AFRC Accounting and Financial Reporting Council 會計及財務匯報局

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Understanding the Baseline – Analysing the Market Readiness for Sustainability Reporting and Assurance in Hong Kong

Policy, Registration and Oversight

January 2025

About the Accounting and Financial Reporting Council

The Accounting and Financial Reporting Council (AFRC) is an independent body established under the Accounting and Financial Reporting Council Ordinance. As an independent regulator, the AFRC spearheads and leads the accounting profession to constantly raise the level of quality of professional accountants, and thus protects the public interest and promotes the healthy development of the accounting profession.

For more information about the statutory functions of the AFRC, please visit www.afrc.org.hk.

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Executive summary

1. This study aims to **provide the AFRC and stakeholders with a comprehensive understanding of current sustainability reporting and assurance practices in Hong Kong**. The findings will guide the development of a sustainability assurance regulatory framework and encourage audit firms to better integrate climate-related risks into financial audits.

2. The study comprises two parts:

    a. **An analysis** of the sustainability assurance practices among 82 constituent listed entities in the Hang Seng Index (**HSI**); and

    b. **Two surveys conducted** on public interest entity[1] (**PIE**) auditors and listed entities in Hong Kong. For the surveys, we received an 89.3%[2] (or 75 responses) response rate from active PIE auditors[3] and a 30.6% response rate (or 797 responses) from listed entities.

3. The key observations are summarised below.

Listed entities' readiness to prepare robust climate reporting

4. **Nearly all listed entities have assessed their climate-related risks, which is a critical step towards managing and reporting on them.** Over one-third of listed entities surveyed considered themselves moderately or highly exposed to the physical impacts of climate change (37%) and to risks arising from the transition to a lower-carbon economy (40%).

5. **4% and 7% of respondents have yet to assess their physical and transition risks, respectively, including 14% in the climate-sensitive materials sector.** By evaluating their exposure, those in climate-sensitive

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[1] A PIE means a listed corporation of which its listed securities comprise at least shares or stocks, or a listed collective investment scheme as defined in section 3(1) of the Accounting and Financial Reporting Council Ordinance (Cap. 588).

[2] The response rate was 100% (or 51) from active local PIE auditors.

[3] Active PIE auditors refer to those with at least one PIE audit engagement. As of 30 April 2024, they comprised 51 local firms, seven from Mainland China and 17 from overseas.

industries can transform their business models and enhance their long-term financial sustainability.

6. **Over half (53%) of the listed entity respondents are gearing up for robust sustainability reporting.** On the other hand, 47% of respondents need to invest more in data and technology, internal controls, systems and governance, and financial and human resources. Among 39% of respondents who considered themselves moderately or highly exposed to climate-related risks, about half (48% to 55%) are ready in all three components.

> **When it comes to the climate, awareness is bliss.** Entities that proactively identify impacts of climate change at an early stage are also better equipped to manage the risks and reap the opportunities effectively.

7. **Large-cap entities are more likely to assign oversight of sustainability reporting to their sustainability committees than Small-cap entities.** 54% of 278 Large-cap respondents did so, compared with 24% of 266 Small-cap respondents.[4] On the other hand, 57% of Small-cap respondents assigned oversight to audit committees, as compared to 28% of Large-cap respondents.

> **The Board, audit committee, and sustainability committee each bear a noble role in the realm of sustainability reporting.**
>
> - The Board, with their wisdom and foresight, provides the overarching strategy, evaluating trade-offs if any, towards a sustainable future.
> - The audit committee, with vigilant eyes, ensures that their reporting ascends to the required standards.
> - The sustainability committee, with steadfast resolve, drives the decarbonisation journey.

[4] Please refer to the Glossary for definitions of Large-cap, Mid-cap and Small-cap listed entities.

8. **Insufficient human resources and expertise are the most pressing organisational challenge in preparing climate reporting (65%)**. This is followed by a lack of understanding among external stakeholders (41%), and a lack of organisational support (36%).

9. **In-house accountants could be better leveraged for sustainability reporting.** 46% of listed entities surveyed involved in-house accountants across all reporting functions. The most cited benefit from involving in-house accountants is to bridge financial and climate reporting (63%). A minority (13%) did not involve their in-house accountants.

Listed entities' considerations on whether to obtain sustainability assurance

10. **Listed entities are increasingly seeking sustainability assurance.** The number of HSI listed entities who have published assurance reports has grown from 51% in 2023 to 65% in 2024. The increase can be attributed to respondents' perception that obtaining assurance could boost investors' confidence (51%), elevate environmental, social, and governance (**ESG**) ratings (51%), and enhance brand reputation (49%).

11. **However, the uptake of voluntary sustainability assurance is less prevalent among smaller listed entities.** Among 682 valid responses[5], 34% of 229 Small-cap entities obtained assurance, as compared to 45% of 233 Large-cap entities. The high costs and voluntary nature of assurance often deter smaller listed entities from pursuing it.

> **Independent assurance, like a steadfast beacon, can aid directors in the faithful discharge of their statutory duties.** Assurance can be a valuable tool for directors, particularly those who are growing their expertise in sustainability reporting.

12. From disclosures being assured to assurance standards applied, **the Hong Kong market displays a wide range of assurance practices**. The plethora

[5] The study excluded 115 responses where surveyed listed entities reported that their financial auditors or other CPA firms had provided reasonable or high levels of assurance on their sustainability disclosures. Further enquiries revealed that these respondents mistakenly believed their disclosures were covered within audits of financial statements.

of different practices may confuse investors and other stakeholders, highlighting the importance of developing the sustainability assurance framework by the AFRC.

a. In 2024, 53% of HSI entities published assurance reports on direct greenhouse gas emissions, and 34% on their indirect value chain emissions. On the other hand, **38% of HSI constituents obtained assurance for their entire sustainability reports**.

b. Over half (53% of 53) HSI constituents with assurance **obtained limited assurance,** as compared to 21% that obtained reasonable assurance and 7% that obtained different levels of assurance for different disclosures. The remaining 19% obtained high or moderate levels of assurance based on AccountAbility[6] 1000 assurance standard (**AA1000AS**).

c. Standards issued by the International Auditing and Assurance Standards Board (**IAASB**) were used frequently, **particularly the International Standard on Assurance Engagements (ISAE) 3000[7] or its equivalent** (70%). Other assurance engagements used were AA1000AS (21%), ISAE 3410[8] (19%), and International Organization for Standardization (**ISO**) 14064-3[9] standard (15%).

Diverse assurance practices will likely sow seeds of confusion among investors. Retail investors, in particular, may lack the technical expertise to discern the disclosures being assured or levels of assurance obtained.

13. The sustainability assurance market is served by Certified Public Accountant (**CPA**) and non-CPA firms, with **non-CPA firms having increased their market share recently.**

[6] AccountAbility is a global advisory and standards firm that serves business, investors, governments, and multi-lateral organisations.

[7] ISAE 3000 *Assurance Engagements Other than Audits or Reviews of Historical Financial Information*.

[8] ISAE 3410 *Assurance Engagements on Greenhouse Gas Statements*.

[9] ISO 14064-3 *Greenhouse gases — Part 3: Specification with guidance for the verification and validation of greenhouse gas statements*.

a. In 2024, over half (53% of 53) HSI constituents with published sustainability assurance reports had **engaged non-CPA firms to conduct the assurance**, up from 40% in 2023. Meanwhile, 40% engaged CPA firms, and 7% engaged both CPA and non-CPA firms;

b. Non-CPA firms also conducted a higher proportion of assurance among Small-cap respondents (73% of 77) compared to that of Large-cap respondents (60% of 104);

c. Not surprisingly, among 263[10] listed entities surveyed that had obtained sustainability assurance:

   i. **Two-thirds (66%) engaged non-CPA firms**. The remaining engaged CPA firms (17%) or both CPA and non-CPA firms (17%); and

   ii. The non-CPA firms were primarily hired for their industry knowledge (51%), ESG expertise (49%), prior experience (40%) and cost considerations (38%).

PIE auditors' readiness to provide sustainability assurance

14. **As of May 2024, ten PIE auditors had delivered sustainability assurance services.** These firms were larger firms and most (88%) belonged to a global network. **These PIE auditors provided limited assurance.**

15. **For those with sustainability assurance engagements, the future appears promising.** All 10 PIE auditors planned to expand their sustainability service practice. To support the business growth, their sustainability teams were composed as follows:

a. Most teams included accountants with ESG qualifications (nine PIE auditors), along with accountants without ESG qualifications (seven); and

b. Half (five)[11] employed non-accountant ESG specialists.

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[10] 263 valid responses were received from Large-cap (104), Mid-cap (82), and Small-cap entities (77).
[11] This included the only firm that did not use accountants with ESG qualifications.

16. **Notably, over one-third of the 75 active PIE auditors now offer sustainability assurance services.** This expansion opens new revenue streams and market opportunities. By demonstrating a commitment to ESG, these firms strengthen their reputation and better able to attract young talents to the profession.

> **Seize the opportunity, embrace the growth.** By seizing this opportunity, firms can position themselves as leaders in the evolving landscape of sustainability assurance. This strategic move will not only broaden their suite of assurance services, but also drive long-term success of the audit profession.

PIE auditors' practices to integrate climate considerations in financial audits

17. **Auditors are required to assess the financial impact of climate-related risks when auditing financial statements.**

18. **Category A auditors,[12] who serve clients in climate-sensitive industries, are leading the way in addressing climate-related risks in financial audits.**

    a. All Category A PIE auditors provided ESG training.

    b. Most (80%) of them involved ESG specialists in financial audits; and

    c. Around two-thirds (60% to 80%) of Category A PIE auditors had access to relevant firm-level and engagement-level internal resources and support.

> **When embarking upon uncharted seas, it's vital to possess knowledge, compass, and a map to illuminate the journey's quest.** Providing ESG training and technical guidance, supported by ESG experts, is an effective way to build ESG-competent financial audit teams.

19. PIE auditors cited a lack of guidelines (65% of 75), difficulty in quantifying the financial impact of climate-related risks (56%), and limited expertise

[12] Category A PIE auditors have more than 100 PIE audit engagements.

on climate-related issues among audit partners and staff (52%) as their **biggest challenges to assess and address climate-related risks** in financial audits.

> **With resources at their fingertips, auditors can face these emerging challenges head-on.** Guidance issued by standard setters include the IAASB's Staff Audit Practice Alert [13], International Financial Reporting Standards (**IFRS**)'s educational material[14] and webcast series[15] and Hong Kong Institute of Certified Public Accountants (**HKICPA**)'s Sustainability Information Centre.[16]

20. Listed entities consider auditors' climate-related expertise alongside other topics such as cybersecurity in auditor selection. There is an opportunity for listed entities in climate-sensitive industries to prioritise auditors' climate-related expertise, with over 40% of them ranking them fourth or fifth in importance among five areas.

> **The road to enlightenment begins with awareness and education.** Financial auditors have a role to educate their clients on the impact of climate change on financial reporting, and by extension, their audits.

Conclusion

21. The analysis reveals significant insights into the readiness and challenges faced by listed entities and PIE auditors in preparing robust climate reporting.

    a. For listed entities, the study shows that listed entities are taking steps towards robust sustainability reporting. Increasingly, they are

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[13] IAASB (2020) *Staff Audit Practice Alert - The Consideration of Climate-Related Risks in an Audit of Financial Statement*.

[14] IFRS (Republished 2023) *Educational material - Effects of climate-related matters on financial statements*.

[15] IFRS (2024) *Webcasts - Connectivity between the financial statements and sustainability-related financial disclosures*.

[16] HKICPA (2024) *Sustainability Information Centre*.

seeking sustainability assurance to bolster investor confidence and enhance their ESG ratings. The most pressing issue cited by listed entities was the lack of sufficient in-house expertise. With their keen analytical skills and business acumen, accountants are well suited for contributing to climate reporting, and listed entities need to leverage them better.

b. Sustainability assurance is a once-in-a-generation opportunity for the accounting profession. To capitalise on the opportunity, CPA firms should strategically invest in staff training and targeted recruitment, positioning themselves at the forefront of this field.

22. Embracing sustainability practices can significantly enhance Hong Kong's reputation as a trusted international financial centre (**IFC**). By demonstrating a commitment to transparency and accountability in sustainability reporting, Hong Kong can attract global investors who integrate sustainability factors in their investments. This will not only strengthen the city's financial sector but also position it as a leader in sustainable finance, driving long-term economic growth and resilience.

Appreciation

23. We would like to express our appreciation to the Hong Kong Exchanges and Clearing Limited (**HKEX**) and the following professional bodies (in alphabetical order) for their support in promoting our surveys: the Hong Kong Chartered Governance Institute; the HKICPA; the Hong Kong Independent Non-Executive Director Association; and the Hong Kong Institute of Directors. Lastly, we are grateful to the respondents for participating in the survey and providing valuable insights.

Section A: Introduction

1. Global action to combat climate change

1.1. **Climate change, driven by human activities like deforestation and fossil fuel burning, is a critical challenge of our time.** The increase in Greenhouse Gases (**GHG**) leads to global warming, extreme weather, and rising sea levels, threatening ecosystems and communities. Urgent action is needed to reduce emissions, adopt renewable energy, and implement sustainable practices to protect our environment for future generations.

1.2. **Sustainable finance has emerged as a powerful force in driving the global response to this challenge.** Investor enthusiasm remained strong, with US$30.3 trillion invested globally in sustainable investing assets.[17]

1.3. A 2023 survey revealed that 54% of investors planned to increase their sustainable investments in the coming year.[18] Sustainable debt issuance grew as well, with green, social, sustainable, and sustainable-linked bonds recording a cumulative volume of US$4.4 trillion at the end of 2023.[19]

Creation of international reporting and assurance standards

1.4. To meet increasing calls for companies to provide high-quality, globally comparable information on sustainability-related risks and opportunities, **the IFRS Foundation established the International Sustainability Standards Board (ISSB) in November 2021**. The ISSB aims to create a global baseline framework for sustainability reporting focused on the information needs of investors and capital markets.

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[17] Global Sustainable Investing Alliance (2023) *Global Sustainable Investment Review 2022*. The data covered sustainable investment in United States, Canada, Europe, Japan, Australia, and New Zealand.

[18] Morgan Stanley (2024) *Sustainable Signals Understanding Individual Investors' Interests and Priorities*. The survey was conducted across 2,820 individual investors across US, Europe, and Japan with investable assets greater than US$100,000.

[19] Climate Bonds Initiative (2024) *Sustainable Debt Global State of the Market 2023*.

1.5. In June 2023, the ISSB published its inaugural set of the IFRS Sustainability Disclosure Standards, namely the IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and IFRS S2 *Climate-related Disclosures* (collectively, **the ISSB Standards**). These standards were endorsed by the International Organization of Securities Commissions in July 2023 as appropriate to serve as a global framework for capital markets.

1.6. As of September 2024, **30 jurisdictions have decided to use or are taking steps to introduce the ISSB Standards into their legal or regulatory frameworks**. Collectively, they represented about 57% of global gross domestic product, over 40% of global market capitalisation, and over half of global GHG emissions.[20]

1.7. To ensure that disclosures are trustworthy, **sustainability reports should be rigorously assured using international auditing standards**:

a. In November 2024, the IAASB issued the International Standard on Sustainability Assurance (**ISSA**) 5000 *General Requirements for Sustainability Assurance Engagements*; and

b. In December 2024, the International Ethics Standards Board for Accountants approved the International Ethics Standards for Sustainability Assurance (including International Independence Standards).

1.8. Both standards are profession-agnostic, meaning they can be used by assurance practitioners regardless of their professional background. This will ensure that sustainability assurance is executed using consistent principles, upholding the quality and credibility of the opinions rendered.

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[20] IFRS Foundation (2024) *Progress on Corporate Climate-related Disclosures—2024 Report*.

2. Hong Kong's vision statement

2.1. As an international financial centre, **Hong Kong must build on its strengths and advance its role in sustainable finance**. Accurate, reliable, and comparable sustainability information for informed investment decisions is paramount to supporting this advancement.

2.2. In March 2024, the Financial Services and the Treasury Bureau (**FSTB**) of the Hong Kong Special Administrative Region (**HKSAR**) Government issued a Statement, setting out **the vision for Hong Kong** to be among the first jurisdictions to align the local sustainability requirements with the ISSB Standards.[21] The vision was reiterated in the Chief Executive's Policy Address in October 2024.[22]

2.3. In December 2024, the HKSAR Government published the Roadmap on Sustainability Disclosures in Hong Kong (**Roadmap**) to achieve the vision (Figure 1). The roadmap includes providing a well-defined pathway for large **publicly accountable entities (PAEs) to adopt the ISSB Standards no later than 2028**. Large PAEs comprise Large Cap issuers[23] and large non-listed financial institutions carrying a significant weight in Hong Kong.

2.4. As mentioned in the Roadmap, **the AFRC is designated the role to develop the proposed regulatory framework for sustainability assurance,** including the registration of assurance providers, the implementation of sustainability assurance and ethics standards, and the establishment of the related regulatory regime. The framework will be issued for public consultation in 2025.

[21] The Financial Services and the Treasury Bureau (2024) *Vision Statement on Turning Obligations into Opportunities in Developing the Sustainability Disclosure Ecosystem in Hong Kong*.

[22] The Government of the HKSAR (2024) *The Chief Executive's 2024 Policy Address*.

[23] For the purpose of the Roadmap, Large Cap Issuers is defined as issuers that are Hang Seng Composite LargeCap Index constituents.

Figure 1: Roadmap on sustainability disclosure in Hong Kong

Source: The Government of the HKSAR (2024) *Roadmap on Sustainability Disclosure in Hong Kong: Ambition · Assurance · Enablement*

AFRC's development of a sustainability assurance framework

2.5. At the AFRC, we believe that robust sustainability reporting and assurance, combined with high-quality financial audits that integrate climate-related risks, enhance stakeholders' confidence in Hong Kong listed entities. This confidence is crucial for reinforcing Hong Kong's position as an IFC and the world's sustainable finance hub.

2.6. In January 2024, we were invited to join the Green and Sustainable Finance Cross-Agency Steering Group (**CASG**).[24] The CASG was formed to

[24] The CASG is co-chaired by the Hong Kong Monetary Authority and the Securities and Futures Commission. Members include the FSTB, the Environment and Ecology Bureau, the Hong Kong Exchanges and Clearing Limited, the Insurance Authority, the Mandatory Provident Fund Schemes Authority, and the AFRC.

coordinate the management of climate and environmental risks to the financial sector, accelerating the growth of green and sustainable finance in Hong Kong, and supporting the HKSAR Government's climate strategies.[25]

2.7. In February 2022, we established the Sustainability and Climate Action Task Force (**SCATF**).[26] The purpose of the SCATF is to provide high-level recommendations to the AFRC on strategic actions related to global developments in financial and sustainability reporting. The recommendations included conducting this study on the current practices in Hong Kong.

3. About this study

3.1. **The objective of this study is to highlight the current practices in Hong Kong** in respect of sustainability reporting and assurance, and the integration of climate considerations in financial audits. The findings will assist the AFRC and our stakeholders in developing a robust regulatory framework for sustainability assurance, and highlighting the progress in integrating climate-related considerations in financial audits.

3.2. This study covers four focus areas:

a. The readiness of listed entities to prepare climate reporting in accordance with the ISSB Standards (**Section B**);

b. The considerations applied by listed entities when deciding whether to obtain independent sustainability assurance or not (**Section C**);

c. The readiness of PIE auditors to provide robust sustainability assurance (**Section D**); and

d. The practices of PIE auditors with respect to integrating climate risks in financial audits (**Section E**).

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[25] FSTB (2024) *Vision Statement on Turning Obligations into Opportunities in Developing the Sustainability Disclosure Ecosystem in Hong Kong.*

[26] The SCATF comprises experts representing key stakeholders from institutional investors, industry associations, professional institutions, listed entities and auditing professionals.

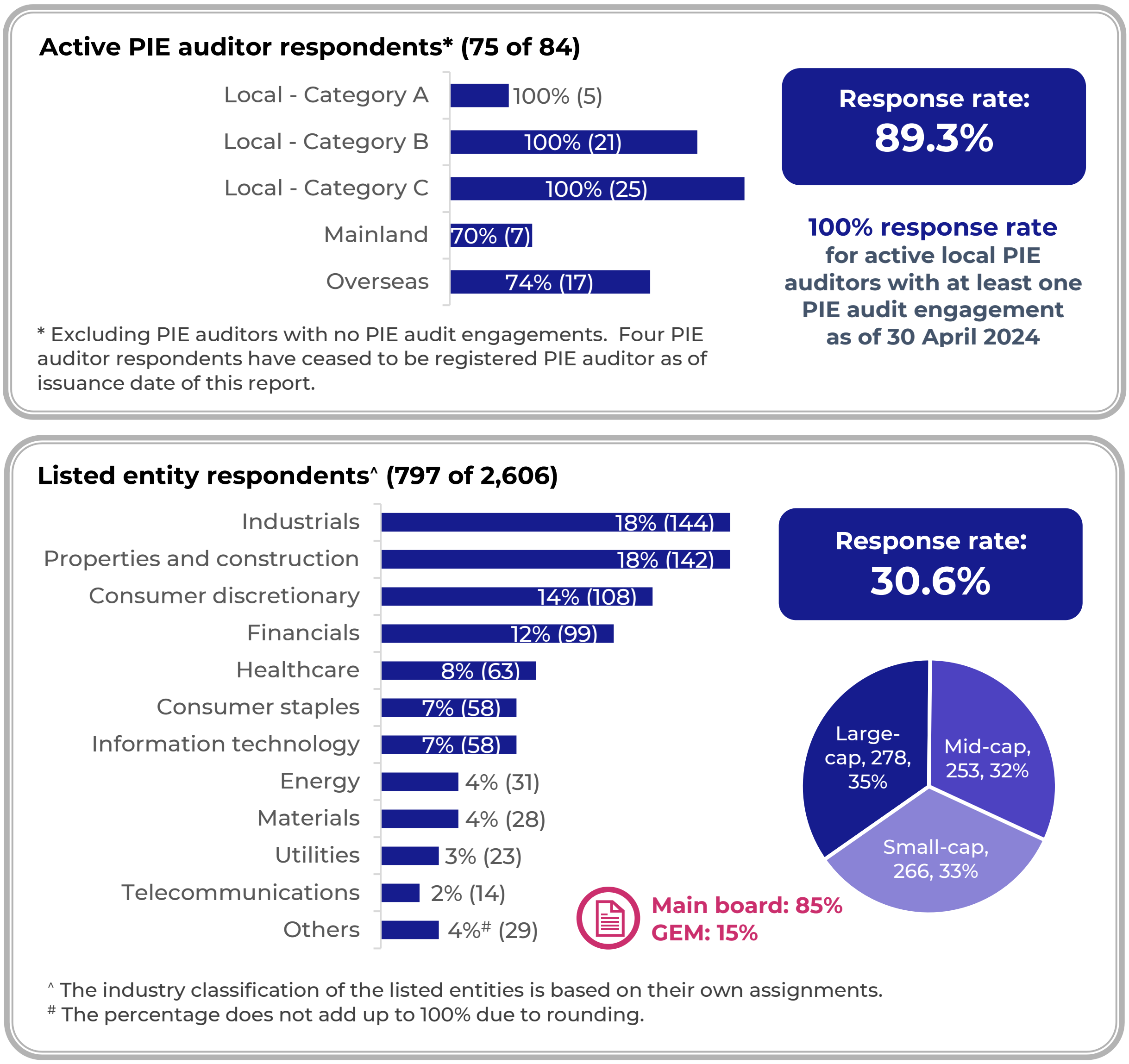
3.3. This study was conducted in two parts:

a. **An analysis** of sustainability assurance obtained by 82 HSI constituents; and

b. **Two surveys** were carried out from 6 to 23 May 2024 on PIE auditors[27] and listed entities in relation to their practices and plans for sustainability reporting and assurance.

[27] A PIE auditor means (a) **a registered PIE auditor**, i.e. a practice unit registered under Division 2 of Part 3 of the Accounting and Financial Reporting Council Ordinance, or (b) **a recognized PIE auditor**, i.e. an overseas auditor recognized under Division 3 of Part 3, including a Mainland auditor recognized under section 20ZT of the Accounting and Financial Reporting Council Ordinance.

Figure 2: Profile of survey respondents



Caution is needed in drawing conclusions about the findings:

a. As the surveys were voluntary, listed entities that responded to the survey were self-selected;

b. 65% of responses from the listed entities were anonymous, for which we were unable to clarify ambiguities and inconsistencies; and

c. For the remaining 35% that provided their identities, we confirmed no duplicated response from the same company. However, we had not performed verification of their survey responses.

Section B: Readiness of listed entities to prepare robust climate reporting

4. Sustainability reporting requirements in Hong Kong

4.1. **Since 2013, listed entities in Hong Kong are subject to some form of sustainability reporting requirements**. What started as a voluntary guide was amended several times into mandatory requirements.

4.2. At the time of undertaking this study, listed entities were required to make governance disclosures on a mandatory basis, and to make environmental and social disclosures on a "comply or explain" basis. **As of November 2024, over 91% of 2,489 listed entities have either complied or explained on all aspects, except for labour standards**.[28]

4.3. In April 2024, the HKEX concluded its public consultation. Listed entities will be required to make enhanced climate-related disclosures (**CRD**) as follows:[29]

a. **All listed entities** will be required to disclose Scope 1 and Scope 2 GHG emissions on **a mandatory basis, effectively from 1 January 2025**;

b. **All Main Board issuers** will be required to further disclose other CRD modelled on IFRS S2 *Climate-related Disclosures* on **a "comply or explain" basis, effectively from 1 January 2025**;[30] and

c. **Large constituents of the Hang Seng Composite Index will be required** to further disclose other CRD on a **mandatory basis, effectively from 1 January 2026**.

[28] HKEX (2024) *Analysis of the ESG Practice Disclosure.*

[29] HKEX (2024) *Consultation Conclusions Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework*

[30] These requirements are active at the time of this study publication.

Full convergence with the ISSB Standards

4.4. When developing the Roadmap, the CASG considered Hong Kong's overall business and financial market composition, and the public accountability and the weight of entities in relation to the economy.

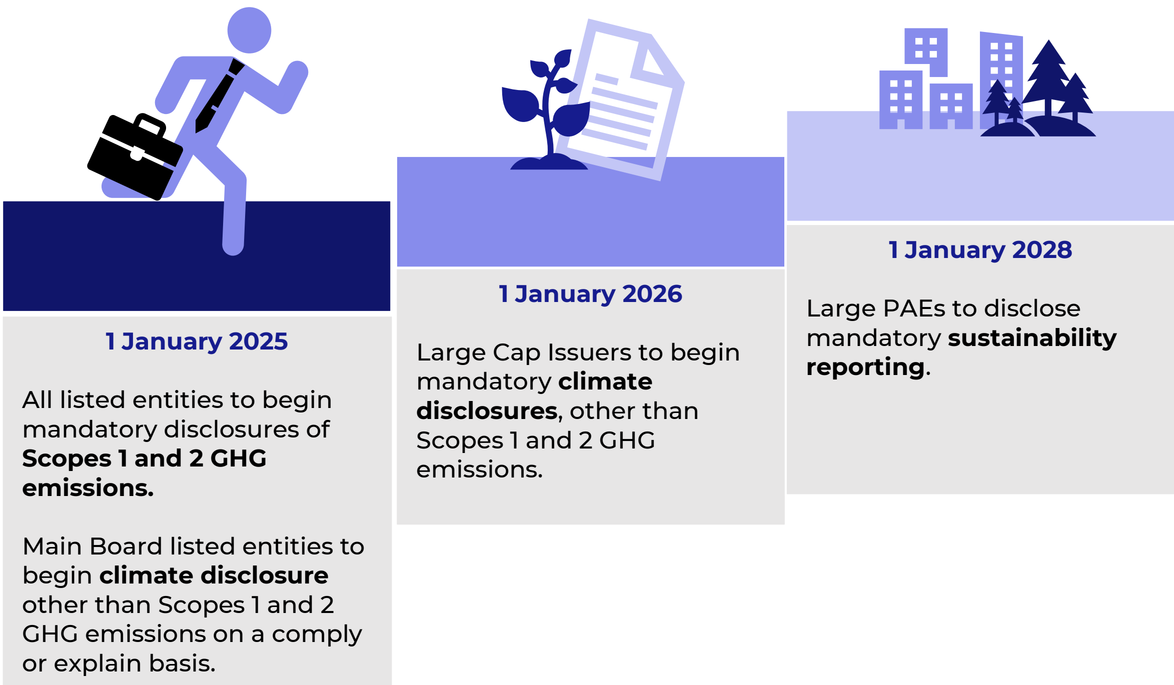
4.5. Under the Roadmap, **Hong Kong will prioritise the application of the Hong Kong Standards by PAEs** using a phased-in approach:

a. The HKEX will consult the market in 2027 on mandating sustainability reporting against the Hong Kong Standards for listed PAEs starting from 1 January 2028 under a proportionate approach; and

b. The relevant financial regulators will seek market comments and feedback on requiring similar reporting by non-listed financial institutions carrying a significant weight in Hong Kong.

This is consistent with the inaugural jurisdictional guide[31] published by the IFRS Foundation in May 2024.

Figure 3: The evolution of sustainability reporting requirements



[31] The IFRS Foundation (2024) *The Inaugural Jurisdictional Guide for the adoption or other use of ISSB Standards.*

4.6. Over the past few years, the HKICPA conducted extensive engagement with over 150 entities to gather views on the application of the ISSB Standards in Hong Kong. This included a technical feasibility study conducted from March to June 2024.[32]

4.7. In December 2024, the HKICPA issued the Hong Kong Financial Reporting Standards (**HKFRS**) Sustainability Disclosure Standards, which are fully aligned with the ISSB Standards. This follows a public consultation from September to October 2024, which solicited general support. These standards may be voluntarily adopted starting from 1 August 2025.

5. Climate risk exposure reported by listed entities

5.1. Understanding climate-related risks enables businesses to safeguard themselves and their stakeholders from evolving regulations and business practices, while also capitalising on opportunities in an increasingly climate-conscious world.

5.2. Based on the recommendations by the Task Force on Climate-related Financial Disclosures (**TCFD**), climate-related risks can be categorised as physical and transition risks.[33]

a. **Physical risks** relate to the physical impacts of climate change to businesses, driven by events such as floods and typhoons or chronic risks from sustained high temperatures or rising sea-level; and

b. **Transition risks** relate to risks arising from the transition to a lower-carbon economy, which include policy, technological, and market changes to mitigate or adapt to climate change.

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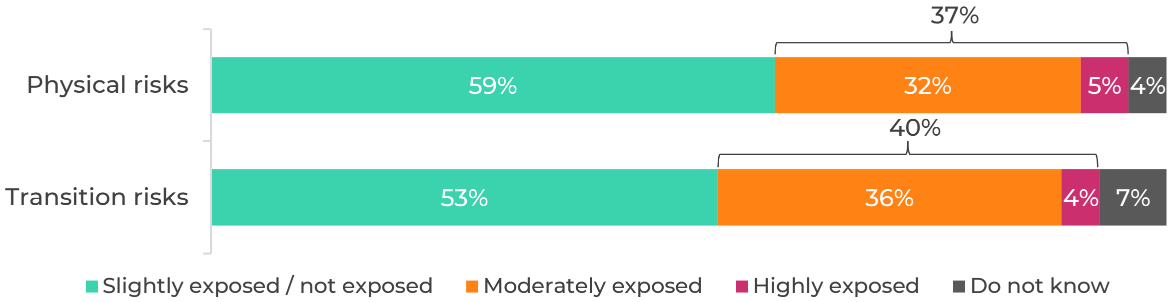
[32] HKICPA (2024) *Explanatory Memorandum* HKFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information and* HKFRS S2 *Climate-related Disclosures.*

[33] TCFD (2017) *Recommendations of the Task Force on Climate-related Financial Disclosures*. With the TCFD disbanded in October 2023, the ISSB took over the monitoring of TCFD framework.

Figure 4. Overall exposure to climate-related risks (n=797)



5.3. Among 797 listed entities surveyed (Figure 4):

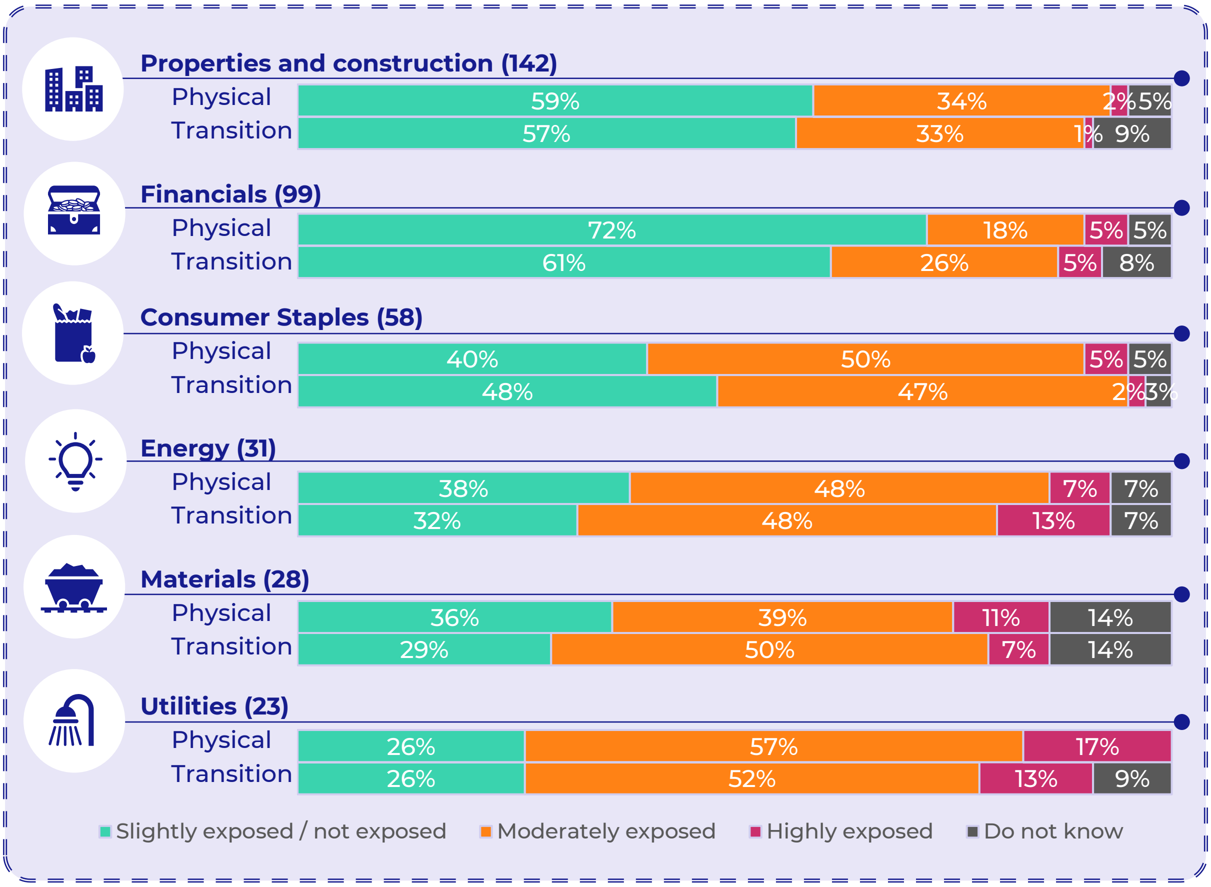
a. **Over one-third considered themselves moderately or highly exposed** to physical (37%) and transition (40%) risks. The prevalence of climate-related risks among Hong Kong listed entities underscores the urgent need for listed entities to identify, address, and report them.

b. **Between 4% and 7% were yet to assess their exposure to physical and transition risks respectively**. By evaluating their exposure, those in climate-sensitive industries can transform their business models and enhance their long-term financial sustainability.

There is a tide in the affairs of men, which taken at the flood, could lead on to fortune. Sustainability reporting need not be taken as a mere compliance exercise. It can be a valuable tool to assist entities in managing risks and reap new opportunities from an increasingly climate-conscious market.

5.4. The TCFD has identified five industries most affected by climate change. We have identified respondents from these climate-sensitive industries and analysed their reported exposures in Figure 5. The reported exposure from other respondents is analysed in Figure 6.

Figure 5. Climate-related risk exposure reported by listed entities surveyed from climate-sensitive industries (n=381)[34]



5.5. Of the 381 listed entities surveyed from climate-sensitive industries (Figure 5):

a. Over half from the consumer staples, energy, materials and utilities sectors reported moderate or high exposures to physical risks and/or transition risks. This is consistent with the TCFD's observations;[35]

[34] The TCFD (2017) identified six industries most affected by climate change: Banking, Insurance, Energy, Materials and Buildings, Agriculture, Food, and Forest Products, and Transportation. The first five were mapped to Financials, Energy, Utilities, Materials, Property and Construction, and Consumer Staples in Hang Seng Industry Classification. Transportation was excluded as it was categorised within another industry and not separately identifiable.

[35] TCFD (2017) *Recommendations of the Task Force on Climate-related Financial Disclosures*.

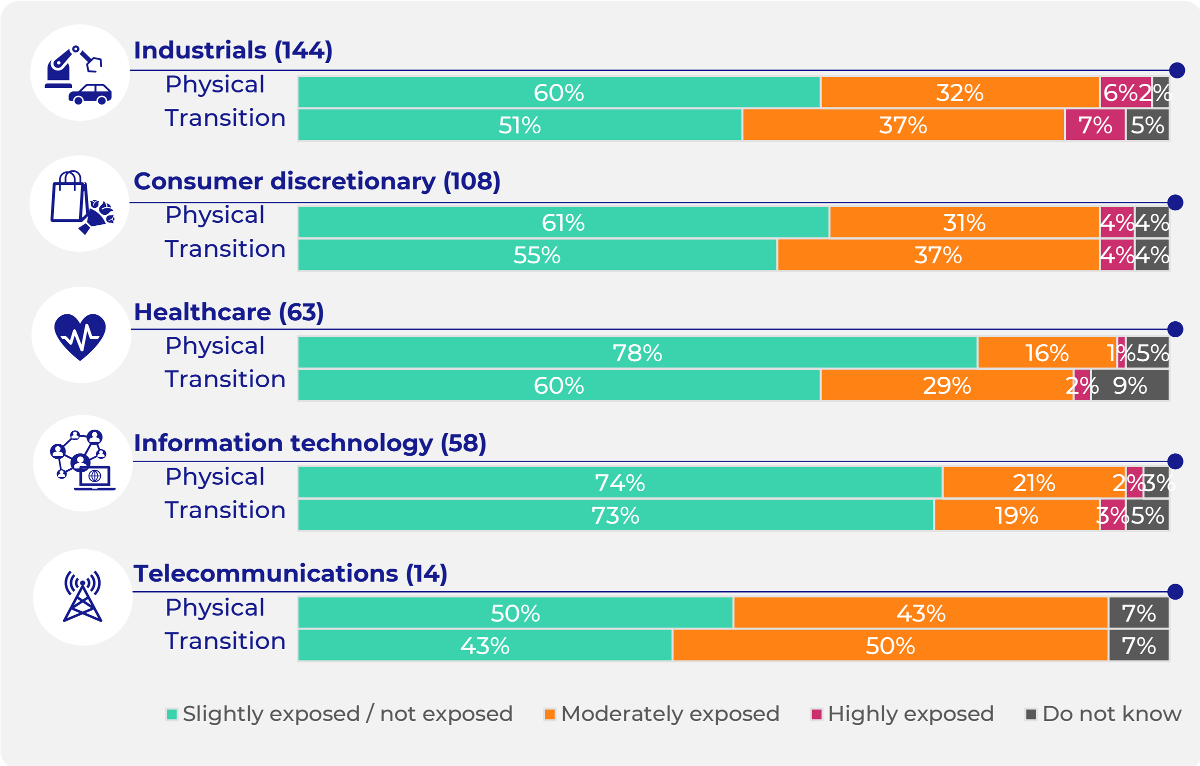
b. **14% of respondents from the materials sector had not yet assessed their climate exposures**. This is an area for improvement; and

c. **Within the financial services sector, 72% and 61% of listed entities believed they were slightly or not exposed to climate-related risks**. This contrasts with findings from the CDP which show that, on average, reported financed emissions from global financial institutions were over 700 times larger than reported operational emissions.[36]

Better three hours too soon than a minute too late. In our quest to address climate change, let us not delay. Awareness is the first step towards meaningful action. Only by understanding the full scope of the related risks, listed entities can develop robust strategies to mitigate them.

[36] CDP Worldwide (2020) *The Time to Green Finance - CDP Financial Services Disclosure Report 2020.*

Figure 6. Climate-related risk exposure reported by listed entities surveyed from other industries (n=387)[37]



5.6. Among the 387 respondents from other industries (Figure 6):

a. Over half believed that they were slightly or not exposed to climate-related risks. Risks can change over time due to evolving regulatory environments and other factors. Entities must remain vigilant and regularly update their risk assessments;

b. **Over half from the telecommunications sector reported no or slight exposure to climate-related risks.** With increasing digitalisation, the electricity consumption from operations maybe increasing rapidly. In addition, climate-friendly regulations may impact their equipment span going forward;[38] and

c. **Over three-quarters from the information technology sector believed that they were slightly or not exposed to climate-related risks.** Considering the carbon footprint of artificial

[37] This figure excluded 29 valid responses that did not indicate a specific industry.
[38] The World Bank (2024) *Measuring the Emissions & Energy Footprint of the ICT Sector.*

intelligence and cloud computing, these entities may wish to ensure their climate-related risk exposures are measured holistically.[39]

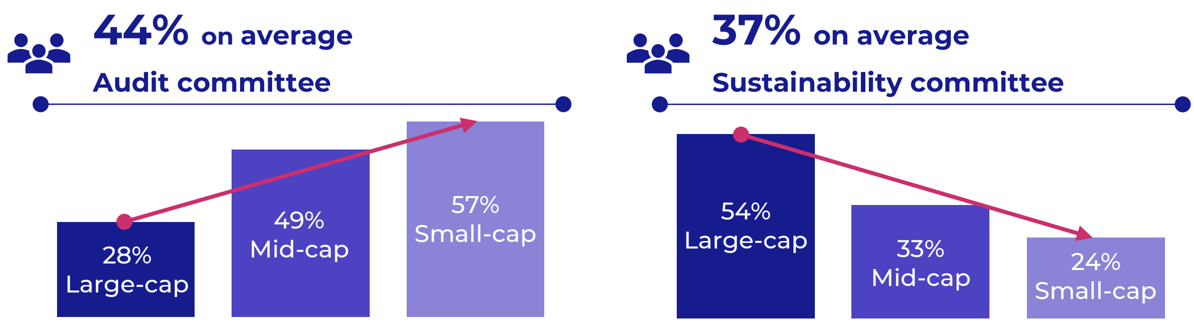
To know thyself is the beginning of wisdom. Listed entities should start with engaging with key stakeholders and to identify and analyse possible risk factors that could affect the long-term sustainability of the business and its stakeholders.

6. Board and management responsibility for sustainability reporting

6.1. **Accountability and good governance are essential to manage the risks and opportunities arising from climate change and other sustainability issues.** In practice, listed entities may assign the oversight of sustainability to the existing Board or the audit committee, or set up new Board committee such as a sustainability committee to conduct the oversight.

6.2. When asked who holds the primary responsibility for climate reporting at the Board and management level, the responses from the listed entities surveyed were mixed.

Figure 7. Board's oversight of sustainability reporting (n=797)



[39] IDC (2024) *AI Datacenter Capacity, Energy Consumption, and Carbon Emission Projections.*

6.3. Of the 797 listed entities surveyed, 44% indicated that **their audit committee was primarily responsible for the oversight of sustainability reporting**. This is followed by the sustainability committee (37%) (Figure 7) and the Board (19%).

6.4. **Larger listed entities were more likely to assign the oversight to the sustainability committee.** 54% of 278 Large-cap respondents did so, compared with 24% of 266 Small-cap respondents. On the other hand, 57% of Small-cap respondents assigned the oversight to audit committee, as compared to 28% of Large-cap respondents. (Figure 7)

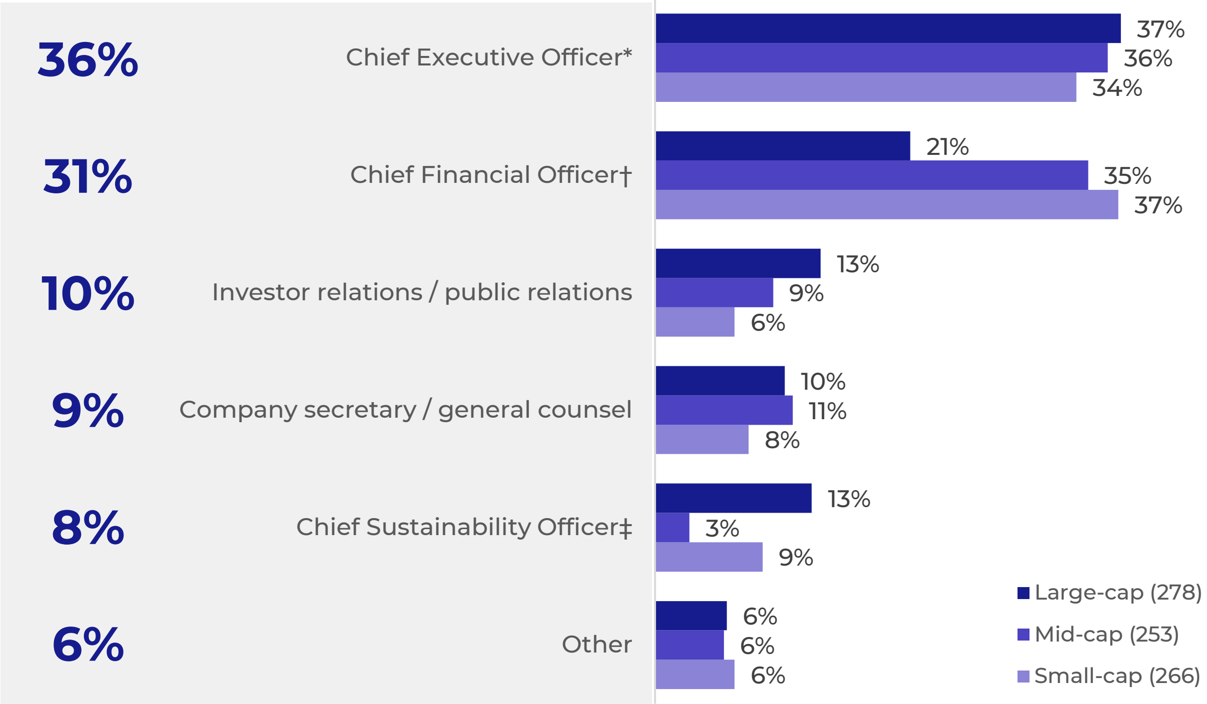
6.5. For good governance, the **Board, audit committee, and sustainability committee have roles to play in sustainability reporting and assurance:**

a. The Board approves the overall strategy, including evaluating trade-offs, if any.

b. The audit committee oversees the management's plan to bring their reporting to the standard required for formal reporting and assurance requirements. This may include the internal controls to ensure information reported is complete, accurate, and capable of being assured;

c. The sustainability committee drives the sustainability and decarbonisation journey, including setting realistic targets and monitoring progress; and

Figure 8. Management responsibility for sustainability reporting (n=797)



Notes: * Including Chief Executive Officer and other executive directors.
† Including Chief Financial Officer and finance team.
‡ Including Chief Sustainability Officer and sustainability team.

6.6. Of the 797 listed entities surveyed (Figure 8), **three-quarters (75%) assigned the responsibility of sustainability reporting to C-suite executives:**

a. The primary responsibility typically rests on the Chief Executive Officer (36%) or the Chief Financial Officer (31%). Balancing sustainability responsibilities with their existing financial duties can be demanding; and

b. Only a minority (8%) created a new role and assigned the responsibility to the Chief Sustainability Officer. This approach ensures dedicated leadership and expertise in driving sustainability initiatives and integrating climate-related risks into their business strategies.

A leader, armed with profound knowledge, guides the people through the shadows of uncertainty. It is essential for the Board to upskill senior management, regardless of their background, to prepare for the rapidly evolving demands of sustainability risk management and reporting.

6.7. Analysed by market capitalisation (Figure 8):

a. **Chief Financial Officers of Small-cap respondents were more likely to be assigned the primary responsibility for sustainability reporting** (37%), compared to Large-cap respondents (21%); and

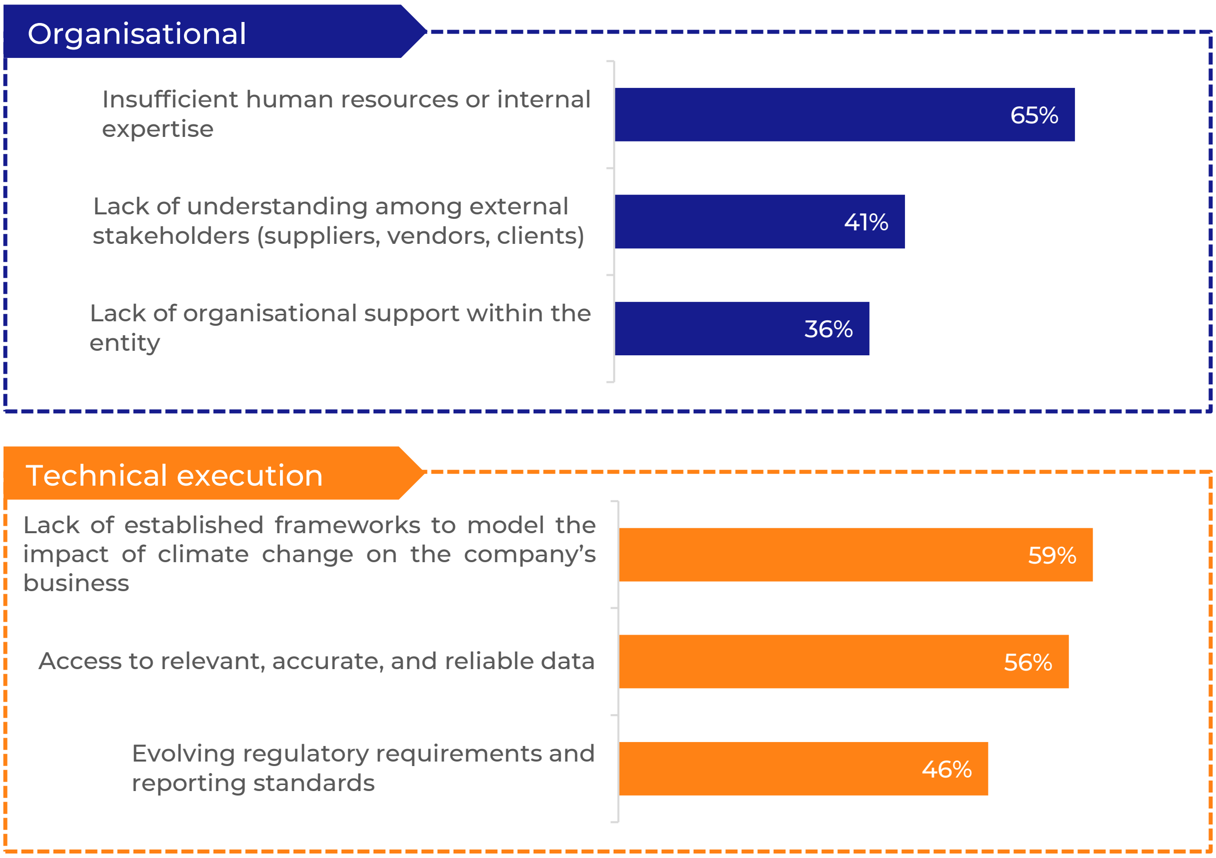
b. A higher proportion of Large-cap respondents delegated this responsibility to their investor relation or public relation teams (13%) compared to 6% from Small-cap respondents.

7. Challenges in preparing climate reports

7.1. As climate reporting requirements become increasingly robust, listed entities should invest in enhancing their capacity. To determine where the investments should be channelled, it is essential to first identify the key challenges.

7.2. Listed entities were asked whether they encountered any of six potential challenges during their preparation of climate reports. These challenges can be categorised into "organisational" or "technical execution".

Figure 9. Challenges in preparing climate reporting (n=797)



Organisational level

7.3. When preparing climate reporting, three key "players" are essential: internal team that collects the data and prepares the report, external stakeholders that provides value chain data, and leadership team that provides strategic direction and organisational support.

7.4. **Close to two-thirds (65%) of listed entities surveyed reported insufficient human resources or internal expertise** to perform climate reporting tasks (Figure 9). This is consistent with a 2023 global study, where listed entities reported a limited knowledge of the ISSB's proposals and intended to fill the gap by prioritising staff development.[40]

[40] The International Organization of Securities Commissions (2023) *Report on International Work to Develop a Global Assurance Framework for Sustainability-related Corporate Reporting.*

Nurturing the roots of talent today will blossom into a sustainable future tomorrow. The availability of trained sustainable professionals is an essential part of a comprehensive sustainable disclosure ecosystem. Initiatives such as the Pilot Green and Sustainable Finance Capacity Building Scheme will help improve the talent pipeline.

7.5. The lack of understanding among stakeholders — including suppliers, vendors, and clients — was a lesser challenge, with only 41% selecting it. Organisational support within the entity, including the Board, was a challenge for even fewer (36%) respondents (Figure 9).

Technical execution level

7.6. A robust framework ensures accurate risk assessment, reliable data supports informed decision-making, and complying with evolving regulatory requirements is vital for effective reporting. We inquired whether listed entities encounter challenges in these areas.

7.7. Over half of the listed entities surveyed experienced challenges with **modelling the impact of climate change on their businesses** (59%) and **accessing relevant, accurate, and reliable data** (56%) (Figure 9). The latter included challenges in collecting value chain data for Scope 3 GHG emissions reporting. Capacity building efforts in this area for small- and medium-sized entities would help improve value chain reporting.

7.8. **Close to half (46%) found evolving regulatory requirements and reporting standards as a challenge** (Figure 9). This situation is particularly complex for Hong Kong listed entities with operations in the European Union, as they may need to comply with the European reporting standards concurrently.

The ISSB Knowledge Hub[41] is designed to help companies prepare their ISSB disclosures. It hosts content developed by the IFRS Foundation and more than 100 resources developed by third-party organisations.

In Hong Kong, besides the HKICPA's website, the CASG website[42] has been enhanced with GHG emissions calculation and estimation tools to help corporates to assess or report emissions based on their activities.

8. Getting ready for robust climate reporting

8.1. For a reporting entity to effectively comply with the CRD requirements, it must be adequately prepared in three components:

a. **Data and technology**: Listed entities need robust data management and analytical capabilities to identify, measure, and monitor their climate exposures.

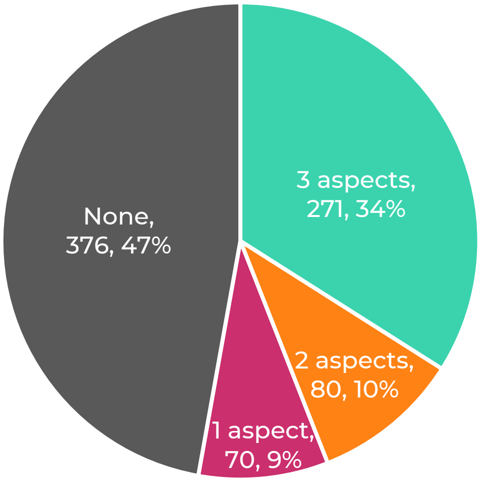
b. **Internal controls, systems, and governance:** Comprehensive internal control frameworks, well-defined reporting processes, and clear governance structures – along with defined roles and responsibilities - are critical for ensuring the quality climate-related information; and

c. **Financial and human resources:** Listed entities need to budget resources for upskilling existing staff or recruiting sustainability talent.

[41] The IFRS Knowledge Hub includes content curated by the IFRS Foundation and its partners to help preparers apply the ISSB Standards from different levels of knowledge and experience.

[42] CASG website can be found at www.sustainablefinance.org.hk.

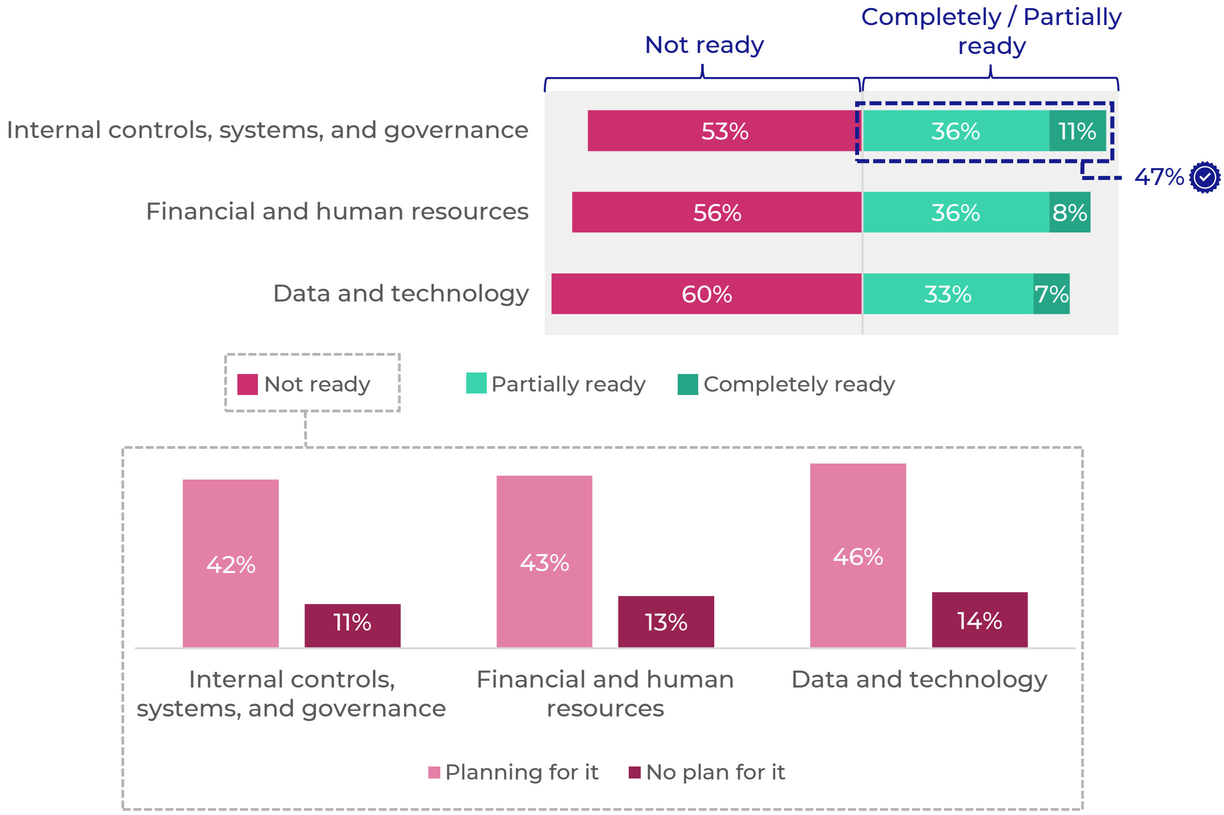
Figure 10. Readiness for climate reporting across three components (n=797)



8.2. We assessed the readiness of listed entities across the three components. **At the time of the study, over one-half of listed entities surveyed were gearing up for robust sustainability reporting, with one-third (34%) considering themselves partially or fully ready across all three components** (Figure 10). These entities are likely leaders in the sustainability space. We encourage them to share their best practices through industry associations, and regional and international forums. **47% needed to invest in all three components** (Figure 10).

> **Let responsibility guide us, for the time to act is now.** The commitment to act is the most important ingredient for robust reporting. Given the increasing number of resources made available, listed entities can make rapid strides to enhance the robustness of their disclosures and meet the expectations of their stakeholders.

Figure 11. Readiness for climate reporting analysed by each component (n=797)



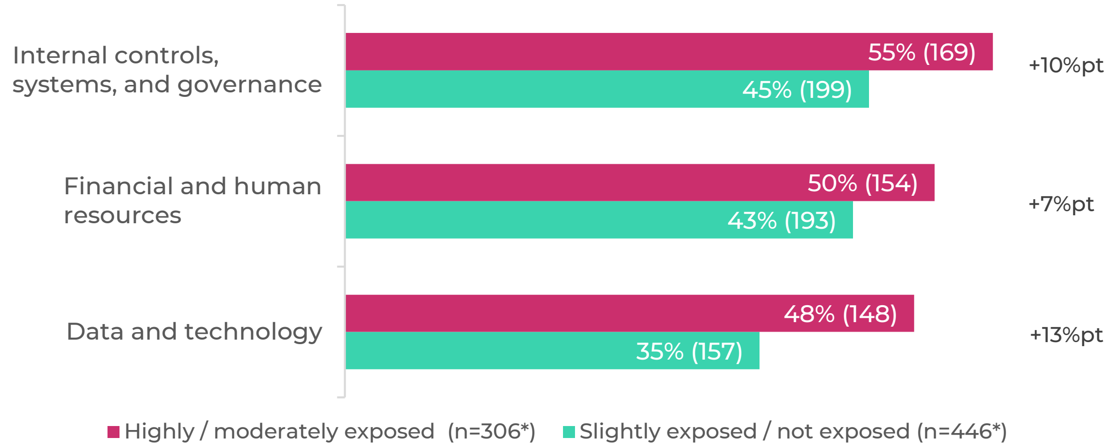
8.3. Among the three components essential for effective climate reporting (Figure 11):

a. **Close to half (47%) of listed entities surveyed were partially or fully ready for "internal controls, systems, and governance".** Meanwhile, 44% were partially or fully ready for "financial and human resources" and 40% for "data and technology".

b. Climate data contains data points collected across multiple teams in a reporting entity. While Excel spreadsheets can fill the gaps at the onset, the data collection process may become increasingly complex over time, leading to frictions and waste. In this context, robust internal controls ensure confidence in the data for external reporting as well as effective internal decision-making involving multiple stakeholders.

To prepare for data collection, listed entities should start with understanding the information required for reporting, and perform a gap analysis to identify the data and reporting gaps.

Figure 12. Readiness for climate reporting analysed by climate exposure[43]



8.4. **Heightened risk awareness drove listed entities to accelerate their preparation for climate reporting** (Figure 12):

a. 38% (or 306 on average) of listed entities surveyed considered themselves moderately or highly exposed to climate-related risks;

b. These entities were seven to 13 percentage points more prepared, as compared to those who considered themselves slightly or not exposed to climate-related risks; and

c. **Despite the higher figures, preparedness for reporting is an opportunity for improvement for these entities.** Half (between 48% and 55%) of the respondents in this group indicated that they were prepared in each component.

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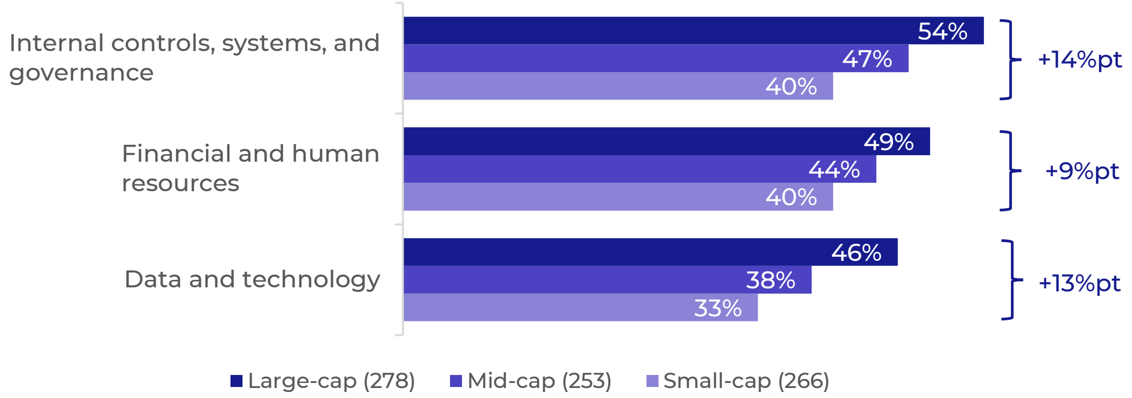
[43] For this analysis, the exposure to climate-related risks was determined by using the average of physical and transition climate-related risks.

Figure 13. Readiness for climate reporting analysed by market capitalisation (n=797)



8.5. **Large-cap respondents were nine to 14 percentage points more prepared** for each of the three components, as compared to Small-cap respondents (Figure 13). This is not surprising as larger entities have more resources and are subjected to higher public scrutiny:

a. Large-cap and Mid-cap respondents are most prepared for the "internal controls, systems, and governance" component, followed by "financial and human resources" and "data and technology".

b. Small-cap respondents were equally ready for the "internal controls, systems, and governance" and "financial and human resources" components, while they were least ready for "data and technology".

c. The differences in preparedness across size segments explain the emphasis of proportionality mechanisms in the reporting standards, as well as the ongoing capacity building initiatives undertaken by financial regulators and other stakeholders.

9. Benefits of involving in-house accountants in climate reporting

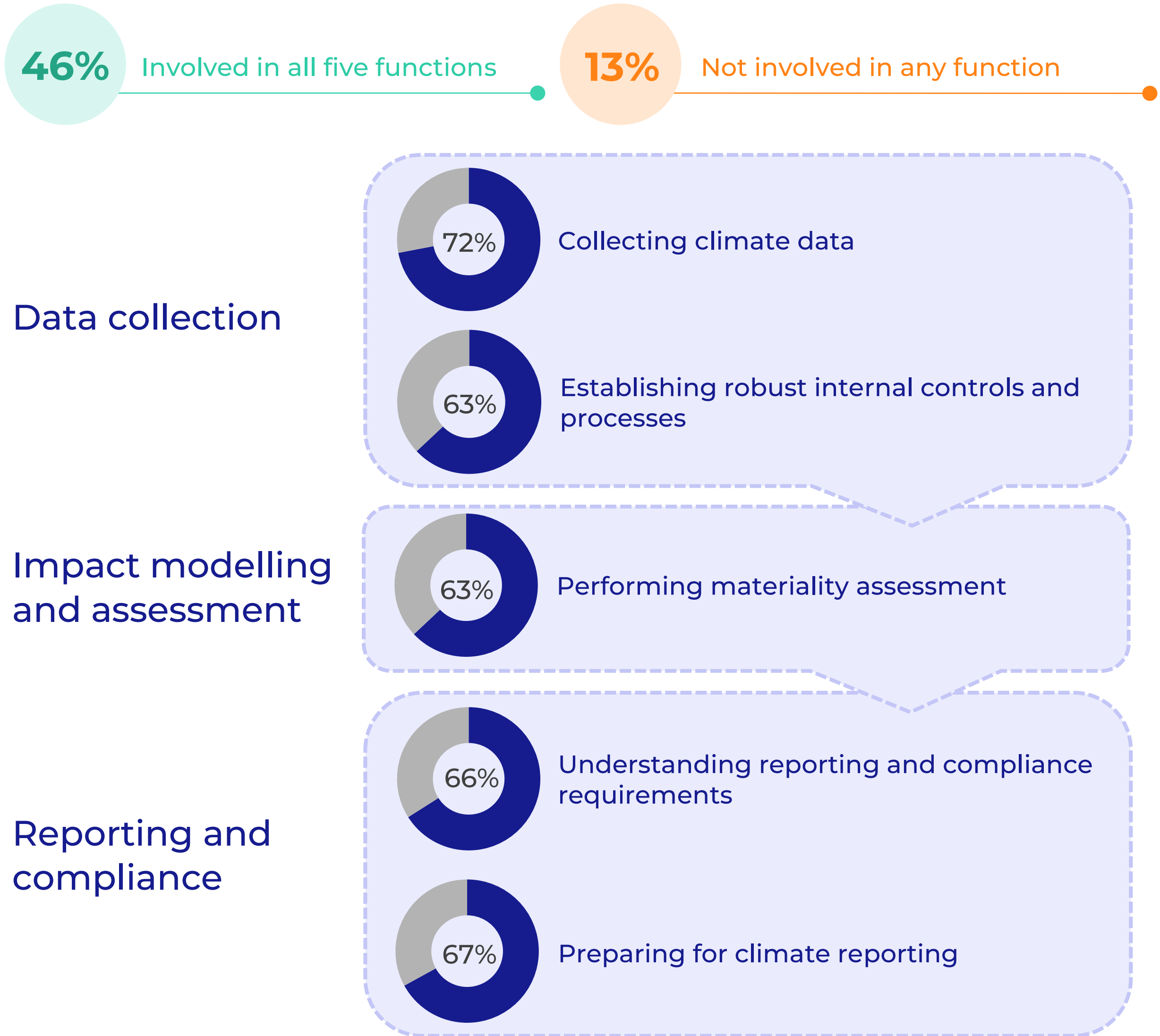
9.1. As corporate reporting evolves beyond financial reporting to incorporate sustainability information, **professional accountants are well positioned to meet the needs of investors and other stakeholders**. This is because they have the skills and understanding to identify material sustainability information and disclose them effectively.

9.2. A 2022 **study showed that accountants were not fully involved in sustainability reporting**. Barriers include a mindset that sustainability issues are peripheral to the business, an overt focus on financial priorities and incremental improvements, and viewing sustainability accounting as a specialisation outside of the accounting function.[44]

9.3. We asked listed entities how they have involved their in-house accountants in five functions for climate reporting. These functions align closely with the skillset of accountants and allow listed entities to leverage on their expertise.

[44] Wenzig et. al. (October 2022) *Path dependence of accountants: Why are they not involved in corporate sustainability? Business Strategy and the Environment*.

Figure 14. Climate reporting functions involving in-house accountants (select all that applies) (n=797)



9.4. **46% of listed entities surveyed involved in-house accountants in all five functions for climate reporting**. Accountants were most engaged in climate data collection (72%). (Figure 14)

9.5. On a positive note, **over half (56%) planned to increase the involvement of in-house accountants in the next three years**. By leveraging the skills of in-house accountants, these entities can enhance the accuracy and reliability of their CRD, ensuring compliance with evolving reporting standards and practices.

Figure 15. Benefits from involving in-house accountants in climate reporting (select all that applies) (n=697)

63% Bridging financial and sustainability reporting helps integrate climate factors into financial reporting

60% Ensuring high quality and rigour of sustainability reporting

55% Leveraging well developed processes for data collection and reporting

54% Leveraging established channels to engage Board, senior management and external assurance providers

9.6. As shown in Figure 15, **a key benefit of involving in-house accountants was to bridge financial and climate reporting** (63%). As climate reporting evolves, investors and other report users increasingly expect more quantitative disclosures, including the anticipated financial effects of sustainability-related risks and opportunities over the short, medium, and long term.

9.7. **In contrast, 13% of listed entities surveyed did not involve any in-house accountants in their climate reporting process (Figure 14).** Reasons include not seeing how climate-related issues relate to financial reporting. These entities overlook the critical role that accounting expertise plays in accurately assessing and disclosing climate risks.

> Reporting entities cite a lack of expertise for sustainability reporting. Accountants are ideally suited to take on this role, with their keen analytical minds, critical thinking, and business acumen.

Section C: Listed entities' considerations for sustainability assurance

10. Assurance practices in Hong Kong

10.1. Independent sustainability assurance enhances the trust and confidence investors and other stakeholders have in sustainability information.

10.2. A study by the International Federation of Accountants (**IFAC**) revealed that:

a. The percentage of the largest listed entities across 22 jurisdictions obtaining sustainability assurance rose from 51% in 2019 to 69% in 2022.[45]

b. The same study showed that the top 50 largest listed entities in Hong Kong made good progress. **Those that voluntarily obtained assurance doubled from 26% in 2019 to 52% in 2022.**

10.3. In contrast, **only 7.5% of listed companies with December year-end had voluntarily obtained sustainability assurance in 2022.** This is based on a study conducted by the HKICPA across 1,882 Hong Kong-listed entities.[46]

Assurance practices among constituents of the Hang Seng Index

10.4. In one part of this study, we **analysed the sustainability assurance reports published by 82 HSI constituents** in 2023 and 2024.[47] Their practices provide a relevant benchmark for leading assurance practices in Hong Kong.

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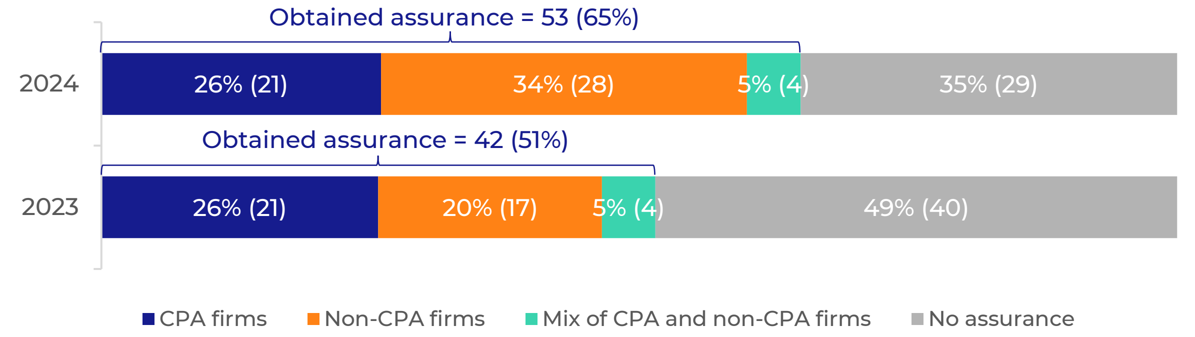
[45] IFAC and the Association of International Certified Professional Accountants (AICPA) & the Chartered Institute of Management Accountants (CIMA) (2024) *The State of Play in Sustainability Disclosure and Assurance*.

[46] HKICPA (2023) *ESG Assurance in Hong Kong 2023: An evolving landscape*. The report covered Hong Kong listed entities with 31 December 2022 as their financial year end.

[47] "2023" covers sustainability assurance reports for the financial years ended between 31 December 2022 to 30 June 2023 while "2024" covers those for the financial years ended from 31 December 2023 to 30 June 2024.

Figure 16. Sustainability assurance reports published by HSI constituents (n=82)



10.5. In 2024, **around two-thirds (65%) of HSI constituents published assurance reports on sustainability disclosures,** an increase of 14 percentage points from 2023 (Figure 16). **The growth was driven by non-CPA firms** that collectively provided sustainability assurance to 32 HSI constituents including 28 that solely used non-CPA firms. CPA firms continued to serve 25 HSI constituents (including 21 that solely used CPA firms). The number of entities which used both CPA and non-CPA firms remained unchanged at four. While the Hong Kong Quality Assurance Agency accounted for ten engagements, in all, eight non-CPA firms and Big Four network firms provided assurance services to 53 HSI constituents, which reflects a diverse and growing market for these services.

10.6. The decline in share of CPA firms is consistent with a previous study, which showed that the market share of audit firms conducting sustainability assurance globally declined by five percentage points between 2019 and 2022.[48] We will elaborate on the considerations for selecting assurance providers in the next section.

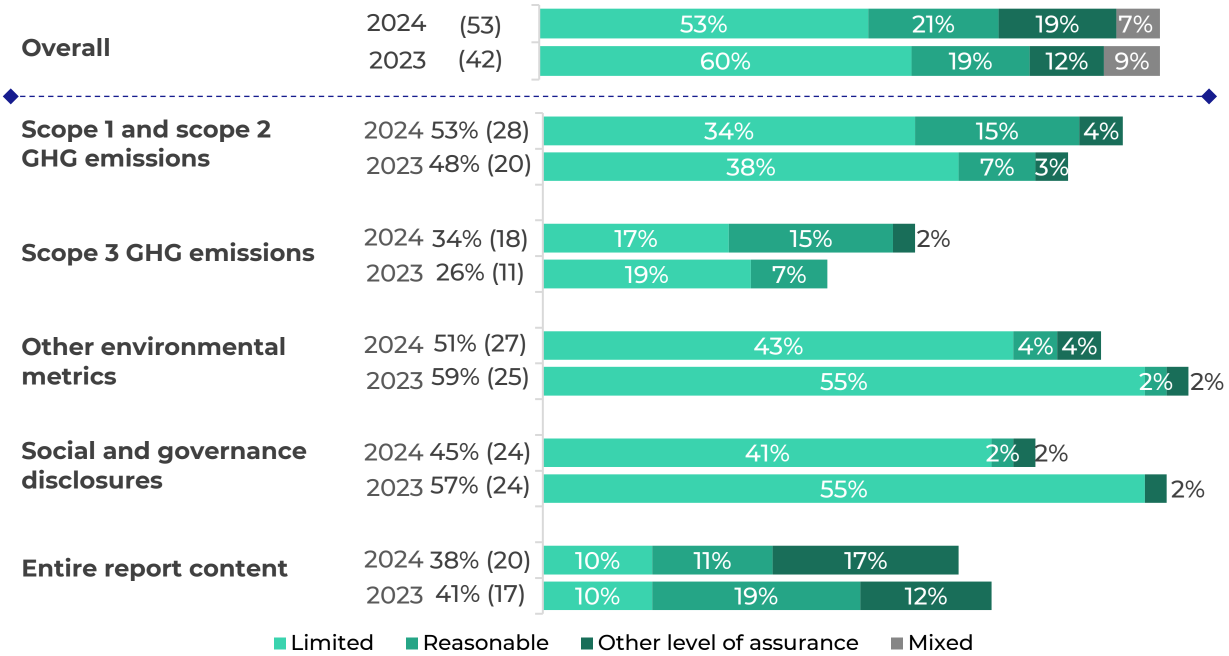
10.7. Disclosures commonly assured can broadly be categorised as follows:

a. **Environmental metrics** such as "Scope 1 and Scope 2 GHG emissions", "Scope 3 GHG emissions", and "Other environmental metrices" (e.g., water use, waste management); and

b. **Social and Governance disclosures** around talent management, supply chains, stakeholder engagement, and worker safety.

[48] IFAC and AICPA & CIMA (2024) *The State of Play in Sustainability Disclosure and Assurance.*

Figure 17. Level of sustainability assurance among HSI constituents that published sustainability assurance reports (n=53 (2024), 42 (2023))[49]



10.8. **HSI constituents were increasingly prioritising sustainability assurance, particularly for GHG emissions** (Figure 17). In 2024, over half (53% of 53) published assurance on their **Scope 1 and Scope 2 GHG emissions**, up from 48% of 42 in 2023. The high assurance percentages reflect the fact that scope 1 and scope 2 emissions are within the entity's direct control and are relatively easier to measure and manage. The assurance on **Scope 3 GHG emissions** rose to 34% of 53, increasing by 12 percentage points from 2023. The increase in assurance engagements, despite the complexity in estimating them, shows the increasing importance of scope 3 emissions for both companies and investors.

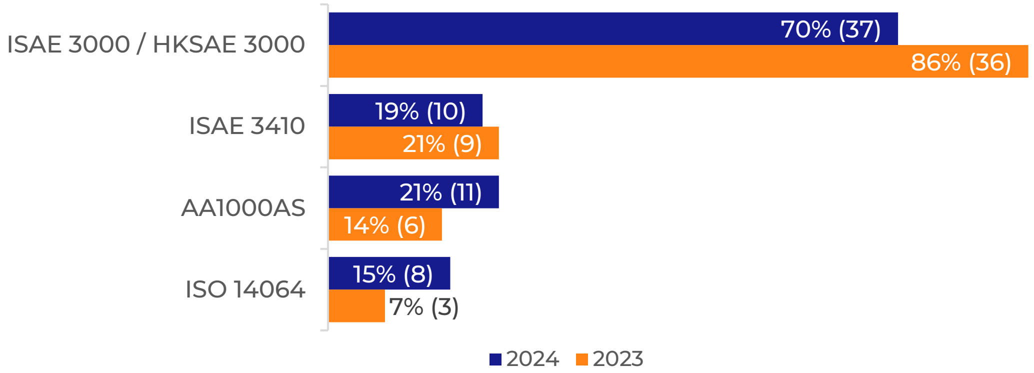
10.9. Assurance obtained on other environmental metrics, as well as social and governance disclosures remained unchanged on an absolute basis. **On the other hand, 20 HSI constituents published assurance covering their entire sustainability reports in 2024, compared to 17 in 2023.** Given the vast scope of a typical sustainability report, unless such assurance

[49] For this diagram, other level of assurance refers to high or moderate levels of assurance as defined in the AA1000AS.

engagements are performed in a robust manner, it may lead to market confusion with regards to quality.

10.10. When analysed by the level of assurance obtained, **over half (53%) of assurance reports in 2024 was limited assurance**, i.e. the assurance provider performs basic procedures to conclude that nothing has come to their attention suggesting material misstatement. The scope is narrower, procedures are less detailed, and conclusions are expressed in negative form (nothing has come to our attention). **21% of HSI constituents obtained reasonable assurance.** It was worth noting that the percentage which covered Scope 3 GHG emissions doubled to 15%. Out of the remaining 26%, 7% obtained different levels of assurance for different disclosures, and the remaining 19% obtained high or moderate levels of assurance based on AA1000AS.

Figure 18. Assurance standard applied in sustainability assurance of HSI constituents (n=53 (2024), 42 (2023))



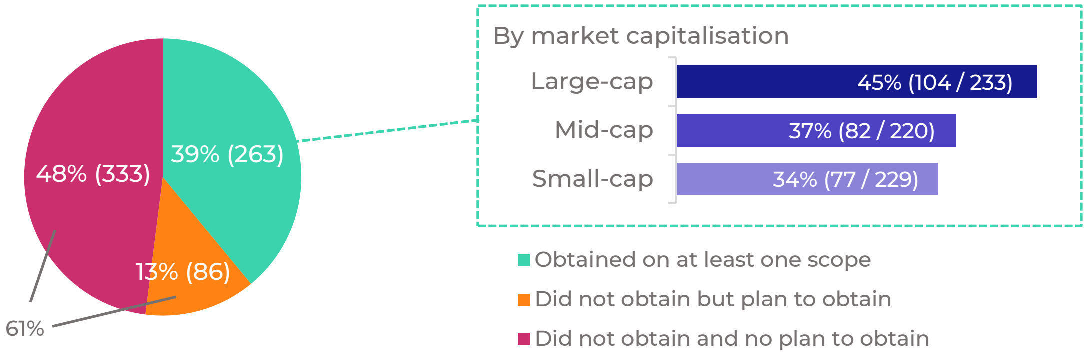
10.11. Overall, **the ISAE standards issued by the IAASB were used most frequently, particularly the ISAE 3000 or its equivalent** (70%) (Figure 18). Other assurance engagements used AA1000AS (21%), ISAE 3410 (19%), and ISO 14064-3 standard (15%). Considering the ISSA 5000 standards are built upon the existing IAASB standards and guidance that are used for sustainability assurance, including the ISAE standards, its prevailing adoption bodes well for the future.

Assurance practices for a broader group of listed entities

10.12. We also surveyed listed entities on their plans to obtain sustainability assurance, along with the related motivations or deterrents.

10.13. We received 115 responses (14% of 797) indicating that their financial auditors or CPA firms provided high levels of assurance on their sustainability disclosures. Since this is not typical practice in Hong Kong, we conducted inquiries with some respondents. They seemed to have misunderstood that the auditor's audit opinion on financial statements covered sustainability disclosures as "other information". Therefore, we excluded these responses, leaving 682 valid responses for analysis.

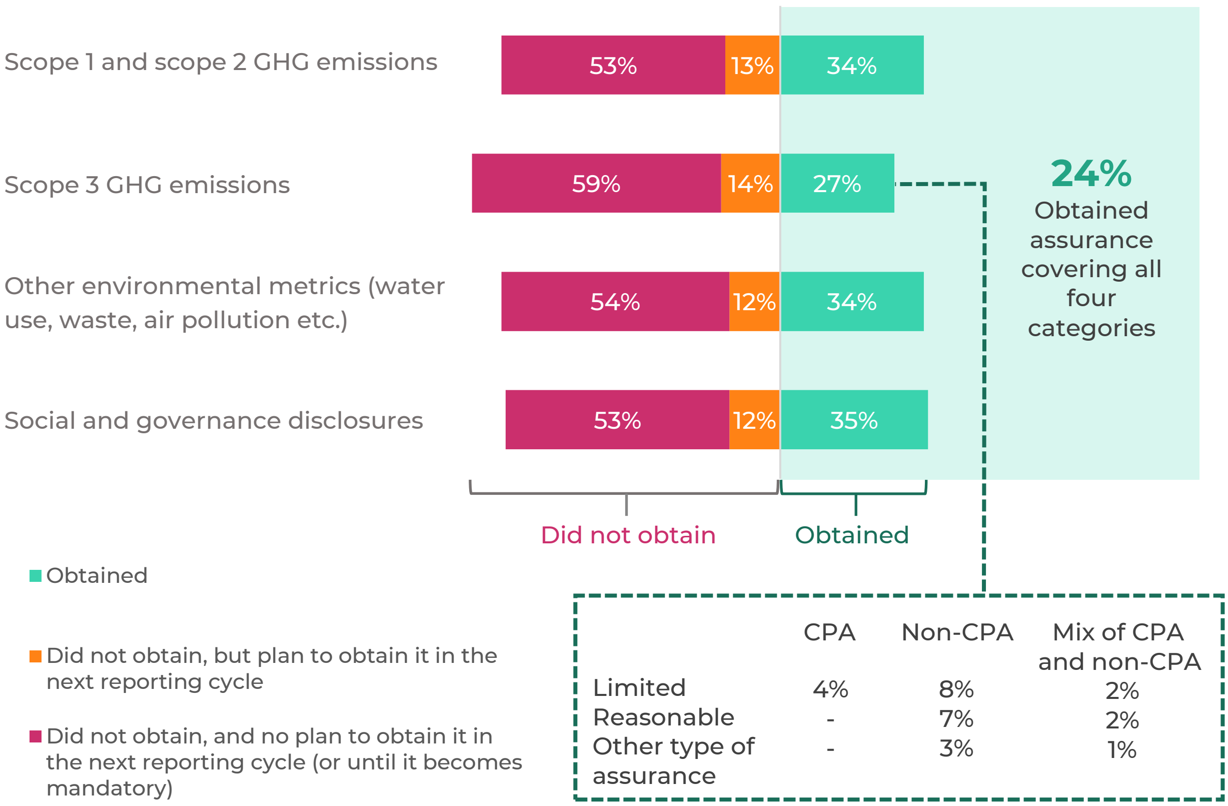
Figure 19. Profiles of listed entities surveyed that obtained or plan to obtain sustainability assurance (n=682)



10.14. Among 682 valid responses from listed entities, **39% had obtained assurance on their sustainability disclosures** (Figure 19). They were reasonably diversified across Large-cap, Mid-cap, and Small-cap segments. **61% did not obtain sustainability assurance, but 13% planned to do so in the next reporting period.**

Build trust today for a sustainable future: Investors increasingly demand credible sustainability information. The finding highlights the need for increased efforts to encourage more entities to obtain assurance on their sustainability reports to meet investor needs.

Figure 20. Disclosures subjected to assurance (select all that applies) (n=682)



	CPA	Non-CPA	Mix of CPA and non-CPA
Limited	4%	8%	2%
Reasonable	-	7%	2%
Other type of assurance	-	3%	1%

10.15. **In terms of the disclosures subject to assurance, nearly a quarter (24%) of listed entity respondents obtained assurance on all four categories** (Figure 20). This percentage is higher than the 11% of HSI constituents.

10.16. **The most assured disclosures were "Scope 1 and Scope 2 GHG emissions" (34%), "other environmental metrics" (34%), and "social and governance disclosures" (35%).** A little over a quarter (27%) obtained assurance on "Scope 3 GHG emissions", with two-thirds of these engagements solely performed by non-CPA firms. This number is slightly higher when compared to HSI constituents, of which 22% obtained assurance on this metric, with slightly more than half of these engagements performed by non-CPA firms.

10.17. Obtaining assurance for Scope 3 GHG emissions is far more challenging than Scope 1 and 2 GHG emissions as it relies on third-party emission data which can vary in availability and reliability.

11. Considerations on whether to obtain sustainability assurance

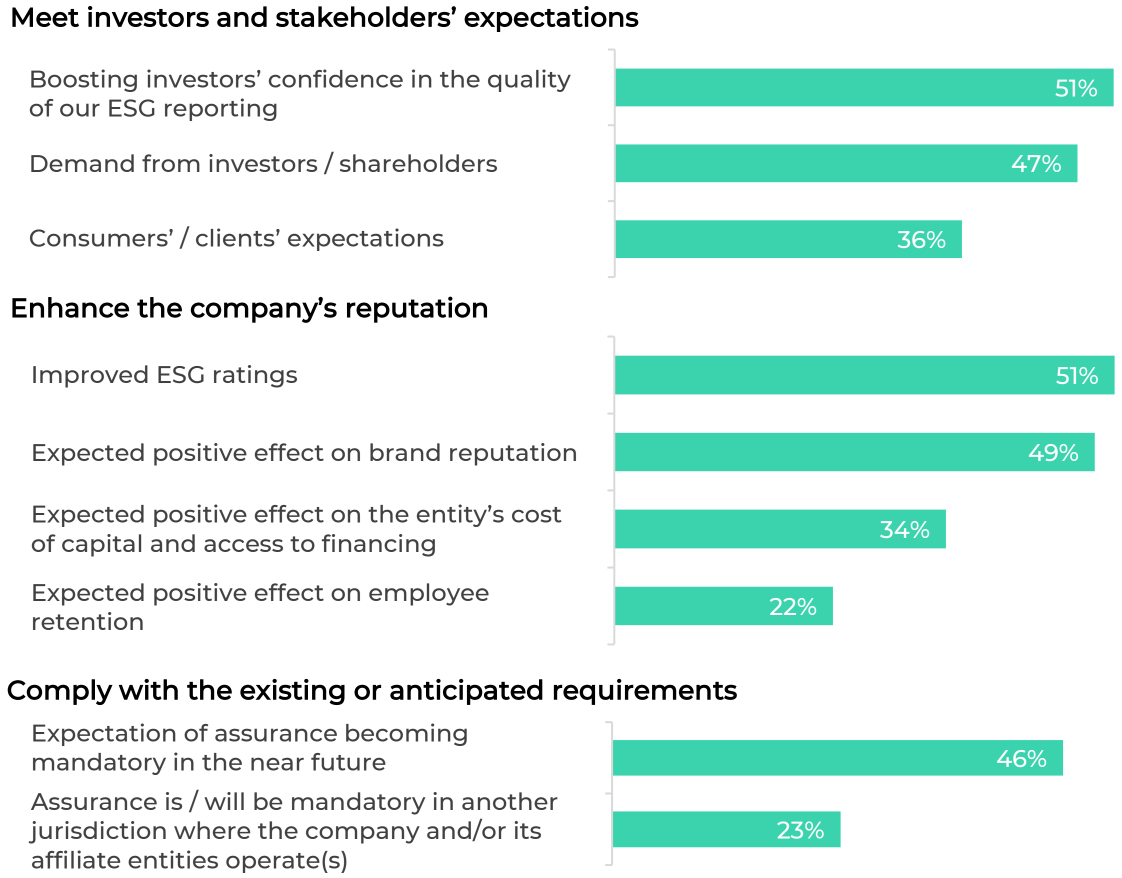
11.1. We surveyed listed entities that obtained or intended to obtain sustainability assurance on their motivation to do so, which broadly fall into three categories:

a. Meet investors and stakeholders' expectations;

b. Enhance the entity's reputation; and

c. Comply with the existing or anticipated requirements.

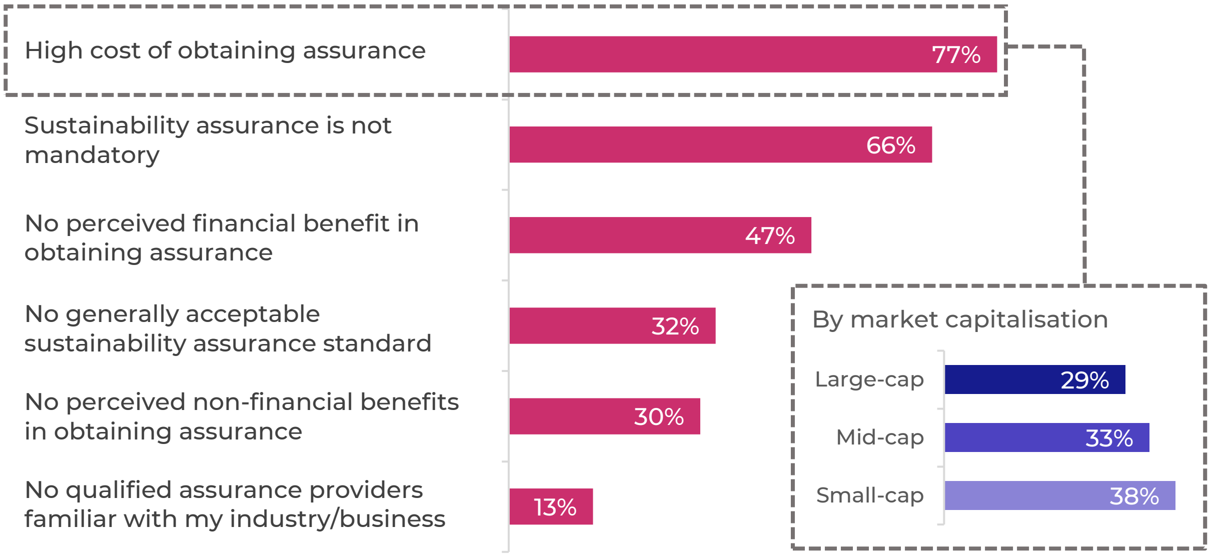
Figure 21. Motivation for obtaining sustainability assurance (select all that apply) (n=349)



11.2. Among 349 valid responses that obtained or planned to obtain assurance by the next reporting cycle, around half did so **to boost investors' confidence in ESG reporting (51%) and meet expectations from investors and shareholders (47%)** (Figure 21)**.**

11.3. Around half also did so to enhance **the company's reputation through improved ESG ratings (51%), positive effect to brand reputation (49%)**, and **in anticipation that assurance would become mandatory (46%)**.

Figure 22. Reasons for not obtaining and having no plan to obtain sustainability assurance (select all that apply) (n=333)



11.4. As shown in Figure 22, among the 333 listed entities surveyed that did not obtain sustainability assurance,

a. **77%** identified **high cost as the key deterrent**, with smaller entities feeling the financial burden more acutely. Further, **many respondents did not perceive the financial (47%) or non-financial (30%) benefits of obtaining assurance.** We urge entities to conduct a thorough cost-benefit analysis and consider the opportunity cost of not obtaining assurance, including compliance and reputational risks from potential greenwashing.

b. **Two-thirds said cited assurance being voluntary** as the reason to not seek it.

> **Plant the seeds of preparation today to harvest the benefits of assurance.** Listed entities that are obtaining assurance cited a host of benefits beyond the mere expectation of assurance becoming mandatory in the future. Even for those entities already obtaining assurance, the evolution to mandatory assurance may involve incremental efforts to refine the governance structures, processes, systems, and controls. Therefore, we urge other entities to start their journey to ensure they are prepared.

c. **Around one-third (32%) cited the lack of accepted sustainability assurance standards as a barrier.** Global efforts, such as the IAASB's development of profession-agnostic ISSA 5000, aim to provide consistent requirements regardless of the assurance provider's background.

d. **Only 13% cited a lack of qualified assurance providers**. The low percentage is a positive sign. The development of robust assurance standards and the expected release of the regulatory framework for sustainability assurance should provide further impetus for qualified assurance providers to offer their services.

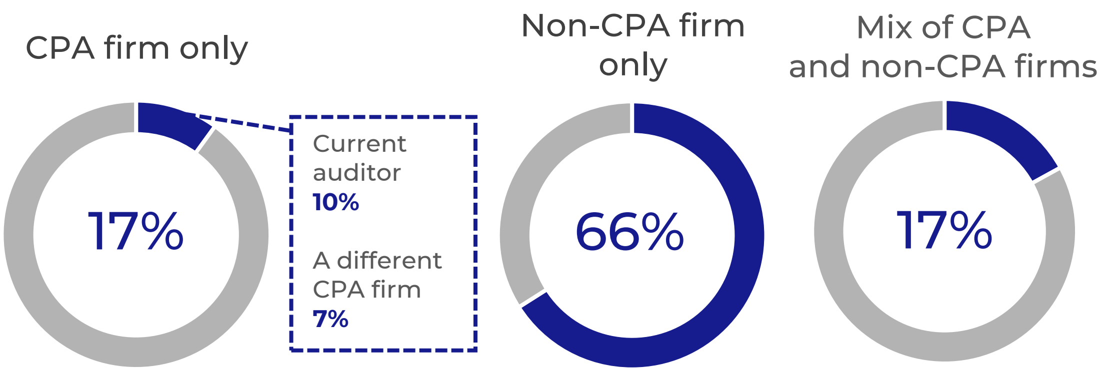
11.5. We also inquired with selected listed entities that obtained sustainability assurance beyond ESG disclosures in their public reports. These entities sought assurance to enhance internal processes including evaluating the effectiveness of their internal GHG reporting platform to verify the reliability of generated information and improve data quality.

11.6. This proactive approach benefits organisations by ensuring that their sustainability efforts are based on accurate and trustworthy data. By strengthening internal reporting mechanisms, these entities not only enhance compliance with regulatory requirements but also improve overall operational efficiency.

12. Considerations for selecting assurance providers

12.1. We asked the 263 listed entities that obtained sustainability assurance whether they engaged their current financial auditor, a different CPA firm, or a non-CPA firm to provide the service.

Figure 23. Profiles of sustainability assurance providers (n=263)

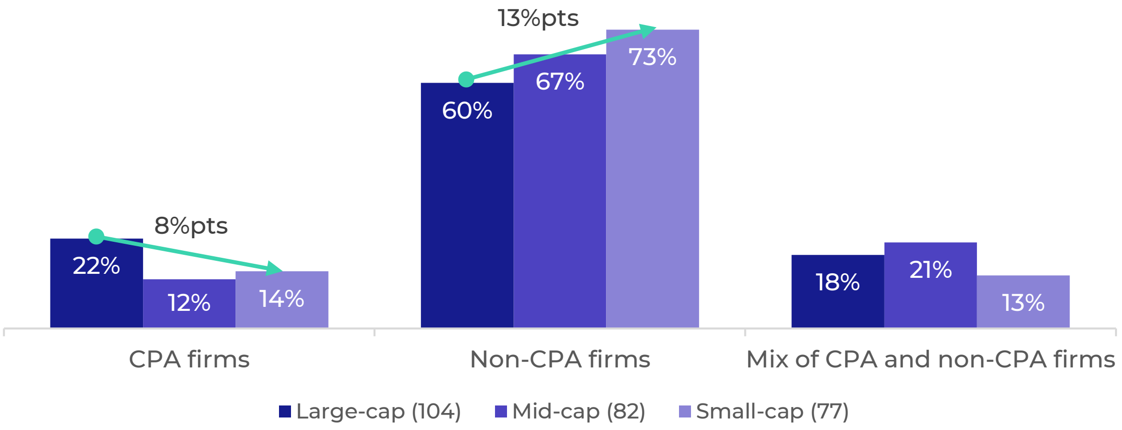


12.2. The results indicate that the choice of assurance providers is diverse (Figure 23). This highlights the dynamic nature of the assurance market, and the different strategies entities employ to meet their needs.

12.3. **66% of listed entity respondents reported opting exclusively for non-CPA assurance providers, and 17% relied solely on CPA firms, with 10% selecting their financial auditors and 7% selecting different CPA firms.** The remaining 17% took a balanced approach, engaging a mix of both CPA and non-CPA assurance providers.

12.4. While we discuss the considerations for selecting assurance providers shortly, in our stakeholder engagements, participants suggested that sustainability information most valued by investors tend to be more forward looking, and non-CPA firms were more comfortable providing assurance on them as compared to the CPA firms. However, as standards and practices mature to incorporate assurance of forward-looking information, we expect participants to apply them in a robust manner, creating a level-playing field.

Figure 24. Profiles of sustainability assurance providers by listed entities' market capitalisation (n=263)



12.5. Further analysis of the profiles of listed entities that reported using CPA firms versus non-CPA firms by market capitalisation show that Large-cap respondents were eight percentage points more likely to engage CPA firms than Small-cap respondents (Figure 24). On the other hand, Small-cap respondents were 13 percentage points more likely to engage non-CPA firms than their Large-cap counterparts.

12.6. Small-cap entities may have simpler business models compared to Large-cap entities, and the resulting sustainability issues may be less complex. Considering that they may have fewer resources to allocate to sustainability issues, and the fact that assurance is voluntary, the commitment of these entities to embark on the sustainability assurance journey is commendable.

Figure 25. Top criteria for selecting sustainability assurance provider (select up to three) (n=263)

12.7. As shown in Figure 25, the criteria for selecting assurance providers varied. **Among the 55 listed entities surveyed that engaged their financial auditors to conduct sustainability assurance, most (62%) prioritised familiarity with the client’s circumstances ahead of industry knowledge and ESG expertise.**

12.8. **Among those that engaged a different CPA firm (46) or a non-CPA firm (219) to conduct sustainability assurance, over half prioritised industry knowledge.** Cost was prioritised by 38% of respondents that engaged a non-CPA firm.

12.9. **Only a small proportion of listed entities (7% to 15% across the three groups) considered assurance methodologies and quality control procedures to be key factors in their selection process.** We encourage listed entities to prioritise these elements as they are crucial for ensuring the quality of assurance engagements.

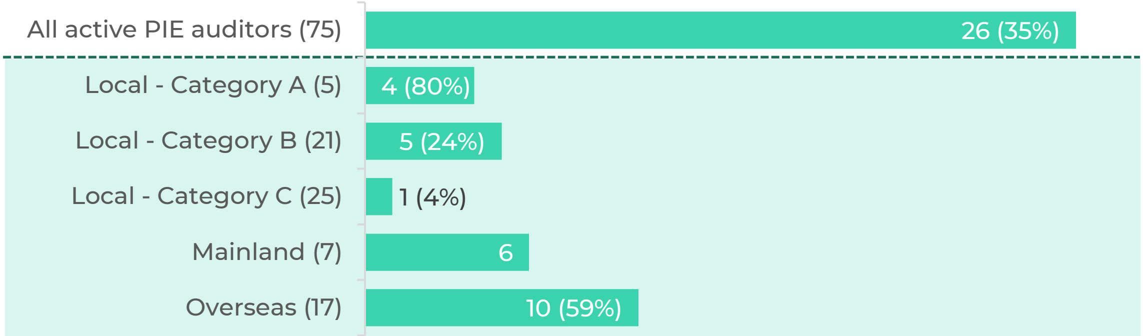
Expertise and integrity are key for high quality assurance. Listed entities should appoint assurance service provider based on their expertise in the subject matter, capability to provide robust assurance methodologies, the effectiveness of their quality management systems, and adherence to ethical and independence requirements.

Section D: Readiness of PIE auditors to provide sustainability assurance

13. Provision of sustainability assurance services

13.1. To understand the readiness of CPA firms, we surveyed 75 active PIE auditors on their sustainability assurance practices, including their team composition, key challenges, and future plans.

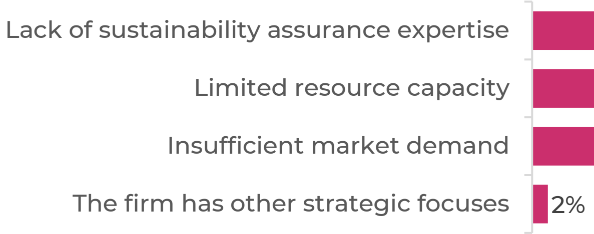
Figure 26. Active PIE auditors that offered sustainability assurance (n=75)



13.2. There is significant growth opportunity for CPA firms to offer sustainability assurance. **35% (or 26 of 75 PIE auditors) offered sustainability assurance services** (Figure 26). 88% (23 of 26) belonged to networks that provided them with methodology and other support to provide sustainability assurance services. In these firms, the sustainability assurance processes, including engagement acceptance, assurance procedures, and assurance reporting are typically built on their existing ones for financial audit, to ensure standardisation and consistency.

13.3. **10 of the 26 PIE auditors received sustainability assurance engagements in the prior year**. They comprised four Category A local firms, four firms from the Mainland, and two overseas firms. As we noted earlier, familiarity with client's circumstances was the top reason cited by listed entities for selecting the CPA firms (especially their financial auditor) for sustainability assurance engagements. In addition, from our stakeholder engagements, some entities also suggested that brand name as an important factor. We will discuss the challenges in providing sustainability assurance in the next section.

Figure 27. Reasons for not providing sustainability service (select all that apply) (n=49)



13.4. 49 PIE auditors, most of them belonging to Category B and C, do not offer sustainability assurance services. These firms cited a **lack of expertise (67%) and limited resources (61%) as the key hurdles** (Figure 27). As the market for assurance expands, these smaller firms need to balance the risks of rushing into new service areas before building sufficient capacity and expertise against the risks of delaying entering the market and potentially missing out on the opportunities.

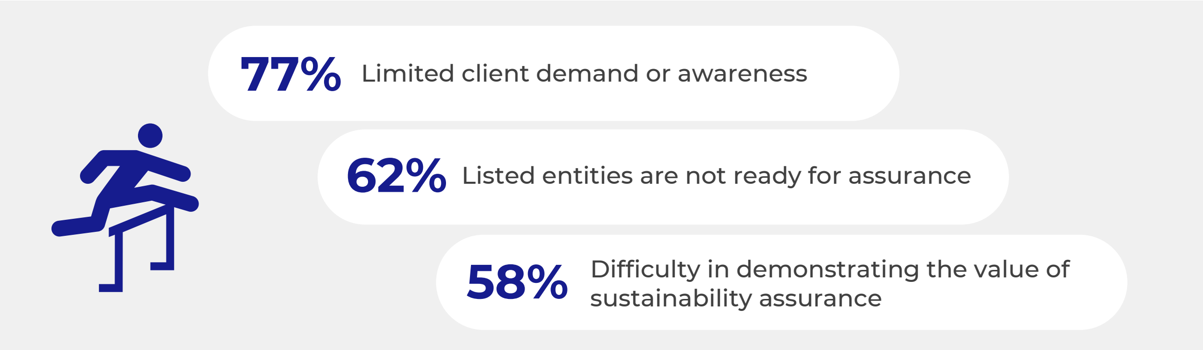
One should push forward to truly grow. The HKICPA provides learning resources including ESG strategy formulation and communication, climate change, ESG reporting best practices, ISSB standards, and ESG assurance and sustainable business practices.[50] We encourage auditors to leverage them.

14. Challenges in providing sustainability assurance

14.1. We asked the 26 PIE auditors offering sustainability assurance services about their challenges from the bidding phase to the execution phase.

[50] HKICPA. *Continuous Professional Development (CPD) Programmes. Environmental, Social, and Governance (ESG)*

Figure 28. Challenges in securing sustainability assurance engagements (select all that apply) (n=26)



14.2. As shown in Figure 28,

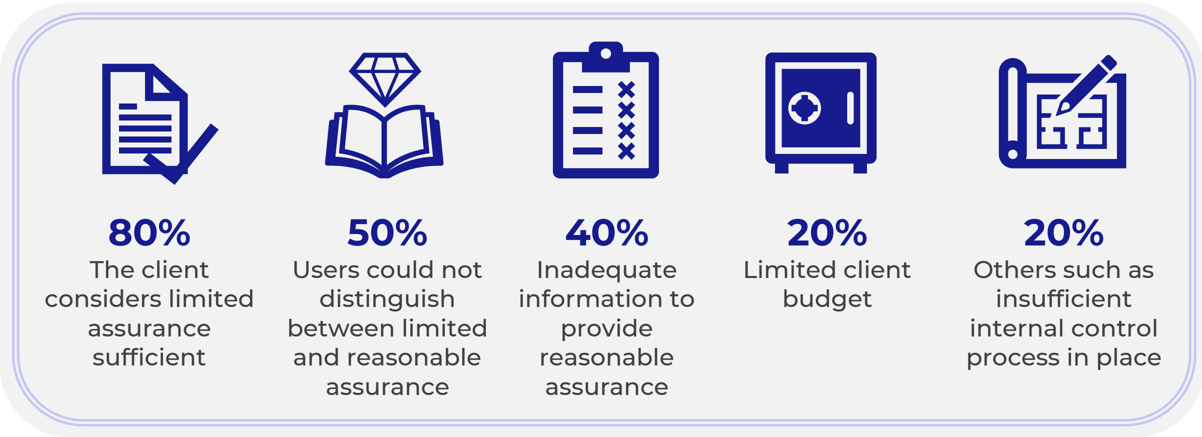
a. Limited client demand or awareness emerged as a significant challenge, with 77% (20) of PIE auditors experiencing it. This may stem from competition from non-CPA firms, with more prior experience.

b. The lack of client's readiness for assurance and difficulty in demonstrating the value of the service, as experienced by 62% (16) and 58% (15) of PIE auditors.

c. The lack of client readiness includes concerns around the quality and reliability of the sustainability data, as well as their internal control systems. Auditors also face communication barriers among the operational staff of companies responsible for sustainability reporting, who were not in the accounting and financial fields.

d. The difficulty in demonstrating the value of service is due to the time it takes for the market to understand the intrinsic value of sustainability reporting and assurance, and, given the diversity of assurance standards and practices, the need for PIE auditors to educate their clients on the value of robust quality management procedures and ethical and independence requirements.

Figure 29. Barrier to providing reasonable assurance (select all that apply) (n=10)



14.3. **In the prior year, all 10 PIE auditors with sustainability assurance engagements provided limited assurance.** Barriers to providing reasonable assurance as shown in Figure 29 include:

a. **Their clients considered limited assurance to be sufficient (eight auditors).** This could stem from a lack of readiness for reasonable assurance, or a choice to opt for the less rigorous and often cheaper option;

b. **The users of assurance reports could not distinguish between limited assurance and reasonable assurance (five auditors).** Educating clients about the implications of each type of assurance could empower them to make more informed decisions and elevate the demand for reasonable assurance in the longer term; and

c. Constraints at the clients' end were less prominent, including inadequate information to provide reasonable assurance (cited by four auditors), limited budget (two), and immature internal controls (two). As many listed companies strive to enhance their sustainability reporting (as discussed in Chapter 8), we expect that these challenges will be addressed over time.

Figure 30. Composition of sustainability assurance teams as of 31 December 2023 (n=10)

- **90%** CPA or equivalent **with** specialised ESG qualifications
- **70%** CPA or equivalent **without** specialised ESG qualifications
- **50%** Other in-house ESG specialists such as engineers / scientists
- **0%** External ESG specialists

14.4. Among the 10 PIE auditors that provided sustainability assurance prior year, **most teams included accountants with ESG qualifications** (nine PIE auditors)**,** along with accountants without ESG qualifications (seven) (Figure 30). Further, **half (five) employed non-accountant ESG specialists**. No firm hired external ESG specialists. Comprehensive and diverse expertise - whether internal or external - is essential for addressing complex sustainability challenges effectively.

> **Identify skill gaps and upskill your team.** As each engagement may require different subject matter expertise, it is crucial to ensure that teams have the right expertise and apply robust assurance methodologies.

Figure 31. Plan to expand the service (select all that apply) (n=10)

- **100%** Expand size of in-house sustainability team by upskilling and re-skilling existing partners and staff
- **80%** Expand the scope of sustainability assurance services
- **70%** Expand size of in-house sustainability team by recruiting
- **60%** Invest in technology to facilitate sustainability

14.5. **All 10 PIE auditors planned to expand their sustainability service practice** (Figure 31).

a. All planned to expand the size of the in-house team, either by upskilling and reskilling existing partners and staff (100%) or by recruiting (70%). Given the highlighted lack of expertise in the market, it's encouraging that all auditors are prioritising internal development as their primary strategy for growth.

b. 60% planned to invest in technology to facilitate sustainability assurance. This investment could include tools for improved ESG data verification and analytics, as well as assurance programs to create a clearer audit trail of the work performed.

14.6. **With these plans, 80% expected to also expand the scope of their services.** This expansion may encompass more complex topics and diverse parameters such as GHG scope 3 emissions, and a wider range of industries, allowing them to offer enhanced sustainability services that meet the evolving needs of their clients.

Section E: Practices of PIE auditors to assess and address climate-related risks in financial audits

15. Requirements to assess and address climate risks

15.1. Auditors are required to assess and address the financial impacts of climate change when auditing financial statements.[51] They must also read sustainability disclosures presented in the annual reports and consider any material inconsistencies with the audited financial statements.

15.2. **One study found that audit clients facing greater exposure to climate-related risks tend to pay higher audit fees** as auditors consider climate change risks and their potential impact as a systematic business risk that is factored into audit fees.[52]

15.3. **Using audit fee as a proxy, another study found that auditors expended greater audit effort (reflected in higher audit fees) in listed entities with tainted ESG reputations.** This study also found that this increased audit effort contributed to improved audit quality by reducing the likelihood of financial statement restatements.[53]

15.4. In the 2023 Audit Focus, the AFRC highlighted "Impacts of Climate Change" as an area that requires special consideration by auditors and set out the AFRC's expectations for auditors.[54] Our expectations include:

a. Assess climate-related impacts on significant transactions, estimates, and disclosures;

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[51] IAASB (2020) *Staff Audit Practice Alert - The Consideration of Climate-Related Risks in an Audit of Financial Statement.*

[52] Hartlieb and Eierle (2022) *Do Auditors Respond to Clients' Climate Change-related External Risks? Evidence from Audit Fees.*

[53] Asante-Appiah (2020) *Does the severity of a client's negative environmental, social and governance reputation affect audit effort and audit quality?*

[54] AFRC (2023) *Audit Focus: 2023 Financial Year-end Audit Reminder.*

b. Consider any material inconsistency of other information, including sustainability reporting, against the financial information of the audit clients;

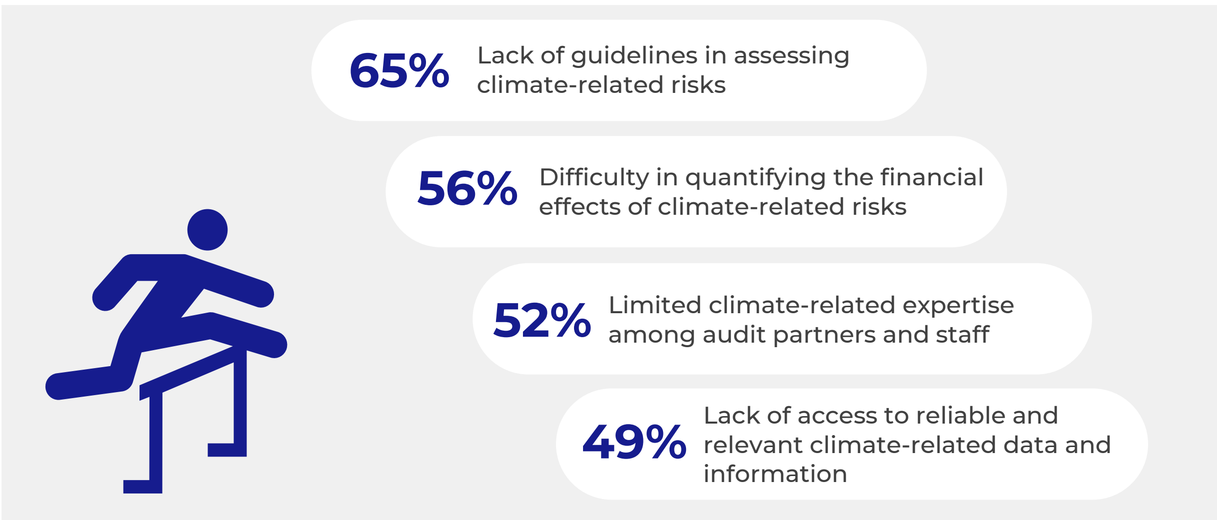
c. Upskill auditor's competence and capabilities on ESG-related requirements and matters; and

d. Evaluate the independence requirements, before acceptance of assurance or non-assurance services related to ESG reporting of audit clients.

16. Challenges in addressing climate-related risks during financial audits

16.1. We asked about the key challenges PIE auditors encountered when addressing climate-related risks in audits of financial statements.

Figure 32. Challenges in assessing climate-related risks (n=75)



16.2. Among the 75 PIE auditors surveyed, **the most prevalent challenge was the perceived lack of guidelines in assessing climate-related risks**, which was cited by 65% respondents.

Sometimes, the answers we seek are like keys hidden in our own pockets — always within reach, yet often overlooked. It is worth noting that standard setters and professional bodies have issued guidance on applying the existing auditing standards in the context of climate change which are useful reference to auditors. For instance,

a. the IAASB's Staff Audit Practice Alert[55] provides guidance to assist auditors in understanding what already exists in the International Standards on Auditing (**ISAs**) that should be considered in financial statement audits by highlighting the ISAs that may be most relevant in relation to climate-related risks and the potential effect on the audits.

b. the IFRS education material[56] reminds stakeholders on the long-standing requirements in IFRS Accounting Standards to report on the effects of climate-related matters in the financial statements when those effects are material.

c. the IFRS webcasts[57] discuss how IFRS Accounting Standards and IFRS Sustainability Disclosure Standards complement each other. Through practical examples, they illustrate how applying the Standards together results in complementary and connected reported information.

d. the HKICPA's Sustainability Information Centre[58] offers convenient access to the latest development, thought leadership as well as learning resources on sustainability, tailored specifically for the accounting profession to stay at the forefront of market developments.

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[55] IAASB (2020) *Staff Audit Practice Alert - The Consideration of Climate-Related Risks in an Audit of Financial Statement.*

[56] IFRS (Republished 2023) *Educational material - Effects of climate-related matters on financial statements.*

[57] IFRS (2024) *Webcasts - Connectivity between the financial statements and sustainability-related financial disclosures.*

[58] HKICPA (2024) *Sustainability Information Centre.*

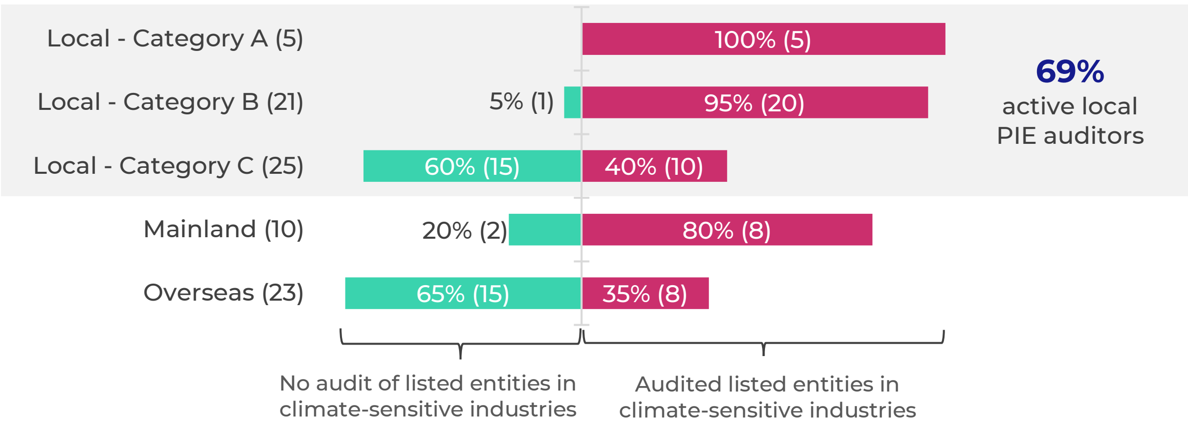
16.3. **Over half also faced challenges in quantifying the financial effects of climate-related risks (56%) and having expertise among audit partners and staff (52%).** These challenges highlight a critical need for targeted training and development programs within firms. By improving their understanding of the financial implications associated with climate change, auditors will be better equipped to provide thorough and informed assessments.

17. Providing ESG risk guidance to financial audit teams

17.1. As mentioned in paragraph 5.4, the TCFD identified five industries that are most affected by climate change. As of 30 April 2024, there were 19% (or 502) Hong Kong listed entities in these industries.[59] To gauge PIE auditors' climate-related risk vulnerability, the prevalence of audits of these entities within the engagement portfolio of 84 auditors with PIE audit engagement(s) on the same date was analysed.

Exposure to listed clients in climate-sensitive industries

Figure 33. Exposure to listed entities in climate-sensitive industries* (n=84)



17.2. Most local PIE auditors audit listed entities in climate-sensitive industries (Figure 33). **Categories A and B had the highest percentage of such clients** at 100% and 95% respectively. This was followed by PIE auditors from the Mainland (80%), Category C (40%), and overseas (35%).

[59] For this diagram, climate-sensitive industries refer to Energy, Materials, Utilities, and Financials with reference to the Hang Seng Industry Classification System adopted by the HKEX.

17.3. Listed entities are opting for large PIE auditors with extensive resources and experience to navigate the complex sustainability reporting landscape. This preference highlights the importance of robust auditing practices in sectors heavily impacted by climate-related risks.

Guidance to assess and address climate-related risks

17.4. We surveyed PIE auditors regarding the availability of firm resources and support for audit teams to adequately consider and address the impact of climate change in their audits. These resources and support comprise the following five items, which are important but not exhaustive:

a. Firm-level internal resources and support

i. **Central risk assessment**: A firm-wide risk assessment to identify audit clients and engagements with heightened climate-related risks;

ii. **Firm-level quality monitoring**: Integration of the climate change factors into audit quality monitoring processes. It includes selecting engagements subject to heightened climate-related risk for engagement quality review; and

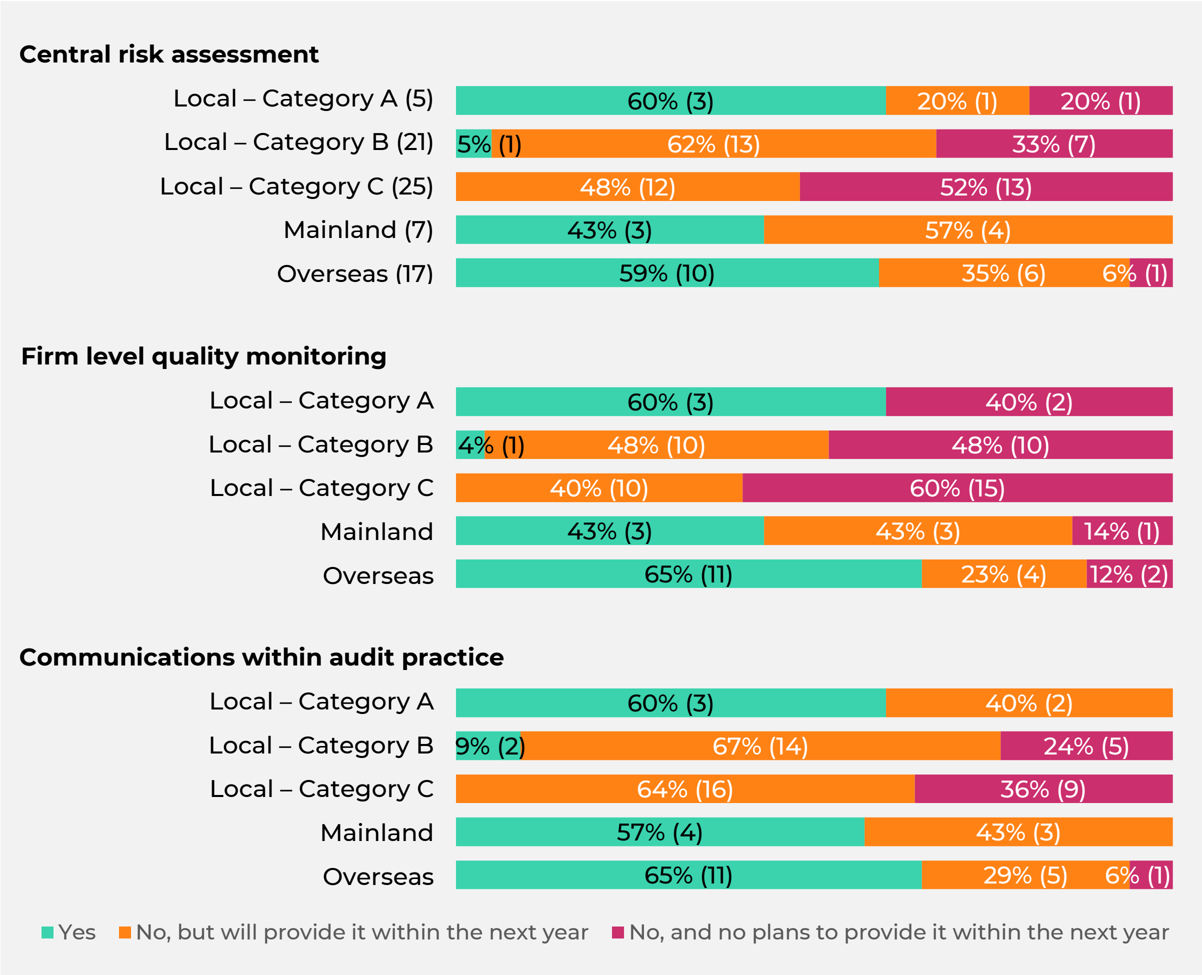
iii. **Communications within audit practice**: Regular communications, such as newsletters and practice alerts that provide guidance, requirements, and regulatory updates to audit partners and staff.

b. Engagement-level internal resources and support

i. **Risk assessment:** Guidance to consider how climate change affects audit risks so proper audit planning can be carried out; and

ii. **Substantive audit procedures:** Audit work programmes for auditing the impact of climate change on financial statements line items and disclosures, for example, on impairment testing or assumptions in valuation.

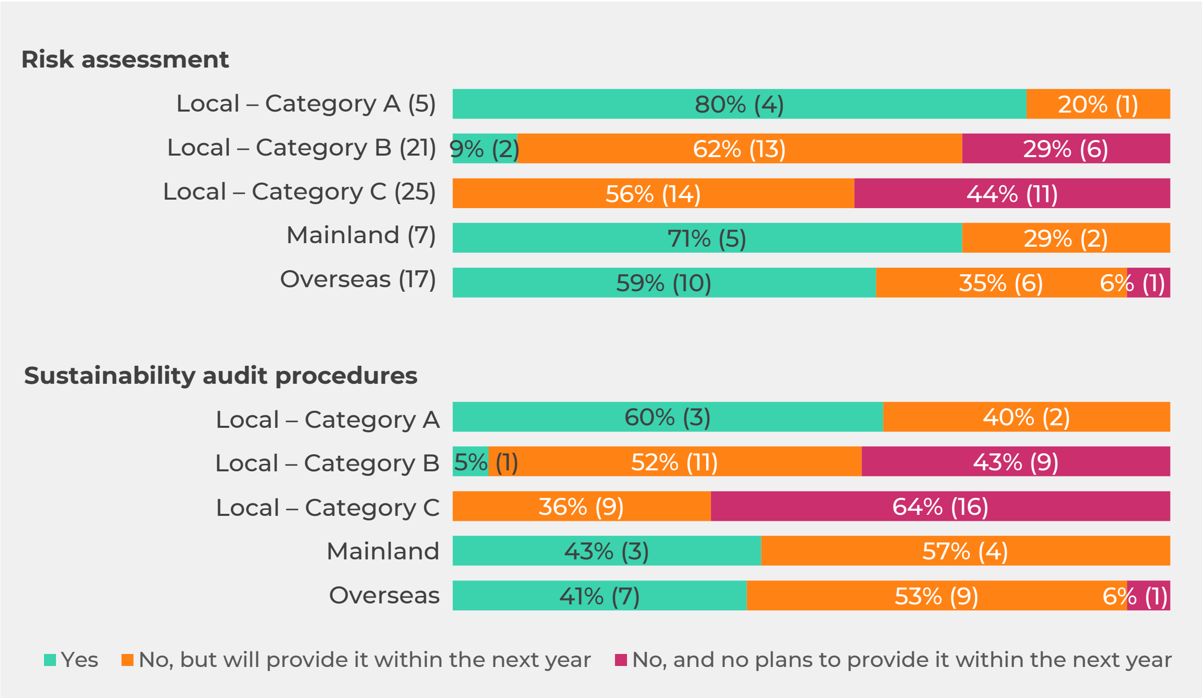
Figure 34. Availability of firm-level support (n=75)



17.5. **A high percentage of PIE auditors surveyed from Category A (60%), the Mainland (43% - 57%), and overseas (59% - 65%) provided firm-level resources and support** (Figure 34). 4% to 9% of Category B auditors provided firm-level resources and support, and represents an area of improvement.

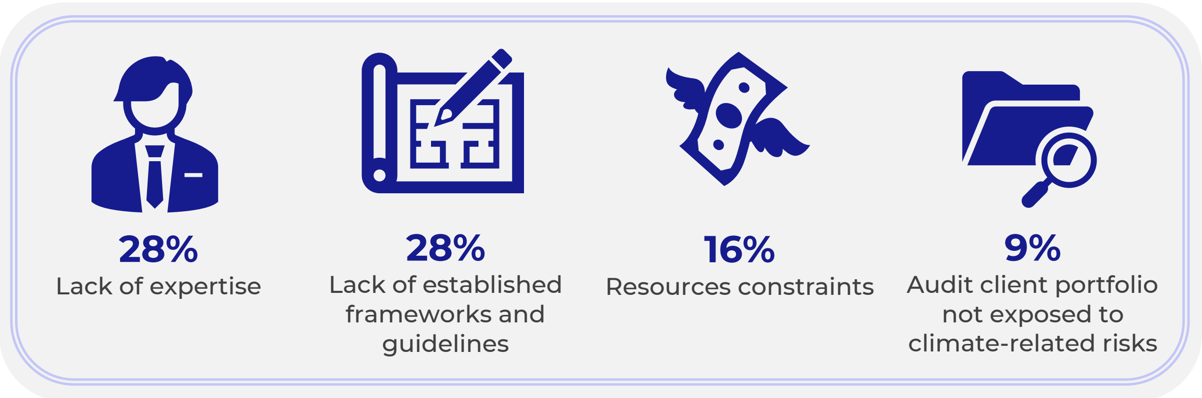
Essential for quality management, firm-level resources and support empower auditors to identify and monitor significant climate risks in their audits. Regular communications, such as newsletters and practice alerts, keep audit partners and staff informed of expectations and available resources.

Figure 35. Availability of engagement level support (n=75)



17.6. Similar to the trend identified on firm-level resources and support, **a high percentage of PIE auditors from Category A, the Mainland, and overseas have access to relevant engagement-level internal resources and support** (Figure 35).

Figure 36. Barriers to providing internal resources and support (select all that apply) (n=32)



17.7. Figure 36 shows the reasons cited by those who have no plans to provide any of the five above mentioned firm-level and engagement-level internal resources. **Lack of expertise and the lack of established frameworks**

and guidelines on accounting for and auditing climate-related risk are the most common reasons, both cited by 28% of respondents.

17.8. As noted in Section 15, some auditing standards already require auditors to consider climate-related issues in their audits. These resources assist audit teams in ensuring that climate change is considered in their risk assessment process and planned audit work, as well as in evaluating its impact on specific audit areas. These resources will improve the consistency of audit teams in identifying, considering, and responding to climate-related risk in their audits. As such, PIE auditors, especially those belonging to Categories B and C, should develop firm and engagement level resources to facilitate the integration of climate-related risks into audits.

Guidance relating to “other information”

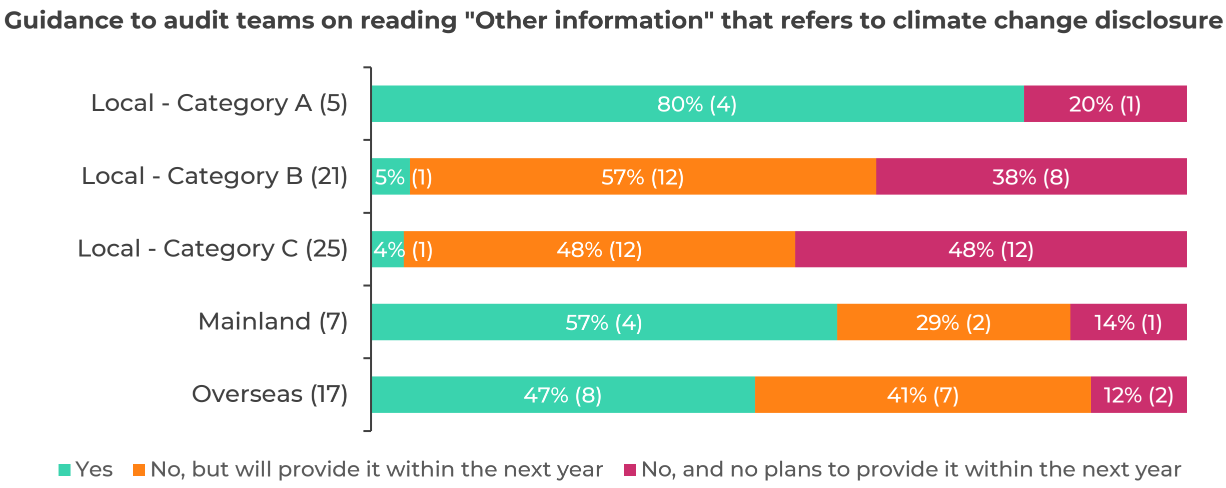
17.9. “Other information” describes the additional financial and non-financial information included in an entity’s annual report alongside the financial statements and the auditor’s report. While “other information” does not fall within the scope of the audit opinion and no assurance is provided by the auditor on it, the auditor should read it to identify material inconsistencies with the audited financial statements and any knowledge obtained during the audit.

17.10. With climate reporting requirements continuing to evolve, audit teams will need guidance to evaluate whether appropriate disclosures have been made and are consistent with the audited financial statements. We asked PIE auditors about whether internal resources and support regarding climate-related “other information” are made available in terms of:

a. **Guidance on climate-related information to be reported in “other information”:** This guidance, when updated regularly, will assist the team to understand the latest climate reporting requirements related to the nature of the entity (e.g. listing rules) and industry; and

b. **Guidance to audit teams on reading “other information” that refers to climate change disclosure:** Audit teams should be reminded to pay attention to climate change disclosure when reading “other information”.

Figure 37. Availability of internal resources by category (n=75)



17.11. The results in Figure 37 align with those regarding firm resources and support for auditing financial statements in Figure 34. **A high percentage of PIE auditors from Category A (80%), the Mainland (57%), and overseas (47%) have access to the relevant internal resources regarding climate-related “other information”.**

17.12. 4% and 5% of Category B and C PIE auditors provided any guidance to the audit teams. Among those that did not provide any guidance, this was attributed to a lack of established frameworks and guidelines on accounting for and auditing climate-related risks (50%).

17.13. As we noted earlier, there are valuable resources already available from standard setters, such as the IAASB’s Staff Audit Practice Alert and IFRS’s Educational material and webcast series. These resources serve as essential references for auditors on applying existing auditing and financial reporting standards to climate change considerations, while also emphasising the connection between financial statements and sustainability-related disclosures.

17.14. Starting from 1 January 2025, all Hong Kong listed entities will be subject to the enhanced CRD requirements in phases, and such disclosure will form part of “other information” if they are disclosed as part of annual report. Timely development of guidance will assist audit teams to remain informed about these developments and in discharging their responsibility.

18. Building ESG-competent financial audit teams

18.1. We are also interested in understanding how PIE auditors plan to enhance their competency in auditing climate change through investments in human capital and training, and to develop specialised knowledge and expertise among their audit teams. The areas of interest include:

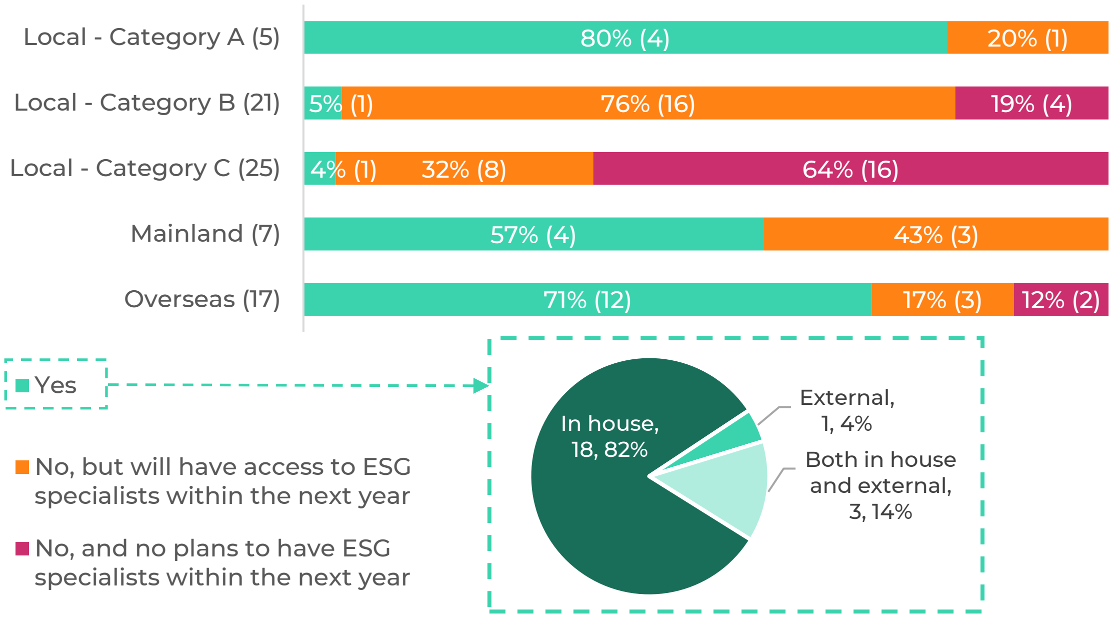
a. Use of ESG specialists and the support they offer;

b. Offering of climate and other ESG-related Continuing Professional Development (**CPD**) training for audit partners and staff; and

c. Consideration of climate and ESG-related qualifications, experience and/or expertise in recruitment of audit partners and staff.

Technical support by ESG experts

Figure 38. Use of ESG specialists (n=75)



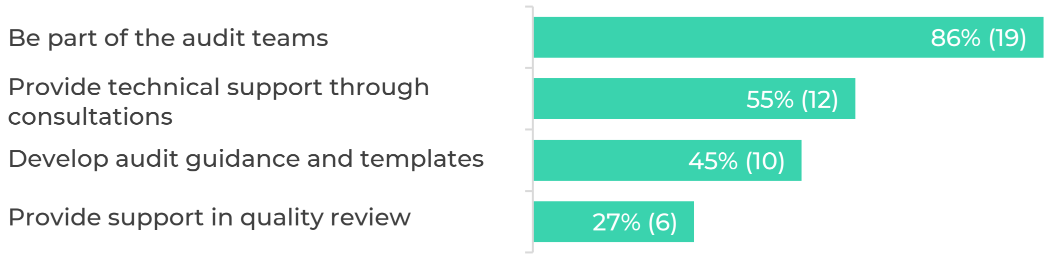
18.2. As shown in Figure 38,

a. **a high percentage of PIE auditors in Category A (80%), the Mainland (57%), and overseas (71%) made use of ESG specialists**.

b. Among those with access to ESG specialists, 82% indicated that these specialists are in-house experts.

c. Further, all remaining Category A and Mainland PIE auditors expect to have access to ESG specialists within the next year. In contrast, only 5% of Category B and 4% of Category C auditors have access to ESG specialists currently. Among those with access, 82% indicated that these specialists are in-house experts.

Figure 39. Support provided by ESG specialists (select all that applies) (n=22)



18.3. The primary types of support provided by ESG specialists over the past year include the provision of assistance to audit teams (86%) and providing support through technical consultations (55%). 45% engaged ESG specialists in developing audit guidance and templates or in audit quality reviews (27%). These areas represent opportunities for leveraging the specialists' capabilities in ways that could significantly enhance audit processes and outcomes (Figure 39).

Combining diverse and expert skills leads to effective audit outcomes. Involving ESG specialist enhances audit quality and ensures a thorough evaluation of climate-related risks in financial audits.

Figure 40. Reasons for not planning to have ESG specialists within the next year (n=22)

18.4. Among the 22 PIE auditors with no plans to have ESG specialists within the next year, **their key hurdles were the lack of financial resources (77%), followed by the inability to identify or recruit the relevant expertise (55%)** (Figure 40).

18.5. In our stakeholder conversations, firms highlighted challenges in recruiting staff with relevant working experiences and educational background/qualifications, especially at the middle-levels. To attract talent, the Hong Kong government includes experienced professionals in ESG, including those involved in standard setting, performance verification and certification as part of its talent list.[60]

ESG training for audit teams

18.6. As emphasised in the AFRC's publication on CPD, an effective CPD programme helps audit professionals stay abreast of emerging industry trends, regulatory changes, and best practices.[61] It will also communicate available resources and support to audit teams to improve consistency in applying firm specific methodology for climate-related matters. In this context, the survey inquired about the CPD training in climate and other ESG-related topics provided to audit partners and staff.

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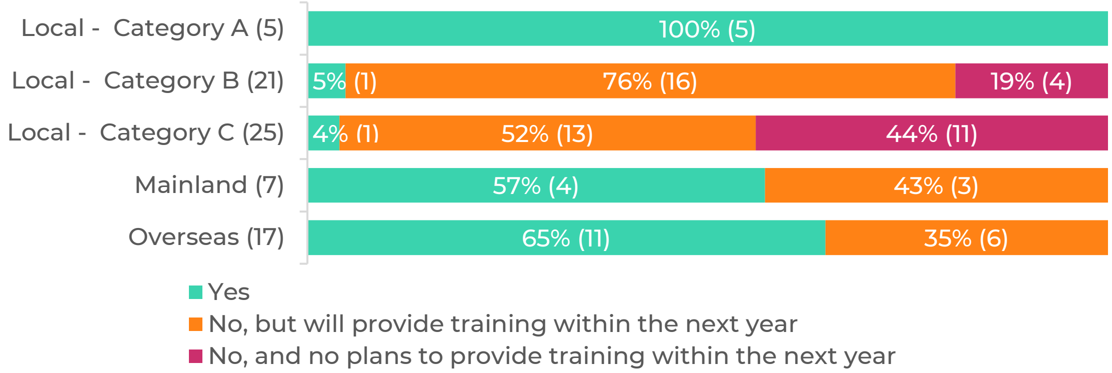
[60] Talent List Hong Kong. *Experienced professionals in Environmental, Social and Governance (ESG) (other than financial professionals) Business Support.*

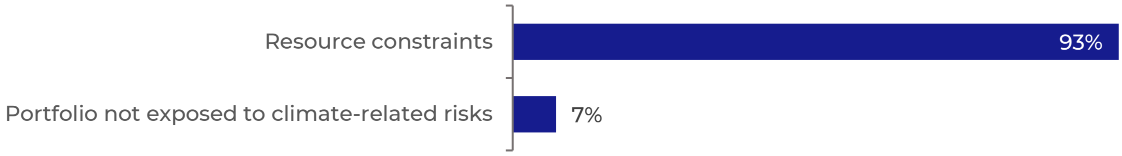
[61] AFRC (2024) *Continuing Professional Development as a Key to Improving Audit Quality in Hong Kong.*

Figure 41. Provision of ESG-related training to audit partners and staff (n=75)



18.7. All Category A, the Mainland and overseas PIE auditors are currently providing, or will provide, climate and other ESG-related CPD training within the next year (Figure 41). However, only 5% of Category B and 4% of Category C auditors have already incorporated ESG topics in their CPD programme for their audit partners and staff.

Figure 42. Reasons for not providing ESG-related training to audit partners and staff within the next year (n=15)



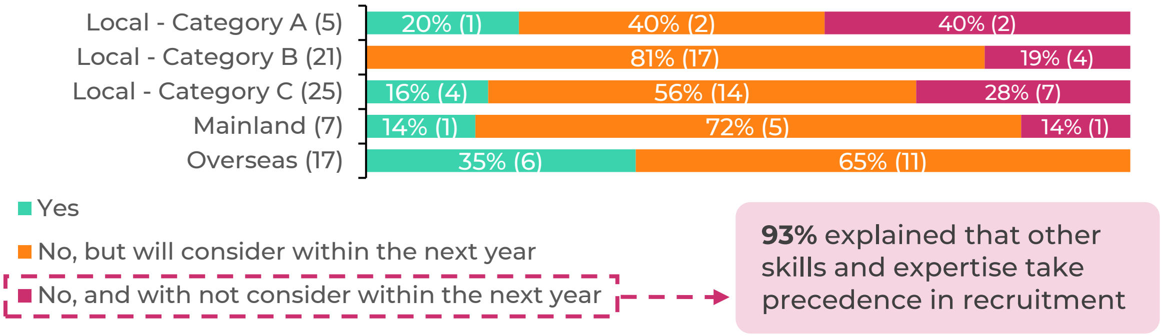
18.8. **For those that have no plans to provide any climate or other ESG-related CPD training to their audit professionals, 93% cited resource constraints** (Figure 42).

18.9. We further analysed to see if the auditors with no plans to engage ESG specialists in the next year would offer relevant training for audit professionals instead to bridge the knowledge gap. **68% of the 22 PIE auditors with no plans to engage ESG specialists in the next year, also did not plan to offer relevant training for their audit partners and staff.**

18.10. As we noted in our publication on CPD, continuous professional development needs to be outcome focused, and firms need to quantify how CPD investments not only improve audit quality, but also staff morale and retention. This is particularly relevant in the area of sustainability.

Recruitment of ESG-trained personnels

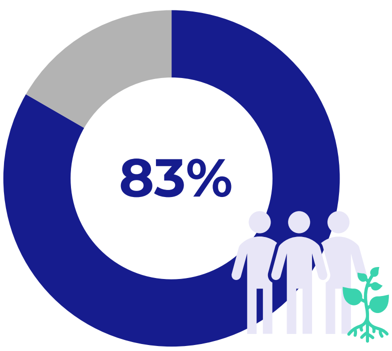
Figure 43. Consideration of ESG-related qualifications and experience when recruiting audit partners and staff (n=75)



18.11. **When asked whether they consider climate and ESG-related qualifications, experience and/or expertise in the recruitment of audit partners and staff, between 60% and 86% of local PIE auditors and the Mainland PIE auditors responded that they consider it or will consider it within the next year.** A small percentage said that they do not consider climate and ESG-related qualifications, with 93% indicating that other skills and expertise take precedence in recruitment (Figure 43).

18.12. We encourage auditors to proactively develop a comprehensive implementation plan that includes, among other elements, evaluating their readiness for CRD in relation to human resources.

Figure 44. Difficulties in recruiting audit professionals with climate-related qualifications, experience, and/or expertise (n=12)



18.13. Among the 12 PIE auditors that intended to recruit audit professionals with ESG qualifications, experience and/or expertise, **83% experienced**

difficulties (Figure 44). **Some highlighted the lack of ESG expertise in the market, particularly among those with an accounting background**.

> **Guidance, resources, and support can empower auditors to address emerging challenges.** Smaller PIE auditors are strongly encouraged to assess the sufficiency of their resources to support financial audit teams to identify and address climate-related risks.

19. Consideration of ESG expertise in auditor selection

19.1. We asked listed entities to rank the importance of the five auditors' competencies below when selecting auditors:

a. ESG-related factors

i. Climate change and other environmental impact; and

ii. Impacts arising from the Social and Governance pillars of "ESG".

b. Non-ESG-related factors

i. Impacts arising from economic challenges (e.g., high interest rates and inflationary pressure, fraud risks);

ii. Use of emerging technologies to improve audit efficiencies; and

iii. Cybersecurity risks.

19.2. While listed entities would consider these competencies in their auditor selection, we are particularly interested in the ranking of ESG-related competencies relative to other factors. This is especially relevant for listed entities in industries more susceptible to climate change, as we expect them to place greater emphasis on ESG-related competencies when selecting their auditors.

Figure 45. Percentage of listed entities ranking auditors' competencies in "climate change and other environmental impact" the fourth or fifth in importance during auditor selection by industries (n=797)

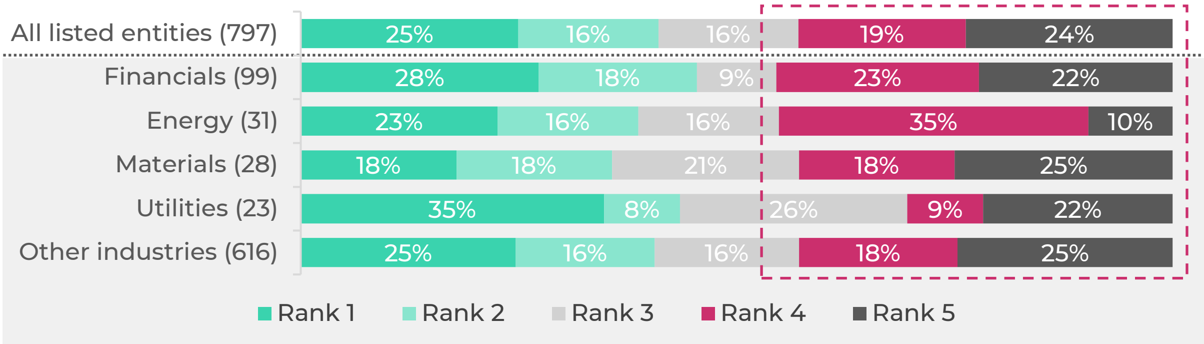
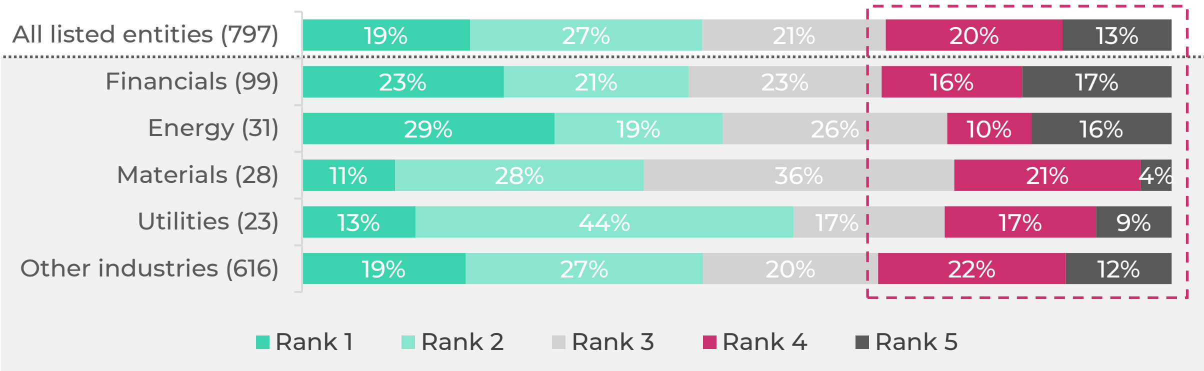


Figure 46. Percentage of listed entities ranking auditors' competencies in "impacts arising from social and governance pillars of ESG" the fourth or fifth in importance during auditor selection by industries (n=797)



19.3. Figures 45 and 46 show the proportion of listed entities that rank auditors' expertise in "climate change and other environmental impacts" and "impacts arising from social and governance pillars of ESG" as less critical compared to other factors during the auditor selection process. It compares climate-sensitive industries against other industries, aiming to evaluate if those in more vulnerable sectors sufficiently recognise and prioritise their risk exposures in their selection criteria.

19.4. Listed entities consider auditors' climate-related expertise alongside other topics in auditor selection, with the respondent rankings evenly distributed. **There is an opportunity for listed entities in climate-sensitive industries to prioritise auditors' climate-related expertise,**

with over 40% of them ranking them fourth or fifth in importance among five areas.

The road to enlightenment begins with awareness and education.

We encourage listed entities to elevate their awareness regarding the importance of an auditor's expertise on climate and other ESG matters during the auditor selection process.

Financial auditors also have a role to educate their clients on the impact climate change and other ESG factors may have on financial reporting and, by extension, their audits.

Glossary

This glossary provides definitions of the acronyms, abbreviations, and key terms used in this report:

AA1000AS	AccountAbility 1000 assurance standard
AICPA	Association of International Certified Professional Accountants
CASG	Green and Sustainable Finance Cross-Agency Steering Group
CIMA	The Chartered Institute of Management Accountants
CPA	Certified Public Accountant
CPD	Continuing Professional Development
CRD	Climate-related Disclosures
ESG	Environmental, Social, and Governance
FSTB	Financial Services and the Treasury Bureau
GHG	Greenhouse Gases. *GHG Protocol defines:* • ***Scope 1*** *GHG emissions are direct emissions from owned or controlled sources.* • ***Scope 2*** *are indirect emissions from the generation of purchased energy.* • ***Scope 3*** *are all indirect emissions (not included in Scope 2) that occur in the value chain, including both upstream and downstream emissions.*
HKEX	Hong Kong Exchanges and Clearing Limited
HKFRS	Hong Kong Financial Reporting Standards
HKICPA	The Hong Kong Institute of Certified Public Accountants
HKSAR	Hong Kong Special Administrative Region
HSI	Hang Seng Index
IAASB	International Auditing and Assurance Standards Board
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
ISAs	International Standards on Auditing
ISAE	International Standard on Assurance Engagements
ISSA	International Standard on Sustainability Assurance
ISSB	International Sustainability Standards Board

ISSB Standards	ISSB (2023) IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and IFRS S2 *Climate-related Disclosures*
Large-, Mid- and Small-cap	For the purpose of this report, listed entities were sorted categorised by market capitalisation as of December 2023 into three tiers with broadly equal numbergroups based on their market capitalisation as of 29 December 2023. • ***Large-cap*** *comprises listed entities with individual market capitalisation exceeding HK$1,400 million. We received 278 responses from a total of 868 Large-cap listed entities;* • ***Mid-cap*** *comprises those listed entities with market capitalisation between HK$210 million and HK$1,400 million. We received 253 responses from a total of 874 Mid-cap listed entities; and* • ***Small-cap*** *comprises those listed entities with market capitalisation below HK$210 million. We received 266 responses from a total of 867 Small-cap listed entities.*
PAEs	Publicly Accountable Entities
PIE	Public Interest Entity
Roadmap	Roadmap on Sustainability Disclosure in Hong Kong
SCATF	Sustainability and Climate Action Task Force
TCFD	Task Force on Climate-related Financial Disclosures

Contacts

If you have any enquires or comments, please feel free to contact us.

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