

HKEX News Update: Review of Issuers' Corporate Governance Practices and New INED Guide

On 17 November 2023, the Stock Exchange published its latest review of issuers' corporate governance ("CG") practices, and a new guide for independent non-executive directors ("INEDs").

Review of issuers' CG practices (the "Review")

The Stock Exchange introduced important updates to the CG Code ("**CG Code**") on 1 January 2022 (the "[2022 Update](#)").

The [Review](#) focused on the CG reports of 400 randomly selected issuers (Sample Issuers) for the 2022 financial year. It focused, in particular, on issuers' compliance with some of new requirements arising from the 2022 Update.

Key findings and recommendations from the Review include:

(a) Corporate culture

- The **2022 Update** introduced a new Code Provision ("**CP**") and provided guidance highlighting the board should establish the issuer's purpose, values and strategy, and ensure that these and the issuer's culture are aligned. All directors must act with integrity, lead by example, and promote the desired culture ^(Note 1);
- Full compliance of all Sample Issuers;
- A **comprehensive disclosure** would include details of aspects considered by the board and directors in their assessment of alignment between the issuer's purpose, values and strategy with its culture, steps taken to implement the desired culture throughout the organization, their organizational values, and how the organizational values are aligned with long-term business goals; and
- **Cross references** should be included in the CG Report if these disclosures are made outside of the CG Report.

(b) INEDs who have served more than nine years ("**Long Serving INEDs**")

- The **2022 Update** introduced that issuers with all Long Serving INEDs should (i) disclose the length of tenure of each Long Serving INED; and (ii) appoint a new INED at the forthcoming annual general meeting ^(Note 2);
- Meaningful reduction of issuers with all Long Serving INEDs on the board;
- In respect of the **re-election of a Long Serving INED**, issuers should disclose the factors considered in determining suitability for re-election, the process (i.e. steps taken by the nomination committee and the board) and related discussions;
- The **Main Board Listing Rule 3.13 (GEM Listing Rule 5.09) Independence Criteria** primarily focuses on a director's actual or potential conflict of interests ^(Note 3), and not a director's ability to bring fresh perspective and independent judgment;
- When **assessing a director's continued suitability** for the role, the board (or the nomination committee) should focus on the INED's mindset and whether the INED remains capable of continuing to provide an independent and objective contribution; and
- **Board evaluations** and a **board skills matrix** are useful tools to help identify a board's existing skillsets and bring any gaps to the board's attention to support the retention of Long Serving INEDs, board refreshment and succession planning.

(c) Diversity

- In January 2022, the Stock Exchange put **an end to single gender boards** by requiring issuers to appoint at least a director of a different gender on the boards no later than 31 December 2024 ^(Note 4);
- **The 2022 Update** also introduced requirements for (i) an annual review of board diversity policies; (ii) the setting of numerical targets and timelines for achieving gender diversity at board level; and (iii) disclosure of gender diversity-related matters at workforce level ^(Note 5);
- High level of compliance except regarding the requirement to disclose numerical targets and timelines for achieving board gender diversity;
- **Remaining single gender board issuers** should proactively seek to appoint at least one director of a different gender and not wait until closer to 31 December 2024 deadline;
- **Disclosures** should include details of: the steps and programmes implemented by the issuer; and a discussion as to whether the issuer is on track to meet its numerical targets and timelines, and if not, what additional actions the issuer is taking to enable it to achieve its diversity goals; and
- Where there is a revision to a diversity target or deadline, issuers should provide a reasoned explanation tailored to their individual circumstances.

(d) Risk management and internal controls (“**Internal Control System**”)

- The **CG Code** requires issuers to confirm that they have reviewed the effectiveness of their Internal Control System, the frequency of such reviews and a confirmation that the Internal Control System is effective and adequate. The board should oversee the Internal Control System on an ongoing basis, and to review its effectiveness at least annually ^(Note 6);
- Full compliance regarding disclosure on Internal Control Systems with confirmation of systems’ effectiveness by most Sample Issuers; and
- **Good Disclosures** should include (i) structure and processes of the Internal Control Systems (key individuals and departments responsible for such systems); (ii) particular risks (principal/emerging) including fraud and/or ESG related risks considered; and (iii) process for regular monitoring and reviews.

(e) Separation of roles of chairman and chief executive

- The **CG Code** provides that the roles of chairman and chief executive should be separate and should not be performed by the same individual ^(Note 7);
- The compliance rate has remained relatively static over the past three reviews (61%-64%); and
- **Disclosures of non-compliance** should focus on how the potential governance issue is effectively addressed by alternative arrangements.

(f) Omission or partial disclosure of Mandatory Disclosure Requirements (“**MDRs**”)

- Issuers must **disclose all applicable MDRs** (including the sub-paragraphs of those MDRs) and must include a negative statement if they consider any of the MDRs not applicable to them in the CG Report; and
- **Cross references** should be included in the CG Report if these disclosures are made outside of the CG reports.

A new guide “[A Snapshot of INEDs’ Roles and Responsibilities](#)”

(a) The guide covers the following areas:

- Actions to take when one becomes a new INED;
- Role in the review and approval of business decisions and transactions;
- Questions to ask when a transaction or a new business is being proposed and approved;
- INED’s role in internal controls;
- INED’s role in financial reporting; and
- INED’s role in incident management.

(b) The guide also provides case studies relating to the following:

- Financial reporting issues;
- Keeping apprised of affairs of the Company / Group;
- Suspicious movement of funds and red flags;
- Prior undisclosed transactions mentioned in financial and annual reports; and
- Red flags in acquisition of new business.

To view the full details of HKEx’s news, please click [HERE](#).

Notes:

1. Code Provision (“CP”) A.1.1 of CG Code and pages 9 – 12 of the Stock Exchange’s [Corporate Governance Guide for Boards and Directors](#) (December 2021).
2. CP B.2.4 of CG Code.
3. Please refer to paragraph 31 on page 8 of the Exchange’s [Analysis of 2019 Corporate Governance Practice Disclosure](#) for the guidance on quoting Main Board Listing Rule 3.13 (GEM Listing Rule 5.09) Independence Criteria as a reason to justify the re-election of Long Serving INEDs.
4. Main Board Listing Rule 13.92 (GEM Listing Rule 17.104).
5. Paragraph J of the MDRs and CP B.1.3 of CG Code.
6. Paragraph H of the MDRs and CP D.2.1 of CG Code.
7. CP C.2.1 of CG Code.