

18 June 2021

Hong Kong Exchanges and Clearing Limited

8/F, Two Exchange Square
8 Connaught Place
Central, Hong Kong

ASIFMA AMG Response to Consultation Paper on Review of Corporate Governance Code and Related Listing Rules

The below responses will be submitted to the Hong Kong Exchanges and Clearing Limited (“HKEx”) online system on or before 18 June 2021.

Q1. Do you agree with our proposal to introduce a CP (i.e. Code Provision under the Corporate Governance Code) requiring an issuer’s board to set culture in alignment with issuer’s purpose, values and strategy?

On behalf of the Asset Management Group (“AAMG”) of Asia Securities Industry & Financial Markets Association (“ASIFMA”), we express the views of our members which are predominantly global asset managers. We welcome the proposed changes to the Corporate Governance Code as steps in the right direction.

We agree with this proposal given the importance of the board in setting the appropriate culture in alignment with an issuer's values, business strategy and purpose. A company’s culture is critical in shaping the attitude and conduct of its employees. The board should define the company’s culture and communicate it to its stakeholders. When talking about culture, investors are ultimately most keen on ensuring value creation for shareholders.

Q2. Do you agree with our proposal to: (a) introduce a CP requiring establishment of an anti-corruption policy; and (b) upgrade a RBP (i.e. Recommended Best Practice) to CP requiring establishment of a whistleblowing policy?

We agree with both proposals and suggest that issuers describe the effectiveness of its whistleblowing and anti-corruption policy, as such policies enhance corporate culture. Globally there have been increased expectations on an outcomes-based measurement. In the UK, the revised 2020 Stewardship Code placed a strong focus on activities and outcomes of stewardship. We believe this will be the trend in future and suggest HKEx consider requiring disclosure of outcomes-oriented metrics and measurement policies.

DEVELOPING ASIAN CAPITAL MARKETS

Q3. Do you agree with our proposal to introduce a CP requiring disclosure of a policy to ensure independent views and input are available to the board, and an annual review of the implementation and effectiveness of such policy?

Ensuring independent views and inputs are available to the board is important. But what is critical is to ensure that the independent views and inputs are considered and discussed by the board. To help achieve this, we see the need for board evaluation.

Currently, having regular board evaluation is an RBP. We suggest upgrading this to a CP and requiring the disclosure of the following board evaluation items in the annual report:

- the purpose and areas of evaluation;
- how the evaluation was conducted;
- the criteria used for evaluation;
- findings from the evaluation; and
- actions recommended by the evaluators.

We believe the above measure will be more effective than just the proposed policy disclosure.

Q4. a) Do you agree with our proposal regarding re-election of Long Serving INEDs to revise an existing CP to require (i) independent shareholders' approval; and (ii) Additional Disclosure?

We strongly support both proposals. This will align HKEx with the practices of other major exchanges around the world for the re-election of long-serving independent directors.

Long tenure is a major problem for INEDs as their independence can increasingly be called into question; we are glad to see the HKEx addressing this in the proposals. This, however, falls short of our members' desire for the adoption of a lead independent director ("LID") – a role that is already recognised in other developed markets including Singapore (see our response to Question 4b) for more details).

We would also urge HKEx to exercise stricter requirements for nomination and appointment of INEDs and to consider the following measures:

- 1) A non-independent Chair of the Board should not chair the Nomination Committee. Since the CEO is a key person to be monitored by INEDs, the CEO should also not be the person nominating INEDs.
- 2) INED nominees should not hold too many cross-directorships or have significant links with other directors through involvement in other companies or bodies.
- 3) Neither exemptions nor discretion should be allowed for the appointment of INEDs who have specific relationships or external factors that make their independence questionable.

b) Do you agree with our proposal to introduce a CP requiring an issuer to appoint a new INED at the forthcoming AGM where all the INEDs on the board are Long Serving INEDs, and disclosing the length of tenure of the Long Serving INEDs on the board on a named basis in the shareholders' circular?

We agree with the proposal, as this can ensure that the composition of the board is regularly refreshed and new perspectives introduced. Furthermore, we suggest that additional new INEDs be appointed in subsequent AGM(s) should long-serving INEDs continue to form a majority among the INEDs. In the future, we suggest that HKEx consider the mandatory retirement of an INED who has been serving on a board for 10 years or longer.

We also look to HKEx and organisations like The Hong Kong Institute of Directors to provide the necessary training of, support for and empowerment of INEDS, thereby creating a strong bench of INEDS in Hong Kong.

Lead independent director ("LID") or Independent Chair

The appointment of a LID is advocated for by the International Corporate Governance Network and Council of Institutional Investors. Both are established international investor-led organizations that promote effective standards of corporate governance and investor stewardship. Regulators in other Asian markets, such as Singapore and Malaysia, have adopted or are promoting the concept of a LID or senior independent director.

The major reason for instituting the role of a LID or senior independent director is to provide a clear point of contact and accountability for shareholders, especially when a lot of companies' boards in Hong Kong have the dominating presence of a controlling shareholder or founding family. The lead or senior independent director also acts as a moderator between the independent directors and other board members as well as senior management executives, which strengthens the independent voices of the board, rather than creating a hierarchy among INEDs. Where LIDs are in place, our members sometimes see the position being rotated amongst incumbent INEDs on an annual basis, which they believe undermines the effectiveness and accountability of the LID.

In the long run, our members would thus like to see the appointment of LID, especially with measures in place to ensure that the role is held by a director for a sufficient amount of time to build the necessary relationships, skills and expertise for the initiative to be effective. Recognising the issues mentioned in paragraph 101 of the consultation paper and that Hong Kong companies may not find the idea of a LID palatable at the moment, we suggest that the Chair be an independent director as a transitional measure.

Other recommendations

To help improve the effectiveness of the board and advance Hong Kong's corporate governance standards, we have two other recommendations which are not in the current proposals:

- 1) Mandatory disclosure of the length of tenure of all INEDs on the board on a named basis in the shareholders' circular and the annual report. The additional information helps investors evaluate the independence of board members and the need for refreshment of the board's composition.

- 2) Adding a new CP or RBP about independent representation in the board. While currently the listing rules mandate at least one-third of the board being independent, greater independent representation should be considered under the following conditions: i) if the Chair and CEO role is combined, ii) the Chair and CEO are family members, or iii) the Chair is non-independent.

Q5. Do you agree with our proposal to introduce a new RBP that an issuer generally should not grant equity-based remuneration (e.g. share options or grants) with performance-related elements to INEDs as this may lead to bias in their decision-making and compromise their objectivity and independence?

We support the proposal that an issuer generally should not grant equity-based remuneration, especially options, with performance-related elements to INEDs, although we are not opposed to the grant of stock (not options) in lieu of cash. We would also not recommend the grant of remuneration with time-based elements.

More importantly, we would highlight that independent director's pay for public companies listed on the Stock Exchange of Hong Kong is generally considered to be relatively low. A finding of a consultation conducted by the Hong Kong Monetary Authority in 2016 was that a basic fee of at least HK\$400,000 per year would be appropriate for INEDs (<https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2016/20161214e1.pdf>). Fees at relatively low levels may discourage quality candidates from taking a board director position or indirectly result in the overboarding phenomenon (i.e. directors serving on multiples boards simultaneously). We encourage the HKEx to conduct a follow-up review of the independent directors' compensation and add an RBP under the CG Code to encourage competitive compensation for attracting quality independent directors.

Q6. a) Do you agree with our proposal to highlight that diversity is not considered to be achieved by a single gender board in the note of the Rule?

We strongly agree that any 'single gender board is not acceptable'. A single-gender board can signal a company's lack of commitment and attention to board diversity, which ultimately can affect board effectiveness. We, however, do not believe that diversity is solely represented by gender, but more importantly encapsulates diversity of skills, views and experience, which should also be recognised in the Rule.

Under the current proposal, after the revised Rules become effective, existing issuers with single gender boards will be allowed a three-year transition period to appoint at least a director of the absent gender. Quality board candidates, in this case 'absent gender' females highlighted in the consultation, may hesitate to join such boards due to a perceived lack of commitment to diversity. Yet, we still see the transition period being too long and suggest it should be shortened to less than two years. We believe that listed issuers are generally able to fill even CEO positions in significantly less time.

Separately, the use of euphemisms such as 'single gender board' and 'absent gender', rather than 'all-male board' and the lack of females on such boards, may dilute the severity of the issue HKEx is attempting to tackle.

b) Do you agree with our proposal to introduce a MDR (i.e. Mandatory Disclosure Requirement) requiring all listed issuers to set and disclose numerical targets and timelines for achieving gender diversity at both: (a) board level; and (b) across the workforce (including senior management)?

We welcome the HKEx's progressiveness in proposing mandatory time-bound quantitative targets for achieving gender diversity both on the board level and across the workforce which we believe would be very effective in this regard.

More specifically, at the board level, we would suggest that there be gender diversity targets related to INEDs, at least in the short-term. The rationale for this comes from the experience in India, where the Company Act 2013 mandated at least one female board director. Many family-controlled companies treated it as a box-ticking exercise and responded with the appointment of female family members of promoters. In 2018, The Securities and Exchange Board of India subsequently mandated the top 1,000 listed companies to have at least one independent female director by 2020. Given the prevalence of family-controlled issuers in Hong Kong, we would suggest that HKEx pre-emptively avoids a similar situation from occurring through establishing INED gender diversity targets in the short-term.

Ultimately, however, our members would like to see companies focusing on reaching 30% female representation on both the board and across the workforce (including senior management) in the medium term.

c) Do you agree with our proposal to introduce a CP requiring the board to review the implementation and effectiveness of its board diversity policy annually?

We agree with this proposal. We recommend issuers to include an annual review of the implementation and effectiveness of its board diversity policy as part of a board evaluation process, as mentioned in our responses to Question 3. Specifically, we recommend that HKEx add in this CP the recommendation of increasing the number and percentage of female INEDs to ensure that issuers make genuine effort in promoting gender diversity on the board.

d) Do you agree with our proposal to amend the relevant forms to include directors' gender information?

Gender is only one aspect when we consider diversity. Beyond gender, some of our members recommend details of how an INED's skills and experience contribute to the board is disclosed (including disclosure of a board skills matrix so investors can understand what skills each director is contributing to the board), whilst other members would like to see ethnicity and nationality being disclosed.

We also recommend HKEx promote and encourage the disclosure of multi-dimensional diversity in not only the board but also the workforce of issuers.

Q7. Do you agree with our proposal to upgrade a CP to Rule requiring issuers to establish a NC (i.e. Nomination Committee) chaired by an INED and comprising a majority of INEDs?

We agree with the upgrade. Our members strongly support making the nomination committee mandatory, with similar 'status' as the audit and remuneration committees. A majority

independent nomination committee chaired by an INED can ensure a good balance of insights. This is in line with other Asian market practices, such as China, Singapore, Malaysia and Thailand.

Q8. Do you agree with our proposal to upgrade a CP to a MDR to require disclosure of the issuer’s shareholders communication policy (which includes channels for shareholders to communicate their views on various matters affecting issuers, as well as steps taken to solicit and understand the views of shareholders and stakeholders) and annual review of such policy to ensure its effectiveness?

We agree with this upgrade, but we believe it falls short of ensuring actual accountability and genuine communication with shareholders. To avoid this becoming a box-ticking exercise, we suggest the MDR to require issuers to disclose actions taken or to be taken following the annual review of the policy. This is to ensure that issuers will ‘walk the talk’. In particular, we look forward to issuers’ engagement with investors beyond the topic of financial results and we encourage regular engagement opportunities with the board and senior executives. This is important especially as we see the board owning the ultimate responsibility and oversight of material matters including ESG matters.

In our view, INEDS are accountable to all shareholders and an independent director, whether a LID or independent Chair, should be easily accessible to shareholders where possible, unencumbered by internal restrictions. A LID or independent Chair should be a key stakeholder in an issuer’s shareholders communication policy. We understand the pushback for the appointment of a LID. But, as stated in our response to Question 4, we consider this role important for companies, particularly those without an independent Chair. We reiterate that the rise in the appointments of LIDs globally reflects the demand of investors.

Q9. Do you agree with our proposal to introduce a Rule requiring disclosure of directors’ attendance in the poll results announcements?

We agree with this proposal as it is often a sign of directors’ commitment to the company. However, attendance is not the only indicator. Many Hong Kong-listed companies have directors who sit on many boards. Based on HKEx data as at 15 April 2021, there are more than 60 directors who are sitting on more than six public boards, with 17 directors sitting on between 10 and 19 public boards. These are unhealthy figures which we believe HKEx should address during this consultation process.

A number of studies including ‘Director Overboarding: Global Trends, Definitions, and Impact’ conducted by ISS Analytics (<https://www.isscorporatesolutions.com/library/director-overboarding-global-trends-definitions-and-impact/>) indicated correlation between overboarding and board underperformance.

According to some of our members’ corporate governance principles and proxy voting guidelines, we would not normally expect a non-executive director to hold more than three significant directorships at any one time, or six directorships for a related group company. In addition to directors’ attendance, we also urge the HKEx to consider requesting for the disclosure of the number of public boards and their respective roles in the poll results announcement.

Q10. Do you agree with our proposal to delete the CP that requires issuers to appoint NEDs for a specific term.

No comment.

Q11. Do you agree with our proposal to elaborate the linkage in the Code by (a) setting out the relationship between CG and ESG in the introductory section; and (b) including ESG risks in the context of risk management under the Code?

We agree with this proposal.

Given the Hong Kong Green and Sustainable Finance Cross-Agency Steering Group commitment to the recommendations of the Task Force on Climate-related Financial Disclosures (“TCFD”), we also recommend that HKEx formulate and disclose a specific timeline for implementing TCFD.

Q12. Do you agree with our proposal to amend the Rules and the ESG Guide to require publication of ESG reports at the same time as publication of annual reports?

Yes, as we believe it would further encourage companies to embed ESG considerations in their business strategy.

Q13. Do you have any comments on how the re-arranged Code is drafted in the form set out in Appendices III and IV to this paper and whether it will give rise to any ambiguities or unintended consequences?

No comment.

Q14. In addition to the topics mentioned in this paper, do you have any comments regarding what is to be included in the CG GL (i.e. Corporate Governance Guidance Letter) which may be helpful to issuers for achieving the Principles set out in the Code?

We support HKEx taking steps to promote good corporate governance and enhancing the CG Code to improve the quality of corporate governance for Hong Kong and Hong Kong listed companies. We agree with many of the proposals in the consultation paper but we see the need for HKEx to take bolder moves. We highly recommend the HKEx to consider our following suggestions:

- 1) Upgrade of board evaluation from BSP to CP
- 2) Add a new MDR for issuers to disclosure the length of tenure of all INEDs on the board on a named basis in the shareholders’ circular and the annual report
- 3) Add a new CP to require issuers’ appointment of a lead/senior independent director where the Chair of the board is non-independent
- 4) The transition period for single gender boards to appoint at least a director of the absent gender should be shortened to less than two years instead of three years as in the proposal
- 5) Add a new CP to require board independency of 50% or above for companies of which the Chair and CEO role is combined, or the Chair and CEO are family members, or the Chair is non-independent.
- 6) Director skills, gender, ethnicity and nationality should be disclosed in the relevant forms (Part 1 of Form B and Form H of Appendix 5 to the MB Rules / Part 1 of Form A and Form B of Appendix 6 to the GEM Rules)
- 7) Add a new MDR to require issuers to disclose actions taken or to be taken upon the annual review of their shareholders communication policy

- 8) Add a new CP to request for targets on increasing the number and percentage of female directors to at least 30% of the board representation

The CG GL should include guidance for any of the above suggestions taken by the HKEx.

As stated in our response to Question 2, there are growing expectations for more outcomes-based measurements globally. In the CG GL, we suggest that HKEx, in anticipating this trend, strongly encourage issuers disclose their metrics for measuring the outcomes of their policies (e.g. anti-corruption policy, whistleblowing policy, shareholders communication policy).

While Environmental and Social (E&S) factors are not the focal points for this consultation paper, we do believe that the board members are accountable for the management, strategy and governance of these factors. We suggest HKEx include in its RBP the accountability and oversight of ESG issues by the board and the setting up of a ESG committee to be chaired by a professional in the areas of ESG / sustainability development and to be joined by the Chair of the board.

Q15. Do you agree with our proposed implementation dates of: (a) for all proposals (except the proposals on Long Serving INED): financial year commencing on or after 1 January 2022; and (b) for proposals on Long Serving INED: financial year commencing on or after 1 January 2023?

We believe all proposals, including the ones related to Long Serving INEDs, should be implemented at the same time, i.e. for financial year commencing 1 January 2022. Disclosures for financial year commencing 1 January 2022 and voting on such matters will only be available in almost the second quarter of 2023. We don't see a particular reason why an additional year should be allowed for certain proposals.