



專業培訓中心  
Professional Training Center

## Updates on Corporate Governance Codes and Preparation of Corporate Governance Report

Date 5 March 2014

Time 19:00 – 21:00

Venue Duke of Windsor Social Service Building



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## Today's Agenda

- Recent developments of Corporate Governance Codes (“Codes”)
- Preparation of Corporate Governance Report
- Common issues on corporate governance in IPO and resumption of trading of listed shares
- Future development
- Q&A

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## Recent developments of Corporate Governance Codes (“Codes”)

- Since financial year beginning 1 January 2005:
  - Introduction of Codes of Corporate Governance under Appendix 14 and Appendix 15 of the Listing Rules and the GEM Listing Rules respectively;
  - Listed issuers are required to include a corporate governance report (“CG Report”) included in the annual report; and
  - Comply or explain basis

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## Recent developments of Corporate Governance Codes (“Codes”)

- Since financial year beginning 1 January/1 April 2012:
  - Setting out the principles of good corporate governance in two levels of recommendations: (a) code provisions (“CPs”); and (b) recommended best practices (“RBP”);
  - Some CPs have been promoted to Rules and many RPBs have also been upgraded to CPs; and
  - Comply or explain basis for CPs, whereas RPBs are encouraged, but not required, to state whether they have been adopted.

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## Recent developments of Corporate Governance Codes (“Codes”)

- Independent non-executive directors (Rules):
  - Independent Non-Executive Director(s) (“INEDs”) should constitute one third of an issuer’s board (previously a recommended best practice). (Rule - full compliance mandatory by 31 December 2012); and
  - Removed the requirement for a company secretary to be ordinarily resident in Hong Kong. (Rule - w.e.f. 1 January 2012).

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## Recent developments of Corporate Governance Codes (“Codes”)

- Corporate governance committee (CP - w.e.f. 1 Apr 2012):
  - Require the board to be responsible for corporate governance and the Group should establish terms of reference on duties that should be performed by the board or committees delegated by the board; and
  - Disclose the corporate governance policy and duties performed in Corporate Governance Report.

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## Recent developments of Corporate Governance Codes (“Codes”)

- Audit committee (CP - w.e.f. 1 Apr 2012):
  - The audit committee should meet at least twice a year (instead of once a year) with the issuer’s external auditor.

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## Recent developments of Corporate Governance Codes (“Codes”)

- Remuneration committee (Rule 3.25 - w.e.f. 1 Apr 2012):
  - To require the establishment of a remuneration committee and require the remuneration committee to be chaired by an INED.

## Recent developments of Corporate Governance Codes (“Codes”)

- Nomination committee (CP - w.e.f. 1 Apr 2012):
  - To require the establishment of a nomination committee and require the nomination committee to be chaired by a chairman of the board or an INED.

## Recent developments of Corporate Governance Codes (“Codes”)

### ■ Disclosures:

- Disclose the CEO’s remuneration (if he is not a director) by name. (Rule - w.e.f. 1 Jan 2012);
- Disclose the senior management\* remuneration by band. (CP - w.e.f 1 Apr 2012);
- Include in the annual report an explanation of the basis on which the company generates or preserves value over the longer term (business model) and the strategy for delivering the objectives of the company (corporate strategy). (CP - w.e.f. 1 Apr 2012);

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## Recent developments of Corporate Governance Codes (“Codes”)

### ■ Disclosures – cont’d:

- Management should provide monthly updates to board members to enable them to discharge their duties. The monthly updates may include information such as monthly management accounts and management updates. (CP - w.e.f. 1 Apr 2012).
- \* *Senior management is defined as the same persons whose biographical details are disclosed as required by Appendix 16 of the Listing Rules.*

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## Recent developments of Corporate Governance Codes (“Codes”)

- Auditors:
  - To require shareholders’ approval for appointment or removal of an auditor before the end of his term of office. (Rule - w.e.f. 1 Jan 2012);
  - The auditor must be allowed to make a written and/or verbal representation at the general meeting to remove him. (Rule - w.e.f. 1 Jan 2012); and
  - Management should ensure the external auditor attend the annual general meeting to answer questions. (CP - w.e.f. 1 Apr 2012).

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## Recent developments of Corporate Governance Codes (“Codes”)

- Board Diversity effective on 1 September 2013:
  - Introduced a Code Provision in the Corporate Governance Code and Corporate Governance Report that requires issuers – on a “comply or explain” basis – to have a policy concerning diversity in the board, and to disclose that policy in their Corporate Governance Report; and
  - Introduced a requirement that if the issuer has a board diversity policy, the disclosure in its Corporate Governance Report concerning the nomination committee should include any measurable objectives that it has set for implementing the policy, and progress on achieving those objectives.

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## Preparation of Corporate Governance Report

- Reporting period covers the annual report period **and significant subsequent events up to the date of publication of annual report**; and
- Mandatory information included:
  - Corporate governance practices;
  - Directors' securities transactions – Model Code of securities transactions;
  - Board of directors;
  - Chairman and chief executive;
  - Non-executive directors;
  - Board committees;
  - Auditor's remuneration;

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## Preparation of Corporate Governance Report

- Mandatory information included – cont'd:
  - Company secretary;
  - Shareholders' rights; and
  - Investor relations

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## Preparation of Corporate Governance Report

- Common issues on compliance of the Codes:
  - A.1.1 - The board should meet regularly and board meetings should be held at least four times a year at approximately quarterly intervals;
  - A.1.3 - Notice of at least 14 days should be given of a regular board meeting to give all directors an opportunity to attend. For all other board meetings, reasonable notice should be given;
  - A.2.1 - The roles of chairman and chief executive should be separate and should not be performed by the same individual. The division of responsibilities between the chairman and chief executive should be clearly established and set out in writing

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## Preparation of Corporate Governance Report

- Common issues on compliance of the Codes – cont'd:
  - A.2.7 - The chairman should at least annually hold meetings with the non-executive directors (including independent non-executive directors) without the executive directors present;
  - A.4.1 - Non-executive directors should be appointed for a specific term, subject to re-election;

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## Preparation of Corporate Governance Report

- Common issues on compliance of the Codes – cont'd:
  - A.4.3 - Serving more than 9 years could be relevant to the determination of a non-executive director's independence. If an independent non-executive director serves more than 9 years, his further appointment should be subject to a separate resolution to be approved by shareholders. The papers to shareholders accompanying that resolution should include the reasons why the board believes he is still independent and should be re-elected;
  - A.5.6 - The nomination committee (or the board) should have a policy concerning diversity of board members, and should disclose the policy or a summary of the policy in the corporate governance report;

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## Preparation of Corporate Governance Report

- Common issues on compliance of the Codes – cont'd:
  - B.1.5 - Issuers should disclose details of any remuneration payable to members of senior management by band in their annual reports;
  - C.1.2 - Management should provide all members of the board with monthly updates giving a balanced and understandable assessment of the issuer's performance, position and prospects in sufficient detail to enable the board as a whole and each director to discharge their duties under rule 3.0801 and chapter 13 (Main Board) or 5.01 and Chapter 17 (GEM Board);

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## Preparation of Corporate Governance Report

- Common issues on compliance of the Codes – cont'd:
  - C.2.1 - The directors should at least annually conduct a review of the effectiveness of the issuers' and its subsidiaries' internal control systems and report to shareholders that they have done so in their Corporate Governance Report. The review should cover all material controls, including financial, operational and compliance controls and risk management functions;
  - D.1.4 - Directors should clearly understand delegation arrangements in place. Issuers should have formal letters of appointment for directors setting out the key terms and conditions of their appointment; and

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## Preparation of Corporate Governance Report

- Common issues on compliance of the Codes – cont'd:
  - E.1.2 - The chairman of the board should attend the annual general meeting. He should also invite the chairmen of the audit, remuneration, nomination and any other committees (as appropriate) to attend.

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## Common issues on corporate governance in IPO and resumption of trading of listed shares

- PN21 / PN2:
  - Practice Note 21 (Main Board) – Due Diligence by Sponsors in respect of Initial Listing Applications; and
  - Practice Note 2 (Gem Board) – Due Diligence by Sponsors in respect of Initial Listing Applications.

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## Common issues on corporate governance in IPO and resumption of trading of listed shares

- Common issues:
  - Control environment – Code of conduct and employee handbook; and Board committees yet to be established;
  - Risk assessment – Formal risk management; and Budget & forecast;
  - Control activities – Policies and procedures yet to be established;
  - Information & communication – Succession plan and Whistling-blowing policy;
  - Monitoring – Internal audit.

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## Common issues on corporate governance in IPO and resumption of trading of listed shares

- Common issues – cont'd:
  - Financial reporting – Access of financial information and financial closing checklist;
  - Sales and receipt cycle – Credit control and pricing policy;
  - Procurement and payment cycle – Selection of suppliers and subsequent assessments;
  - Bank and cash cycle – Segregation of duties and variance analysis;
  - Inventory cycle – Documentation of stock movement and overhead allocation;
  - PPE – Register of assets and effective quotes; and
  - HR and payroll – Performance appraisal and training

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## Common issues on corporate governance in IPO and resumption of trading of listed shares

- Specific issues:
  - Use of personal bank accounts in the course of business is not in compliance with the PRC Company Law and affects the integrity, competence and suitability of the Directors;
  - Non-compliance with Hong Kong Companies Ordinance Section 111 and 122; and
  - Industry/business specific – patents, industry regulations and labour ordinance/laws, etc.

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## Future Development

- Environmental, Social and Governance (“ESG”) Reporting Guide (the “Guide”):
  - In January 2013, The Stock Exchange of Hong Kong Limited had issued Appendix 27 of the Listing Rules (Appendix 20 of the GEM Listing Rules) “the ESG Reporting Guide” which is expected to be adopted for annual report ending after 31 December 2012;
  - Subject to further consultations planned to be commenced in 2014, some recommended disclosures will be raised to the level of “comply or explain” by 2015; and
  - The Guide mentions that listed issuers may consider offering assurance on their ESG report.

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## Future Development

- Environmental, Social and Governance (“ESG”) Reporting Guide (the “Guide”) – cont’d:
  - General disclosure and key performance indicators (“KPIs”);
  - Four ESG subject areas: Workplace Quality, Environmental Protection, Operating Practices and Community Involvement.
  - Any examples?

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## Future Development

- Review of CG Reports of Listed Issuers:
  - Conducted by HKEx on the 1,083 CG reports issued by listcos with financial period from 1 April to 31 December 2012;
  - Determine the effectiveness of the Code's implementation;
  - 36 per cent of issuers complied with all the Code Provisions;
  - 97 per cent of issuers complied with 70 or more Code Provisions, out of 74;
  - 84 per cent of issuers complied with all the 30 new Code Provisions in the first eight months of their implementation;

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## Future Development

- Review of CG Reports of Listed Issuers – cont'd:
  - 43 per cent of issuers complied with all the 44 Code Provisions that have been in the previous version of the Code. This compared favourably with the 2009 review when 39 per cent of the issuers fully complied under the same Code Provisions. This compliance rate also compared favourably with the findings of all previous reviews; and

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## Future Development

- Review of CG Reports of Listed Issuers – cont'd:
  - “Our latest review shows that issuers have embraced the changes to the Code and have achieved a high rate of compliance. **This is a positive sign that issuers recognise the importance of corporate governance and are more ready to adopt a higher standard of governance**” said David Graham, HKEx's Chief Regulatory Officer and Head of Listing.
  - [http://www.hkex.com.hk/eng/rulesreg/listrules/listpresent/Documents/listcomup\\_201309.pdf](http://www.hkex.com.hk/eng/rulesreg/listrules/listpresent/Documents/listcomup_201309.pdf)

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Q&A  
Section?

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