

April 2024

Unveiling best practices: Exchange's evaluation of issuers' corporate governance frameworks



Introduction

The Stock Exchange of Hong Kong Limited (the "**Exchange**") published the findings of its latest review of issuers' corporate governance practices (the "**Review**") on 17 November 2023. The Review provides guidance to issuers on the improvements they could make to their corporate governance ("**CG**") practices. It focuses, in particular, on compliance with the new requirements introduced to the Corporate Governance Code in 2022. The Review marks a significant stride towards promoting exemplary governance.

Background

The Exchange amended the Corporate Governance Code ("**CG Code**") on 1 January 2022, and the requirements under the new CG Code will apply to CG reports for the financial year commencing on or after 1 January 2022 (the "**CG Update**"). The CG Update provides guidance to issuers on the improvements they could make to their corporate governance practices, with changes highlighting the importance of corporate culture aligning with the company's purpose, values and strategy. The Review analyses the CG reports of 400 randomly selected issuers ("**Sample Issuers**") for the 2022 financial year and reports on their compliance with the new requirements introduced in the CG Update.

Key findings and recommendations from the Review

Aspects	Reports of Sample Issuers	Suggestions
Corporate culture	All of the Sample Issuers reported compliance with the code provision (" CP ") on corporate culture. However, they did not always include detailed disclosure on their desired corporate culture in their CG Reports.	Comprehensive disclosure should include (among other things) details on: (i) the link between corporate culture and the issuer's business objectives; (ii) the implementation of the desired corporate culture into the issuer's daily operations; and (iii) an assessment of the progress and success of such implementation. Good disclosure on corporate culture should also avoid generic disclosure or overly narrow focus on corporate governance. Where such disclosures are made outside of the CG Report (for example in the Chairman's Statement), it is suggested that issuers provide appropriate cross references in the CG Report.
Long serving independent non-executive directors (" INEDs ")	The CG Update has resulted in a meaningful reduction of boards whose INEDs consisted of all long serving INEDs. All of the relevant Sample Issuers that retained long serving INEDs disclosed the factors they considered in determining the INED's suitability for re-election.	Board composition should be regularly assessed in line with changes to an issuer's business environment and other challenges. The Exchange believes that periodic board refreshment, in particular the appointment of new INEDs, can foster the sharing of diverse perspectives. Where a long serving INED is retained, sufficient details should be disclosed regarding the suitability of such individual for re-election, including the process undertaken by the nomination committee and the board to confirm his / her continued independence.
Diversity	Since the CG Update, the percentage of single gender board issuers has dropped by 8%.	Existing single gender board issuers (around 550 issuers) should proactively seek to appoint at least one director of a different gender by the deadline of 31 December 2024. It is important that board composition reflects a suitable balance of skills, experience and diversity of perspectives. It is recommended that issuers: (i) disclose numerical targets and timelines for achieving board gender diversity; and

Aspects	Reports of Sample Issuers	Suggestions
		(ii) formulate long-term targets and timelines to further progress gender diversity on their boards beyond the required minimum and within their wider workforce.
Risk management and internal controls	All of the Sample Issuers disclosed information on their risk management and internal controls and a large majority confirmed that their existing systems are effective.	Conducting appropriate risk assessment and implementing internal controls that help manage such risks is key to good corporate governance. It is equally important to regularly monitor the internal controls in place and review their effectiveness at least annually. CP Reports should include sufficient details on the issuers' internal control review to support their findings that the internal controls remain effective, such as: (i) the structure and processes of the Internal Control Systems and their responsible persons or departments; (ii) particular principal or emerging risks, including fraud and/or ESG related risks; and (iii) the process for regular monitoring and reviews.
Other observations	The Exchange observed a high level of compliance with the mandatory disclosure requirements (" MDRs ") and CPs of the CG Code, consistent with the findings of their previous reviews.	Issuers should ensure they understand the disclosure requirements for all MDRs, (including the sub-paragraphs of relevant MDRs), and make disclosure accordingly in their CG Reports. If issuers determine that any of the MDRs is not applicable to them, they should state the same in their disclosures.

Key takeaways

Delivering effective corporate governance practices is more than a box-ticking exercise and requires careful consideration. Listed issuers should familiarize themselves with the amended rules and ensure compliance with the new requirements, particularly regarding disclosures on corporate culture, long serving INEDs, diversity disclosure requirements and risk management and internal controls. The Exchange has noted the importance of high quality reporting in the Review, remarking that high quality reporting helps differentiate the approach that companies take and provides confidence to the market. The Exchange is conducting a review of its corporate governance framework and is expecting to put forward proposals for a public consultation in due course.

Contact us



Michelle Chung

Partner
T: +852 3166 6927
E: michelle.chung@shlegal.com



Angela Ng

Associate
T: +852 25332706
E: angela.ng@shlegal.com

Stephenson Harwood is a law firm of over 1300 people worldwide, including 200 partners. Our people are committed to achieving the goals of our clients – listed and private companies, institutions and individuals.

We assemble teams of bright thinkers to match our clients' needs and give the right advice from the right person at the right time. Dedicating the highest calibre of legal talent to overcome the most complex issues, we deliver pragmatic, expert advice that is set squarely in the real world.

Our headquarters are in London, with eight offices across Asia, Europe and the Middle East. In addition, we have forged close ties with other high quality law firms. This diverse mix of expertise and culture results in a combination of deep local insight and the capability to provide a seamless international service.

© Stephenson Harwood 2024. Any references to Stephenson Harwood in this communication means Stephenson Harwood and/or its affiliated undertakings. Any reference to a partner is used to refer to a partner of Stephenson Harwood or a partner of Wei Tu Law Firm. The association between Stephenson Harwood and Wei Tu Law Firm is not in the form of a partnership or a legal person.

Full details of Stephenson Harwood LLP and its affiliated undertakings can be found at www.shlegal.com/legal-notices.

Information contained in this briefing is current as at the date of first publication and is for general information only. It is not intended to provide legal advice.

Unless you have consented to receiving marketing messages in relation to services of interest to you in your personal capacity, the services marketed in this message are offered only to the business for which you work.

**STEPHENSON
HARWOOD**
WEI TU CHINA ASSOCIATION
罗夏信-伟途 联营