

HKIRA Investor Relations Symposium – ESG and Beyond

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Draft opening address by Guest of Honour

Dr Kelvin Wong, SBS, JP, Chairman, AFRC

Eva (Dr Eva Chan, Chairman, HKIRA), distinguished guests, ladies and gentlemen,

It is my honour and privilege to join you today at this Symposium with the theme “ESG and Beyond”.

In recent years, we have witnessed the leaping momentum of Hong Kong in developing itself into a green and sustainable financial hub. A raft of initiatives have been launched by the Government, for example, the issuance of green bonds, the establishment of the Green and Sustainable Finance Cross-Agency Steering Group and the Green and Sustainable Finance Grant Scheme. More recently, we have seen the launch of Core Climate (Hong Kong’s new international carbon marketplace) by the HKEX on 24 November. In the business sector, corporates have been taking a proactive approach to setting and fulfilling their ESG targets, aiming at creating business growth values and projecting a socially responsible profile to investors.

To support this green vision, the AFRC established the Sustainability and Climate Action Task Force (SCATF) in February 2022. The purpose of the SCATF is to provide high-level recommendations to the AFRC Board on strategic actions that should be considered in relation to global developments in financial and sustainability reporting. This should include a Climate Change Action Roadmap for the AFRC that is aligned with Hong Kong’s Climate Action Plan 2050.

ESG is certainly opening up ample opportunities for businesses and capital markets. Yet, let us not be overwhelmed by the rosy prospects and forget to look beyond the acronym, to think more deeply and broadly about other ESG-related issues. These issues include (i) greenwashing (ii) roles and responsibilities of the Board, auditors and audit committees and (iii) investor education. I will briefly touch on these three issues today.

Greenwashing

Considering the commercial benefits of ESG, such as tax incentives, creating customer loyalty and investment value, cost of capital and gaining a positive corporate image, corporates are keen to ride on the bandwagon and make efforts on formulating strategies to achieve their ESG goals. But let’s face the music, dishonesty is out there. Some irresponsible corporates may just want to wear the green halo of ESG but do nothing or only do the minimal. Some even use measurement and disclosure tricks to deceive customers and investors. From fashion, food, and furniture to car manufacturing, we have heard many greenwashing stories around the world. The results of greenwashing are: misrepresentation, misselling and mispricing, creating false expectations and harming those investors who put their money in based on impression rather than information.

Why is greenwashing possible? Because there are opportunities for fraud (The Fraud Triangle). And why there are opportunities for fraud? Because there is no unified framework or global standards in ESG reporting at the moment. To make matter worse, there are no mandatory regulatory requirements imposed on the issuers on the form and who to provide assurance for sustainability reports.

Some statistics here. According to a survey by the International Federation of Accountants (IFAC) conducted in 2021 (on reports for the financial year 2019) and 2022 (on reports for the financial year 2020):

- Slightly more than 30% of the samples in Hong Kong obtained assurance on their ESG information in the 2022 Survey (world average: 58%).
- Less than 30% of these assurance engagements in Hong Kong were conducted by an audit firm in the 2022 Survey (world average: 61%).

Based on a brief ESG assurance research exercise conducted by the HKICPA covering all the December year-end listed companies for 2020, only 85 out of 1,900 (4.5%) companies obtained external assurance. Most of them were limited assurance engagements.

With a lower-than-world average ratio of ESG information receiving assurance, and with most being limited assurance engagements, the credibility of ESG information of the listed entities remains dubious.

The silver lining is, the International Sustainability Standards Board (ISSB) is establishing sustainability-related disclosure standards constituting a comprehensive global baseline. In respect of standard setting, the AFRC has an oversight role over the HKICPA. We will ensure that the HKICPA will take into consideration the latest international standards and best practice when setting the relevant sustainability standards for Hong Kong.

Roles and responsibilities: Board, Auditors and Audit Committee

To ensure transparent and reliable ESG disclosures and to counter greenwashing, the Board, auditors and audit committees all have their critical roles to play.

Companies need to have a governance structure in place for the preparation of ESG-related information in financial reporting such that the information presented is readable and reliable for investors' decision-making.

Compared with the more mature markets in Europe and the U.S., Hong Kong is only at the initial stage of its development of ESG reporting. Certain companies currently lack mature systems, processes and internal controls to accurately collect and report the required sustainability information. It is the Board's role to ensure that the appropriate resources, infrastructure, processes, systems, targets and data are in place for the disclosure of such information.

Having a strong foundation for collecting ESG data means that the company's external reporting will become more useful to investors and other stakeholders. The alignment of financial and non-financial reporting is essential to achieve a holistic view of the

company through its reporting. This will in turn allow investors and other stakeholders to better analyse the risks and opportunities for a company.

The Board should oversee an evaluation process to assess how the relevant data enhances the sustainable performance of the organisation in the long run. Whilst the short-term costs to properly collect and validate sustainability data may be high, in the long run this could save a significant amount of money for the organisation and have a positive impact on financial performance.

Audit committees are expected to engage with the management, including internal audit, fraud risk specialists, and independent auditors to understand the extent to which greenwashing risk is being considered and mitigated.

As auditors are at the downstream of the process to ensure the quality of financial and sustainability reporting (and identify greenwashing), they should have adequate knowledge to understand the infrastructure of an organisation that puts its ESG efforts together, and specifically, how ESG data is collected. They should also be able to identify and understand the business and financial impact arising from ESG factors when auditing financial statements. Auditors' ability to assess the climate-related risks and detect any material misstatements in the financial statements of audited entities plays a key role in protecting the interests of investors.

Investor education

It is important that all parties involved in the ESG reporting/investing ecosystem undertake efforts to ensure that the end investors have a good understanding of the sustainability features of the assets or products they invest in. Investors are encouraged to develop their ability in understanding the financial and non-financial information and implications in relation to ESG initiatives for making informed investment decisions. Self-protection is always better than seeking protection from others, and it starts with financial literacy. In this respect, I would like to commend the work of the HKIRA which has dedicated itself to promoting excellence in the investor relations profession in Hong Kong. It has also run many education and training programmes to promote financial literacy and professional competence in the financial industry.

The above are my thoughts on the three issues and hopefully, they would serve as a stimulus for further discussion around the theme today. As a closing note, I wish the HKIRA great success in today's symposium. Thank you.