issuers").

With effect from January 1, 2025, all issuers must report on Scope 1 and Scope 2 emissions for financial years commencing on or after January 1, 2025. These disclosures are intended to provide a solid basis for assessing a company's potential climate impact caused by GHG emissions.

Scope 3 emissions paint a more comprehensive picture of a company's carbon footprint. From January 1, 2025, Main Board Issuers must disclose Scope 3 emissions and all other climate-related disclosure requirements on a "comply or explain" basis, and GEM Issuers are encouraged to make disclosures voluntarily. From January 1, 2026, LargeCap Issuers will be required to make these disclosures on a mandatory basis.

The New Climate Requirements include certain implementation relief to address concerns over reporting challenges caused by lack of resources, technical knowledge and/or expertise. When applying the related relief, issuers are expected to provide considered reasons as to why specific disclosure requirements could not be complied with and provide action plans indicating when the requirements will be met.

The implementation timeline only relates to issuers' disclosure obligations under the new Part D of the ESG Code. All other non-climate disclosure requirements in Parts A to C of the ESG Code will continue to apply and must be included in issuers' ESG reports.

Alignment with ISSB Standards

The New Climate Requirements are based on the ISSB climate-related disclosures standards (IFRS S2). The HKEx implementation guidance also makes use of the ISSB general requirements for disclosure of sustainability-related financial information standards (IFRS S1). By aligning with the ISSB Standards, the HKEx is preparing issuers for eventual sustainability reporting in line with internationally recognised standards. The HKEx has produced a detailed side-by-side comparison between the IFRS S2 requirements and the New Climate Requirements, which depart from IFRS S2 in a few instances.

[2] Implementation Guidance for Climate Disclosures under HKEX ESG reporting framework, April 2024.

The ISSB Standards require certain additional disclosures not required by the ESG Code. The ISSB Standards require entities to disclose: (i) Scope 1 and Scope 2 emissions disclosures on a disaggregated basis between the consolidated accounting group and other investees; (ii) additional information about category 15 GHG emissions; and (iii) industry-based metrics, although all such disclosures are encouraged by the ESG Code or the implementation guidance. Further, the ESG Code does not require or encourage disclosure of the percentage of remuneration linked to climate-related considerations.

Conversely, the ESG Code requires issuers to make a negative statement (clarifying that relevant disclosures are only required if applicable) where they do not: (i) have a climate-related transition plan; (ii) apply a carbon price in decision-making; or (iii) factor climate-related considerations into remuneration policies. Such requirements are not prescribed under the ISSB Standards.

The ESG Code confirms that ESG reports that comply with the ISSB Standards will be deemed to comply with the New Climate Requirements. By comparison, whilst there is a close correlation between the European Sustainability Reporting Standards (the "ESRS") and the ISSB Standards, the European Union has not made a general determination of equivalence between the ISSB Standards and the ESRS. This makes the New Climate Requirements one of the first sets of mandatory climate-related disclosures that are deemed as equivalent to the ISSB Standards.

Comparison with Other APAC Countries

Other APAC countries are considering following suit. The draft Australian sustainability reporting standards (the "ASRS") were developed using the ISSB Standards as a baseline but include certain modifications. Notably, the ASRS limits the applicability of IFRS S1 general disclosure requirements to climate-only matters. Climate-related financial disclosures do not apply to climate-related emissions (e.g., ozone-depleting emissions) that are not GHG emissions.

Japan and Singapore have released similar exposure drafts based on the ISSB Standards. The Sustainability Standards Board of Japan (the "SSBJ") proposed sustainability-reporting standards that are closely aligned with the ISSB Standards, albeit including certain "jurisdiction-specific options" such as the ability to report information for a different period from financial statements. The SSBJ expects to publish the finalised standards by April 2025.

In July 2023, the Sustainability Reporting Advisory Committee in Singapore proposed to mandate climate-related disclosures for issuers and large non-listed companies in Singapore with a similar phased implementation timeline. The proposals are aligned with IFRS S2. Additionally, reporting entities will be required to apply the general disclosure requirements under IFRS S1 as they relate to climate-related risks and opportunities.

Whilst China has proposed a new set of climate-disclosure rules for large listed companies on GHG emissions, use of carbon offsets, and plans, systems and processes to manage climate risk, the draft rules do not explicitly reference the ISSB framework. However, the inclusion of the double-materiality concept (reporting on how the company impacts the environment as well as how the environment impacts the company) is more closely aligned with the ESRS than the ISSB, which is focused solely on enterprise value.

Practical Tips

As a leading capital market destination, Hong Kong plays a vital role in promoting sustainable finance. Investors increasingly consider ESG factors in their decision-making. Transparent and robust sustainability reporting is needed to provide investors with the information required to make informed investment decisions.

Issuers already report on emissions, waste, energy consumption and certain environmental KPIs on a "comply or explain" basis. To prepare for mandatory disclosures of Scope 1 and Scope 2 emissions (and eventually Scope 3 emissions), issuers should familiarise themselves with the Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard (2004) and the requirements for measuring GHG emissions. Whilst Scope 3 emissions disclosure will only be mandatory for LargeCap Issuers, all issuers should start collecting the relevant data and calculations now in light of the direction of travel for climate-related disclosures. Issuers should also consider potential exposure to ESG-related reporting frameworks in other jurisdictions, such as the EU's Corporate Sustainability Reporting Directive and the U.S. SEC's recently enacted climate-related disclosure rule, currently stayed pending the outcome of legal challenges to the rule.

Issuers should also undertake a gap analysis of their current sustainability disclosures and ESG reports to establish action plans for complying with the New Climate Requirements. The HKEx has previously commented on the importance of good disclosure and the need to avoid partial disclosures (which can be passively misleading statements). Issuers should review existing ESG disclosures to ensure they are up to date, free of greenwashing and a complete reflection of sustainability practices, climate-related targets and opportunities and risks. The HKEx places a high value on proper disclosure to the market and enforcement action may be taken when requirements are not met.

It is clear that the HKEx expects company boards and senior management to drive the promotion of sustainability from the top and closely assess, report, monitor and manage climate-related risks and opportunities. With the New Climate Requirements on the horizon, issuers should conduct a thorough review of their internal governance and risk management process, controls, procedures and resources to ensure that they are well-positioned to manage such risks and opportunities.

The New Climate Requirements aligned with the ISSB Standards present an opportunity to avoid duplicative climate-related disclosures. Issuers with multinational operations should seek to integrate their internal governance procedures and controls and disclosure and reporting mechanisms. Further, issuers should consider integrating sustainability reporting with financial reporting early, as additional resources or capacity may be required to provide integrated reporting. Issuers should consider aligning reporting entities and operations in ESG reports with their financial reporting.

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