Directors' Duties Navigator: Climate Risk and Sustainability Disclosures*

Fourth edition, September 2024

**Previously titled 'Primer on Climate Change: Directors' Duties and Disclosure Obligations'*

CCLI Commonwealth Climate and Law Initiative

Climate Governance Initiative

Hong Kong

1. Legal and Regulatory Landscape Regarding Climate Change

1.1. Government approach to climate change

1.1.1. Climate change legislation

Hong Kong does not have climate change legislation.

1.1.2. Transition plans and targets

In October 2021, the Hong Kong Special Administrative Region (**HKSAR**) Government published its Climate Action Plan 2050. The plan affirms, *inter alia*, its target of achieving carbon neutrality by 2050, states a new target of reducing carbon emissions by 2035 by 50% relative to 2005 levels and outlines the Government's strategies for decarbonisation and budgets for mitigation and adaptation.[1] Hong Kong's Climate Action Plan 2050 may have substantial impacts on the operations of Hong Kong corporations, in particular those which are in or are closely connected to high-emission sectors.

Hong Kong does not have a national transition and adaptation plan. However, in August 2023, the Hong Kong Monetary Authority (**HKMA**) issued a circular outlining high-level principles on planning for the transition to a net-zero economy to banking institutions under its supervision.[2] Particularly, this circular noted that international disclosure requirements were expected to require reporting of certain information regarding transition plans, and it therefore emphasized that all HKMA 'authorised institutions'[3] should consider enhancing the transparency of their transition planning process and/or transition plans.[4]

In addition, the Green and Sustainable Finance Cross-Agency Steering Group (the **Steering Group**), which is co-chaired by the Hong Kong Securities and Future Commission (**SFC**) and the HKMA and includes several Government agencies, was established in 2020 to coordinate the management of climate and environmental risks to the financial sector and to accelerate the growth of green and sustainable finance.

1.1.3. Wider government approach to climate change

The Budget for FY 2023-24 highlights that Hong Kong is well-positioned to establish itself as an international green technology and financial centre due to its accumulated expertise and talent in innovation and technology development, particularly in green tech.[5]

The HKSAR Government has been proactive in promoting green technology, exemplified by the establishment of the Green Tech Fund (**GTF**) and its leadership in green finance. In February 2023, Hong Kong issued an HKD 800 million tokenized green bond, the first of its kind globally, highlighting its flexible legal and regulatory environment for innovative bond issuance.[6] Additionally, in January 2023, Hong Kong issued USD 5.75 billion in Government

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1 Hong Kong Special Administrative Region, 'Hong Kong's Climate Action Plan 2050' (October 2021) <https://www.climateready.gov.hk/files/pdf/CAP2050_booklet_en.pdf> 38, 59-63.

2 Hong Kong Monetary Authority, 'Planning for net-zero transition' (Ref: B1/15C, B9/197C, 29 August 2023) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2023/20230829e1.pdf>.

3 HKMA authorised institutions include deposit-taking institutions, comprising of licensed banks, restricted licence banks, and deposit-taking companies. HKMA, The three-tier Banking System, <https://www.hkma.gov.hk/eng/key-functions/banking/banking-regulatory-and-supervisory-regime/the-three-tier-banking-system/>.

4 Hong Kong Monetary Authority, 'Planning for net-zero transition' (Ref: B1/15C, B9/197C, 29 August 2023) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2023/20230829e1.pdf>, Principle 6.

5 Hong Kong Special Administrative Region, The 2023-24 Budget (22 February 2023) < https://www.budget.gov.hk/2023/eng/pdf/e_budget_speech_2023-24.pdf>

6 Hong Kong Monetary Authority, Press Release - HKSAR Government's Inaugural Tokenised Green Bond Offering (16 February 2023) < https://www.hkma.gov.hk/eng/news-and-media/press-releases/2023/02/20230216-3/>

green bonds across multiple currencies, marking the largest ESG bond issuance in Asia.[7] Since the launch of the Green and Sustainable Finance Grant Scheme in 2021, over 340 related debt instruments have been issued and have now been extended to 2027.[8]

The Budget for FY 2024-25 stated that the Financial Services, the Treasury and the SFC will formulate a roadmap and vision statement to assist companies and financial institutions in sustainability reporting and analysis of relevant data, in line with Hong Kong's vision of promoting green and sustainable finance.[9] Hong Kong's sustainability disclosure framework has been discussed in detail in the later sections.

In May 2024, the HKMA published the HK Taxonomy. It provides a standardised framework for the classification of financial products based on their environmental sustainability credentials, to inform better decision-making and facilitate green finance flows. The HK Taxonomy encompasses 12 economic activities falling under the sectors of power generation, transportation, construction, and water and waste management. The HK Taxonomy is voluntary but encouraged. The HKMA will undertake efforts to expand the HK Taxonomy to include more sectors and activities, including transition activities.[10] The HKMA has also issued detailed guidance to better equip companies to benefit from the HK Taxonomy.[11]

The Glasgow Financial Alliance for Net Zero, a global coalition of financial institutions committed to the climate transition, announced in 2023 that it will expand into Hong Kong. The Hong Kong chapter will undertake capacity-building efforts for financial institutions on net-zero efforts, transition planning and scaling transition finance.[12]

There is no carbon trading legislation in Hong Kong. However, in October 2022, the Hong Kong Stock Exchange (**HKEX**) launched Core Climate, a voluntary carbon market with international scope, to facilitate effective and transparent trading of carbon credits.[13]

In 2020, the HKSAR Government launched the Green Tech Fund (**GTF**) which has received state funding to support efforts to address climate change.[14] As of FY 2024-25, the GTF has been provided with HK$400 million in funding and 30 projects from various institutions have been funded to research technologies for the cell storage and generation of hydrogen fuel, manufacturing of biochar-enhanced construction materials, and air cleaning system for reducing roadside air pollution.[15]

In addition to green tech and green finance which remains the core focus, the HKSAR Government has highlighted other key focus areas such as green aviation, green

7 Hong Kong Monetary Authority, Press Release - HKSAR Government's Institutional Green Bonds Offering (05 January 2023) < https://www.hkma.gov.hk/eng/news-and-media/press-releases/2023/02/20230216-3/>

8 Hong Kong Special Administrative Region, The 2024-25 Budget (28 February 2023) < https://www.budget.gov.hk/2024/eng/pdf/e_budget_speech_2024-25.pdf>.

9 ibid.

10 Hong Kong Monetary Authority, 'Hong Kong Taxonomy for Sustainable Finance' (3 May 2024) < https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2024/20240503e1.pdf>.

11 Hong Kong Monetary Authority, 'Hong Kong Taxonomy for Sustainable Finance: Supplemental Guidance' (3 May 2024) < https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2024/20240503e1.pdf>.

12 Glasgow Financial Alliance for Net Zero, 'GFANZ Announces Hong Kong Chapter to Support Asia-Pacific Net-Zero Transition' (31 August 2023) <https://www.gfanzero.com/press/gfanz-announces-hong-kong-chapter-to-support-asia-pacific-net-zero-transition/>.

13 Hong Kong Stock Exchange, HKEX Launches Core Climate, Hong Kong's International Carbon Marketplace, supporting Global Transition to Net Zero (28 October 2022) <https://www.hkex.com.hk/News/News-Release/2022/221028news?sc_lang=en>.

14 Green Tech Fund <https://www.gtf.gov.hk/en/about_the_fund/about_the_fund.html>.

15 Hong Kong Special Administrative Region, The 2024-25 Budget (28 February 2023) < https://www.budget.gov.hk/2024/eng/pdf/e_budget_speech_2024-25.pdf>.

city (including electric vehicles) and green shipping in the Budget for FY 2024-25.[16]

1.2. Regulatory approaches to climate change

1.1.1. Climate change as a systemic financial risk

HKSAR regulators recognise that climate-related financial risks are foreseeable and are proactively addressing them.[17]

In November 2020, the Chief Executive of the HKMA acknowledged that "*[c]limate risk is one of the biggest threats to our planet and future generations"* and that regulators must determine how the financial sector can *"play its part in tackling this risk*".[18]

Similarly, in February 2021, speaking about the international climate finance agenda, the CEO of the SFC, warned that:

> *"International organisations, national authorities and the private sector now have no real option other than to participate. If they do not, they risk being left behind as investments shift in favour those businesses which can properly describe how they are managing the strategic risks resulting from climate change."*[19]

1.1.2. Financial regulation and guidance

<u>Financial Institutions</u>: In July 2020, HKMA, a member of the Network for Greening the Financial System (**NGFS**), issued a circular regarding best practices by major international banks in managing climate risks, as well as several other publications regarding green and sustainable finance and the pricing in of climate transition risks by banks.[20]

In June 2022 the HKMA wrote to all authorised institutions to set out its two-year plan to integrate climate risk into its supervisory role, and in December 2022, issued revisions to its Supervisory Policy Manual which included climate change as an emerging risk type which authorised institutions should consider.[21] In April 2023, the HKMA provided detailed guidelines for the banking sector regarding Climate Risk Stress Tests to test the climate resilience of HKSAR's banking system.[22]

In August 2023, the HKMA published high-level principles to support authorised institutions in preparing for the transition towards a net zero economy.[23] A summary

16 ibid.

17 Alexander Stock SC and Jennifer Fan, Legal Opinion on Directors' Duties and Disclosure Obligations under Hong Kong Law in the Context of Climate Change Risks and Considerations (19 October 2021) <https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Legal-Opinion-Hong-Kong-Directors-obligations-and-climate-change.pdf>.

18 Eddie Yue, 'Managing climate risks in Hong Kong' (9 November 2020) [3] <https://www.bis.org/review/r201109b.htm>.

19 Ashley Alder, 'Climate change and finance: What's next for the global regulators? Climate Risk and Green Finance Regulatory Forum 2021' (11 February 2021) 5 <https://www.sfc.hk/-/media/EN/files/ER/PDF/CEO_Speech_Climate-Risk-and-Green-Finance-Regulatory-Forum-2021.pdf>.

20 See Hong Kong Monetary Authority, 'Range of practices for management of climate risks' (7 July 2020) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2020/20200707e1a1.pdf>; HKMA, 'White Paper on Green and Sustainable Banking' (30 June 2020) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2020/20200630e1.pdf>; HKMA, 'Common Assessment Framework on Green and Sustainable Banking' (31 December 2019) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2020/20200513e1a1.pdf>; HKMA, 'Effect of Climate-related Risk on the Pricing of Bank Loans: Evidence From Syndicated Loan Markets in Asia Pacific' (13 August 2021) <https://www.hkma.gov.hk/media/eng/publication-and-research/research/research-memorandums/2021/RM06-2021.pdf>.

21 Hong Kong Monetary Authority, Embedding climate risk in banking supervision (30 June 2022) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2022/20220630e1.pdf>; HKMA, Supervisory Policy Manual, v.2 (23 December 2022) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2022/20221223e2a1.pdf>.

22 Hong Kong Monetary Authority, Guidelines for Banking Sector Climate Risk Stress Test (April 2023) < https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2023/20230421e1a1.pdf>

23 Hong Kong Monetary Authority, 'Planning for net-zero transition' (Ref: B1/15C, B9/197C, 29 August 2023) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2023/20230829e1.pdf>.

of these key high-level principles is provided below:

(a) *Setting clear objectives and targets*: Define clear, science-based goals aligned with the Paris Agreement. As transition planning capabilities grow, set quantitative targets using scenario analysis.

(b) *Setting up a robust governance framework and embedding transition considerations into internal processes*: Establish strong governance and embed transition considerations into internal processes, including risk management and business strategies.

(c) *Devising appropriate initiatives and actions to achieve the objectives*: Develop specific actions and milestones to achieve objectives, using relevant standards and frameworks.

(d) *Engaging with clients*: Actively engage with clients to align and support their transition pathways.

(e) *Performing reviews and updates*: Regularly update the transition plan to reflect evolving climate scenarios and sectoral pathways.

(f) *Maintaining transparency*: Enhance transparency to meet stakeholder expectations and disclosure requirements.

This circular further noted that the HKMA will continue to engage with the industry and conduct a survey on transition planning practices to share best practices. The HKMA will consider the benefits of these planning efforts when incorporating climate considerations into the Supervisory Review Process.

<u>Fund Managers</u>: In August 2021, the SFC issued amendments to the Fund Manager Code of Conduct, which require fund managers to consider climate risks (defined as physical, transition and liability risks) in their investment and risk management processes, and require managers of at least HK$8 billion in assets to make a reasonable effort to report their investees' and funds' scope 1 and 2 GHG emissions from November 2022.[24] The amendments also impose specific governance responsibilities on board- and management-level functions with respect to climate-related risks.

<u>Insurance Companies</u>: There is no specific and detailed guidance on insurance companies regarding climate-related risks. However, the Guidelines on Enterprise Risk Management (the **ERM Framework**) issued by the Insurance Authority, which regulates and supervises the insurance industry in HKSAR, requires insurance companies to: (a) routinely identify all reasonably foreseeable and relevant material risk and risk interdependencies for risk and capital management including emerging risks such as climate risk;[25] (b) implement an underwriting policy which addresses the approach and controls that identify underwriting risks including emerging risks such as climate risks;[26] and (c) review the risk management framework in light of emerging and new risks (such as climate change).[27] Further, the Insurance Authority also conducts periodic surveys to understand the industry's readiness, progress, practices and challenges in managing climate risks. In February 2024, the Hong Kong Federation of Insurers, an industry body, introduced an Insurance Industry Climate Charter to establish

24 Securities and Futures Commission, 'Circular to licensed corporations: Management and disclosure of climate-related risks by fund managers' (20 August 2021) <https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/intermediaries/supervision/doc?refNo=21EC31>.

25 Insurance Authority, Guidelines on Enterprise Risk Management (GL21) (01 January 2020) < https://www.ia.org.hk/en/legislative_framework/files/GL21.pdf>, Paragraph 6.1.2.

26 ibid, Paragraph 7.4.2(b).

27 ibid, Paragraph 8.1.

climate principles and actionable objectives to which signatories in the sector may voluntarily commit.[28]

The Mandatory Provident Fund Schemes Authority (**MPFA**) is a statutory body established under the Mandatory Provident Fund Schemes Ordinance. The MPFA regulates and supervises operations of privately managed provident fund schemes and the Mandatory Provident Fund (**MPF**) System.

In November 2021, the MPFA under the aegis of the Steering Group, issued a circular detailing the 'Principles for Adopting Sustainable Investing in the Investment and Risk Management Processes of MPF Funds' (the **MPFA Principles**).[29] The MPFA Principles are seven principles grouped under four heads – governance, strategy, risk management and disclosure:

1. *Principle 1*: To be in line with their fiduciary duty, MPF trustees should be mindful of all material financial risks impacting the interest of MPF scheme members. ESG factors could be a source of financial risk with long-term financial impact on the value of MPF investment portfolios.

2. *Principle 2*: The board of directors of MPF trustees should have oversight of the integration of ESG factors into the investment and risk management processes and assign management with a clear role in reporting progress against goals set.

3. *Principle 3*: MPF trustees should consider incorporating ESG factors along with all other substantial financial factors that may contribute to achieving the long-term retirement objectives of MPF scheme members and document how ESG factors are treated.

4. *Principle 4*: MPF trustees should consider ESG factors with no prejudice for the objective of obtaining an appropriate risk-return profile on purely financial grounds.

5. *Principle 5*: MPF trustees should disclose the MPF schemes' integration strategies and investment managers' integration policies and report implementation progress regularly.

6. *Principle 6*: MPF trustees should describe how ESG factors are factored into the relevant investment strategies by the investment managers and how the investment managers identify, assess, and manage relevant and material ESG factors.

7. *Principle 7*: MPF trustees should disclose metrics and targets adopted by investment managers where available.

The MPFA Principles do encompass consideration of climate risk within the fold of ESG factors. Most importantly, Principle 7 of the MPFA Principles, recommends using the TCFD frameworks to assess and price risks and opportunities.[30]

In August 2022, the MPFA issued a circular letter to incorporate sustainable investing reporting into the MPF schemes' annual governance report.[31] MPF trustees were required to submit the first annual governance reports for each scheme (in the format provided in this circular letter) with the financial year end on or after 30 November 2022 to the MPFA.[32] This reporting format includes matters on ESG

28 Hong Kong Federation of Insurers, 'Insurance Industry Joins Hands to Address Climate Issues' (1 March 2024) <https://www.hkfi.org.hk/media-release/insurance-industry-joins-hands-to-address-climate-issues>.

29 Mandatory Provident Fund Schemes Authority, Principles for Adopting Sustainable Investing in the Investment and Risk Management Processes of MPF Funds (26 November 2021) <https://www.mpfa.org.hk/en/-/media/files/information-centre/legislation-and-regulations/circulars/mpf/20211126/cir-20211126.pdf>.

30 ibid.

31 Mandatory Provident Fund Schemes Authority, Initiative to Enhance Transparency of Governance Reporting of MPF Schemes (03 August 2022) <https://www.mpfa.org.hk/en/-/media/files/information-centre/legislation-and-regulations/circulars/mpf/20220803/cir-20220803.pdf>.

32 ibid.

factors which would encompass disclosure of climate-related risks and opportunities.

In order to combat financial greenwashing, the SFC requires specific disclosures for ESG funds (as discussed below) and SFC-authorised unit trusts and mutual funds cannot be named or described as an ESG fund without SFC authorization and approval.[33] To obtain such authorization, the fund's name must correspond to its primary strategy or investment objective and it must be approved by the SFC.[34] Under the SFC's most recent guidance, funds that fail to comply with their stated ESG investment objectives or strategies may be subject to enforcement action by the SFC, in addition to removal from the SFC's list of ESG funds.[35]

In 2020, the HKEX launched the Sustainable and Green Exchange (**STAGE**), an online portal designed to provide greater information, access, and transparency to the public on a wide range of sustainable green and social investment products.[36]

The HKMA has issued a guidance note on good practices for Due Diligence Processes for Green and Sustainable Products. This guidance note outlines five high-level principles: (i) setting up a robust product governance framework for green and sustainable products; (ii) conducting comprehensive "greenness assessments" of clients and transaction due diligence for green lending; (iii) performing post-offering monitoring and controls to ensure the proper management of green and sustainable products; (iv) enhancing transparency and accountability in respect of green and sustainable products; and (v) building appropriate expertise in product development and comprehensive due diligence processes.[37] Financial institutions are also subject to specific disclosure requirements, as discussed in section 3.1.3 below.

1.2.1. Liability risk: enforcement action by regulators

Based on publicly available sources, HKSAR financial regulators have not taken any enforcement action against companies and/or their directors about ESG/climate change.[38]

2. Directors' Duties and Climate Change

2.1. Legal framework for directors' duties

Hong Kong is a common law jurisdiction.

Directors' duties in Hong Kong are informed by a combination of statutes (principally the *Companies Ordinance (Cap 622)*) and common law. Directors owe fiduciary duties to the company including the duty to act *bona fide* in the best interests of the company,[39] the duty to avoid unauthorised conflicts of interest and unauthorised receipt of profits,[40] and the duty to act for proper purposes.[41] However,

33 Securities and Futures Commission, 'Circular to management companies of SFC-authorised unit trusts and mutual funds – ESG funds' (29 June 2021) <https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/products/product-authorization/doc?refNo=21EC27>.(superseding its 2019 Circular on ESG fund disclosure).

34 ibid.

35 Securities and Futures Commission, 'List of ESG funds; <https://www.sfc.hk/en/Regulatory-functions/Products/List-of-ESG-funds>.

36 Hong Kong Stock Exchange, 'HKEX Launches Stage, Its Sustainable And Green Exchange' (01 December 2020) <https://www.hkex.com.hk/News/News-Release/2020/201201news?sc_lang=en>.

37 Hong Kong Monetary Authority, Due Diligence Processes for Green and Sustainable Products (2022) < https://www.hkma.gov.hk/media/gb_chi/doc/key-information/guidelines-and-circular/2022/20221209c3a1.pdf>.

38 Lisa Chung, ESG in APAC – Hong Kong by Slaughter & May (Slaughter & May, 30 June 2023)< https://insights.slaughterandmay.com/apac-esg-hong-kong/index.html#group-section-Greenwashing-risks-IP07iOzTkk>.

39 Re Tysan Holdings Ltd [2013] 4 HKC 425, 35, per Mimmie Chan J, 38.

40 Libertarian Investments Ltd v hall (2013) 16 HKCFAR 681, 75, 78-81.

41 Passport Special Opportunities Master Fund LP & Another eSun Holdings Ltd & Others [2011] 4 HKC 62 at 57-60, 88, 90, 143, 147, 150-156, per Barma J.

For a more detailed guidance on directors' duties in Hong Kong, see, Alexander Stock SC and Jennifer Fan, Legal of these duties, only the common law duty to exercise reasonable care, skill and diligence has been codified in legislation. Section 465(1) of the *Companies Ordinance* provides that a director of a company must "*exercise reasonable care, skill and diligence*".[42]

Under the law of Hong Kong, the duty of care, skill and diligence comprises an objective and subjective element. The standard of reasonable care, skill and diligence expected is based on what could reasonably be expected of a person carrying out the functions of a director,[43] as well as the subjective knowledge, skill and experience the impugned director has.[44] Importantly, the subjective characteristics of the director in question can only raise the expected standard.[45]

The duty of care, skill and diligence owed by directors under the law of Hong Kong is relevant to climate risks in several respects. These include:

- the establishment and maintenance of risk management processes;
- due diligence and informed decision-making;
- supervision of management and committees;
- assessment of financial statements; and
- disclosure of material information in accordance with the Hong Kong Stock Exchange Listing Rules.

2.2. Guidance on interpretation of directors' duties

2.2.1. Legal Guidance

A 2021 legal opinion from Alexander Stock SC and Jennifer Fan of Temple Chambers found that, to the degree that climate risks intersect with and affect the best interests of a company, directors are both "*entitled*" and "*obliged*" to take these into account when discarding their obligations.[46]

Concerning climate change, the two most salient directors' duties are the duty to act *bona fide* in the best interests of the company and the duty to exercise reasonable care, skill and diligence. In Hong Kong, the best interests of the company are broadly understood as being commensurate with the financial interests of the members as a whole.[47] As such, under the law of Hong Kong, directors are entitled to consider climate risks in their decision-making processes to the extent that they have or are likely to have, an impact on the financial interests of the company's members.

Directors who fail to consider climate risks may fall short of their duty to act in the best interests of the company given the prominence and foreseeability of climate-related financial risks. Notably, a failure to consider could encompass situations where climate risks were considered but not given adequate weight or considered based on inadequate or incorrect information. Furthermore, in a jurisdiction such as Hong Kong where financial

Opinion on Directors' Duties and Disclosure Obligations under Hong Kong Law in the Context of Climate Change Risks and Considerations (19 October 2021) < https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Legal-Opinion-Hong-Kong-Directors-obligations-and-climate-change.pdf>; Ernest Lim, Commonwealth Climate and Law Initiative, Directors' Liability and Climate Risk: White Paper on Hong Kong (10 December 2021) < https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Directors-liability-and-climate-risk-White-paper-on-HK-FINAL.pdf>.

42 Companies Ordinance (Cap 622), s. 465(1).

43 Companies Ordinance (Cap 622), s. 465(2)(a).

44 ibid, s. 465(2)(b).

45 Re D'Jan of London Ltd, Copp v D'Jan [1994] 1 BCLC 561, 563.

46 Alexander Stock SC and Jennifer Fan, Legal Opinion on Directors' Duties and Disclosure Obligations under Hong Kong Law in the Context of Climate Change Risks and Considerations (19 October 2021) < https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Legal-Opinion-Hong-Kong-Directors-obligations-and-climate-change.pdf>; Ernest Lim, Commonwealth Climate and Law Initiative, Directors' Liability and Climate Risk: White Paper on Hong Kong (10 December 2021) <https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Directors-liability-and-climate-risk-White-paper-on-HK-FINAL.pdf>.

47 Greenhalgh v Arderne Cinemas Ltd [1950] 2 All ER 1120, 1126; Stefan HC Lo and Charles Z Qu, Law of Companies in Hong Kong (Sweet & Maxwell, 4th edn, 2023) [8.030].

regulators have undertaken concerted and coordinated efforts to improve climate risk literacy and governance, the objective standard expected of directors in addressing climate risks could foreseeably be higher than in other jurisdictions.

There is no statutory business judgment rule under Hong Kong's *Companies Code*.[48] While courts do not generally interfere with commercial decisions that are honestly made, will seek to ascertain the veracity of assertions made by directors.[49]

2.2.2. Regulatory guidance

In its 2021 Guidance on Climate Disclosures, the HKEX discusses the roles and responsibilities of the board and management, respectively, with regard to the oversight and management of climate-related issues based on the TCFD disclosure recommendations.[50] Although the HKEX guidance does not seek to clarify or apply the statutory or common law duties of directors in Hong Kong, this guidance and the mandatory corporate governance disclosures discussed below indicate that HKEX expects listed entities to ensure that the board engages in oversight of ESG issues, including with respect to corporate strategy.[51]

On 14 June 2024, the HKEX announced proposed amendments to the Corporate Governance Code and related Listing Rules. The effective date for the proposed changes is 1 January 2025, with a three-year transition period.[52] By one of the proposed amendments, HKEX has required all directors of issuers to receive mandatory continuous professional development in each financial year. The training must cover 'corporate governance and ESG matters, including developments on sustainability or climate-related risks and opportunities relevant to the issuer and its business'.[53]

2.3. Director's liability and litigation risk

Directors who dismiss, or unduly diminish the significance of climate risks, foreseeably face personal liability on several fronts under the law of Hong Kong.[54]

The enforcement of claims against directors under the *Companies Ordinance* in Hong Kong involves two main avenues: derivative actions and unfair prejudice claims. A derivative action allows shareholders to bring a claim on behalf of the company if the board fails to do so. Common law and statutory derivative actions exist, with the latter being broader. Under common law, shareholders must prove fraud or abuse of power by the directors and wrongdoer's control but negligence alone is not enough unless the director profited.[55] In contrast, statutory derivative actions under the *Companies Ordinance* cover 'misconduct', such as fraud, negligence, or breach of duty, without requiring proof of the wrongdoer's control or personal gain.[56]

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48 Douglas M. Branson & Low Chee Keong, Balancing the Scales: A Statutory Business Judgment Rule for Hong Kong?, (2004) 34 HONG KONG L.J. 303.

49 Stefan HC Lo and Charles Z Qu, Law of Companies in Hong Kong (Sweet & Maxwell, 4th edn, 2023) [8.044].

50 HKEX, 'Guidance on Climate Disclosures: Reporting on TCFD recommendations' (November 2021) <https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/guidance_climate_disclosures.pdf?la=en>.

51 ibid.

52 Hong Kong Stock Exchange, 'Review of Corporate Governance and Related Listing Rules' (14 June 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/June-2024-Review-of-CG-Code/Consultation-Paper/cp202406.pdf>.

53 Hong Kong Stock Exchange, 'Review of Corporate Governance and Related Listing Rules' (14 June 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/June-2024-Review-of-CG-Code/Consultation-Paper/cp202406.pdf>, para. 47.

54 Ernest Lim & Umakanth Varottil, 'Climate Risk: Enforcement of Corporate and Securities Law in Common Law Asia' (2022) 22 Journal of Corporate Law Studies 1, 391-430.

55 Daniels v Daniels [1978] Ch 406, 413. See, Tam Lai King v Incorporated Owners of Malahon Apartments [2010] 5HKLRD 63 [59] (for requirement regarding wrongdoer's control).

56 Companies Ordinance (Cap 622), s. 731. However, statutory derivative actions cannot be initiated against companies

To bring a statutory derivative action, shareholders need court permission, which involves proving there's a serious issue to be tried and that it's in the company's interests.[57] However, any damages awarded go to the company, not the individual shareholder, which can discourage derivative actions. Environmental NGOs may still pursue such actions, particularly concerning mismanagement of climate-related risks, by purchasing shares and satisfying the necessary criteria.[58]

Unfair prejudice claims are another route, used when directors' misconduct personally affects a shareholder.[59] While both unfairness and prejudice requirements need to be proved, this provision covers breaches of fiduciary duty, such as failure to address climate-related risks or make necessary disclosures.[60] This remedy is available for both Hong Kong and non-Hong Kong companies.[61] The court can provide various remedies, including ordering the purchase of shares or regulating the company's future conduct.[62]

Additionally, in terms of public enforcement, the SFC can intervene in cases where members have been unfairly prejudiced or denied crucial business information.[63] Where the SFC applies to the court for an order, the relief that the court can grant includes: (1) requiring an act to be carried out or not to be carried out; (2) ordering the company to sue any person; (3) removing any director or officer; and (4) making any order that the court considers appropriate.[64]

There are no court cases against directors relating to climate risk, as yet, however, with the strong focus on financial sector regulators and the proactive nature of the HKSAR Government, regarding mitigating climate change, more action on this front cannot be ruled out.[65]

3. Directors' Duties and Sustainability Disclosure Obligations

3.1. Narrative sustainability disclosures

3.1.1. Sustainability disclosure frameworks

Hong Kong regulators have endorsed the TCFD framework for disclosure of climate-related financial risk and have adopted various regulations and guidance to implement the TCFD and the ISSB climate disclosure standards.

3.1.2. Specific sustainability disclosure requirements for listed entities

Part XIVA of the *Securities and Futures Ordinance* (Cap 571) (**SFO**) provides that listed corporations, and therefore their directors, have an obligation of continuous disclosure regarding information which is likely to materially influence the price of their shares in certain circumstances.

The Hong Kong Stock Exchange's Main Board Listing Rules (the **Listing Rules**) require listed companies to disclose information regarding profit forecasts, among other matters. Such disclosure

incorporated outside Hong Kong which have established a place of business in Hong Kong, and common law derivative action may be the only option in such case. Companies Ordinance (Cap 622), s. 2.

57 Companies Ordinance (Cap 622), s. 733.

58 Ernest Lim, Directors' Liability and Climate Risk: White Paper on Hong Kong (CCLI, 10 December 2021) <https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Directors-liability-and-climate-risk-White-paper-on-HK-FINAL.pdf>.

59 Companies Ordinance (Cap 622), s. 724(1)-(3).

60 Ernest Lim, Directors' Liability and Climate Risk: White Paper on Hong Kong (CCLI, 10 December 2021) <https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Directors-liability-and-climate-risk-White-paper-on-HK-FINAL.pdf>.

61 Companies Ordinance (Cap 622), s. 722(1). This provision defines company to include non-Hong Kong company, the latter of which are companies incorporated outside Hong Kong and which have established a place of business in Hong Kong (see s 774 Companies Ordinance).

62 Companies Ordinance (Cap 622), s. 725(2).

63 Securities and Futures Ordinance (Cap 571), s. 214.

64 Securities and Futures Ordinance (Cap 571), s. 214(2).

65 Ernest Lim & Umakanth Varottil, 'Climate Risk: Enforcement of Corporate and Securities Law in Common Law Asia' (2022) 22 Journal of Corporate Law Studies 1, 391-430.

could foreseeably be precipitated by a climate-related financial risk being realised.

Under rule 13.24B (1) of the Listing Rules, an issuer must announce if an event occurs during the profit forecast period which makes the assumptions underlying the profit forecast materially different. Rule 13.24B (2) provides that an issuer must also announce if there are activities outside the issuer's ordinary course of business that materially contribute to or reduce the profit stated in the profit forecast. Climate or nature-related risks/ events and opportunities that may materially impact the profitability of the issuer would therefore need to be disclosed.

In addition, rule 13.91 of the Listing Rules requires companies to furnish an annual ESG report. As amended in 2019, this annual ESG report, makes disclosure of the following corporate governance matters mandatory:

- the board's oversight of ESG issues;
- the board's ESG management approach and strategy, including the process used to evaluate, prioritise and manage material ESG-related issues; and
- how the board reviews progress made against ESG-related goals and targets with an explanation of how they relate to the companies' operations.[66]

Since July 2020, these amendments to the Listing Rules have also required issuers to disclose, amongst other things, "*significant*" climate-related issues which have or may have, an impact on the company on a comply-or-explain basis, beginning 1 July.[67]

HKEX conducted a review of issuers' ESG disclosures in 2022 and found that the introduction of the rules had driven behavioural changes amongst issuers, and encouraged efforts in managing climate change risk.

In April 2023, HKEX published a consultation paper seeking market feedback on proposals to enhance climate-related disclosures under the ESG framework.[68] It proposed amendments of the ESG reporting framework under the Listing Rules in order to align the framework with the 2023 TCFD-aligned ISSB standards on climate, and to make such disclosures mandatory (rather than continuing on the existing comply or explain basis).

In April 2024, the HKEX published its consultation conclusions and introduced the new climate disclosure requirements, which will be incorporated into Part D of the ESG Guide as set out in Appendix C2 to the Listing Rules.[69] The ESG Guide will be renamed as the ESG Code from 1st January 2025 when the new rules take effect. The proposals mark a significant milestone in achieving the commitment to mandate TCFD-aligned disclosures by 2025 as announced by the Steering Group.

Under the new ESG Code, all listed issuers must disclose scope 1 and 2 GHG emissions on a mandatory basis for

66 Hong Kong Stock Exchange, 'Amendments to the Main Board Listing Rules: Update No.128' (2019) <https://en-rules.hkex.com.hk/rulebook/update-no-128>; HKEX, 'Amendments to the GEM Listing Rules: Update No.64' (2019) <https://en-rules.hkex.com.hk/rulebook/update-no-64>.

67 Hong Kong Stock Exchange, 'Amendments to the Main Board Listing Rules: Update No.128' (2019) <https://en-rules.hkex.com.hk/rulebook/update-no-128>; HKEX, 'Amendments to the GEM Listing Rules: Update No.64' (2019) <https://en-rules.hkex.com.hk/rulebook/update-no-64>; HKEX, 'Guidance on Climate Disclosures: Reporting on TCFD recommendations' (November 2021) <https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/guidance_climate_disclosures.pdf?la=en>.

68 Hong Kong Stock Exchange, Consultation Paper: Enhancement of Climate-Related Disclosures under the Environmental, Social and Governance Framework (April 2023) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/April-2023-Climate-related-Disclosures/Consultation-Paper/cp202304.pdf>.

69 Hong Kong Stock Exchange, 'Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework' (19 April 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/April-2023-Climate-related-Disclosures/Conclusions-Apr-2024/cp202304cc.pdf>.

financial years commencing on or after 1 January 2025. A phased approach will apply with respect to other ISSB-aligned climate disclosure requirements, whereby, in addition to scope 1 and scope 2 GHG emissions disclosures:

(a) All main board-listed issuers must make the other ISSB-aligned climate disclosures on a 'comply or explain' basis for financial years commencing on or after 1 January 2025.
(b) Issuers that are included in the Hang Seng Composite LargeCap Index must make disclosures the other ISSB-aligned climate on a "comply or explain" basis in financial years commencing on or after 1 January 2025. This will be replaced by a mandatory disclosure for financial years commencing on or after 1 January 2026.
(c) GEM-listed issuers are encouraged to make the other ISSB-aligned climate disclosures on a voluntary basis for financial years commencing on or after 1 January 2025.[70]

In response to concerns around issuers' readiness and data availability, the HKEX has introduced implementation reliefs for certain disclosure requirements.[71] In April 2024, HKEX also published implementation guidance for the climate reporting requirements.[72]

Just prior to releasing the new climate disclosure requirements, the HKSAR Government's Financial Services and the Treasury Bureau also published a vision statement outlining the approach of the government and financial regulators towards developing a comprehensive framework for sustainability disclosure in Hong Kong based on the ISSB standards, in addition to the standards for climate disclosure.[73] The Hong Kong Institute of Certified Public Accountants will assume the responsibility for developing local sustainability reporting standards aligned with the ISSB standards and the ISSB's May 2024 Adoption Guide.[74]

The vision statement indicates that the roadmap for the appropriate adoption of the ISSB Standards, announced in the government's 2023 policy address, will be launched in 2024. The roadmap aims to provide a transparent and well-defined pathway for sustainability reporting for businesses in Hong Kong and allow sufficient time for businesses to prepare for the Hong Kong Standards.[75]

3.1.3. Specific sustainability disclosure requirements for financial institutions

70 ibid, para.8; Charltons, 'Exchange Publishes Consultation Conclusions on New Climate Disclosure Requirements Effective 1 January 2025' (June 2024) <https://www.charltonslaw.com/exchange-publishes-consultation-conclusions-on-new-climate-disclosure-requirements-effective-1-january-2025/>.

71 Hong Kong Stock Exchange, 'Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework' (19 April 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/April-2023-Climate-related-Disclosures/Conclusions-Apr-2024/cp202304cc.pdf>, para.13. These include – (a) Reasonable information relief: allows issuers to use all reasonable and supportable information available at the reporting date without undue cost or effort. (b) Capabilities relief: allows issuers to consider their "available skills, capabilities and resources" at the point of preparing the climate-related disclosure. (c) Commercial sensitivity relief: exempts disclosure of commercially sensitive information, provided a set of conditions are met. (d) Financial effects relief allows disclosure of qualitative rather than quantitative financial information, provided a set of conditions are met.

72 Hong Kong Stock Exchange, 'Implementation Guidance for Climate Disclosures under HKEX ESG Reporting Framework' (April 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/guidance_enhanced_climate_dis.pdf>.

73 See, Financial Services and Treasury Bureau, 'Vision Statement on Turning Obligations into Opportunities in Developing the Sustainability Disclosure Ecosystem in Hong Kong' (25 March 2024) <https://gia.info.gov.hk/general/202403/25/P2024032500391_452899_1_1711358339971.pdf>; G Hutchinson, 'Hong Kong SAR government issues vision statement on adoption of the ISSB standards (Linklaters, 4 April 2024) <https://sustainablefutures.linklaters.com/post/102j4er/hong-kong-sar-government-issues-vision-statement-on-adoption-of-the-issb-standard>.

74 Financial Services and Treasury Bureau, 'Vision Statement on Turning Obligations into Opportunities in Developing the Sustainability Disclosure Ecosystem in Hong Kong' (25 March 2024) <https://gia.info.gov.hk/general/202403/25/P2024032500391_452899_1_1711358339971.pdf>, para 8.

75 ibid. para. 7-8, 10.

HKMA authorised institutions*:* Financial institutions and funds are also subject to increased climate disclosure obligations. In December 2020, the HKMA announced that reporting by TCFD recommendations would be mandatory for companies in the banking, asset management, insurance and pension fund sectors by 2025.[76]

In December 2021, the HKMA issued the Supervisory Policy Manual Module GS-1 Climate Risk Management which sets out HKMA's requirements regarding governance, strategy, risk management, and disclosure practices of authorised institutions to build climate resilience.[77] In August 2023, the HKMA released a circular to all authorized institutions, outlining key principles for transitioning to a net-zero economy.[78] Amongst other issues, these principles highlighted the nudge by the regulator towards enhancing disclosures on the transition planning process and/ or transition plans of the authorised institutions.[79] The details of other principles have been dealt with in Section 1.1.3 above.

In August 2024, HKMA issued a circular on best practices for climate-related risk governance based on the observations from the supervisory exercises conducted by HKMA.[80] This circular focuses on three key aspects: (a) fostering and overseeing the effective development and implementation of climate strategy; (b) exercising appropriate oversight of climate risk management; and (c) cultivating a strong organisational climate risk culture.[81] This circular further noted that authorised institutions have published climate-related disclosures aligned with TCFD recommendations in advance of regulatory requirements.[82]

SFC authorised institutions: In June 2021, the SFC issued a circular to management companies of SFC-authorised funds on the disclosures ESG funds that market to retail investors should make, including a description of the ESG focus of the fund, its ESG investment strategy, and any related risks.[83]

The 2021 SFC amendments to the Fund Manager Code of Conduct, which require fund managers to consider climate risks (defined as physical, transition and liability risks) in their investment and risk management processes, and require managers of at least HK$ 8 billion in assets to make a reasonable effort to report their investees' and funds' scope 1 and 2 GHG emissions from November 2022.[84] Therefore, both ESG-focused funds and other funds are required to disclose ESG-related information (including, where relevant, information relating to climate change).

3.1.4. Directors' duties regarding sustainability disclosures

Directors are responsible for relevant disclosures under the *Companies*

76 Hong Kong Monetary Authority, 'Cross-Agency Steering Group Launches its Strategic Plan to Strengthen Hong Kong's Financial Ecosystem to Support a Greener and More Sustainable Future' (17 Dec 2020) <https://www.hkma.gov.hk/eng/news-and-media/press-releases/2020/12/20201217-4/>.

77 Hong Kong Monetary Authority, 'Supervisory Policy Manual: Climate Risk Management' (December 2021) <https://www.hkma.gov.hk/media/chi/doc/key-functions/banking-stability/supervisory-policy-manual/GS-1.pdf>.

78 Hong Kong Monetary Authority, 'Planning for net-zero transition' (Ref: B1/15C, B9/197C, 29 August 2023) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2023/20230829e1.pdf>.

79 ibid, Principle 6.

80 Hong Kong Monetary Authority, 'Good practices on climate-related risk governance' (22 August 2024) <https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2024/20240822e1.pdf>.

81 ibid.

82 ibid.

83 Securities and Futures Commission, 'Circular to management companies of SFC-authorised unit trusts and mutual funds – ESG funds' (29 June 2021) <https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/products/product-authorization/doc?refNo=21EC27>.

84 Securities and Futures Commission, 'Circular to licensed corporations: Management and disclosure of climate-related risks by fund managers' (20 August 2021) <https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/intermediaries/supervision/doc?refNo=21EC31>.

Ordinance and the HKEX Listing Rules. The *Companies Ordinance* read with the *Companies (Directors' Report) Regulation*, company directors are statutorily required to publish a directors' report which provides an overview of the company's business operations.[85] For listed companies, the HKEX Guidance on Climate Disclosures and the Corporate Governance Guide for Boards and Directors emphasize the responsibility of the board to ensure appropriate and adequate reporting and compliance with all applicable disclosure requirements, which extends to the 2025 ESG Code.[86] Further, all Hong Kong-incorporated companies are required to include a business review section in their annual directors' report which discusses their environmental policies and performance, compliance with relevant laws and regulations and their key relationships with stakeholders.[87] This section will encompass a discussion on aspects regarding the impact of climate change on business operations.

While Listing Rules do not have statutory force, they constitute the mainstay for listed companies. Courts have emphasised that 'directors of listed companies are under the same if not more onerous duties, bearing in mind that they are governed by the Listing Rules, and considering the fact that public investors look to them for the proper governance of the company and its compliance with the Listing Rules'.[88]

Directors need to be mindful of their individual and collective obligations about applicable disclosure requirements and take proactive measures to engage with the management in this regard. The duty to disclose is likely to gain more force once the new climate disclosure framework is enforced.

3.1.5. Liability risk arising from narrative sustainability disclosures

Directors may face significant liability risks arising from violations of sustainability disclosure requirements if these violations also meet the grounds for private and public enforcement avenues discussed in Section 2.2 above. Further, if a director wilfully fails to comply with the disclosure requirements regarding the directors' report, such director may be subject to a criminal fine and imprisonment.[89]

Additionally, based on the regulatory ambit, relevant regulators also have the power to sanction directors and the company for violations of the sustainability disclosure requirements. For instance, the SFO may impose liability on those responsible for issuing public communications for failure to take reasonable care in respect of the accuracy of information involved. Under Section 108(2) of the SFO, where a company has made any fraudulent, reckless or negligent misrepresentation by which another person is induced to acquire any securities or investment products from the issuer, the directors of that company will be presumed to have made the misrepresentation unless they prove that they did not authorise the making of the misrepresentation. Under Section 281(3)(b) of the SFO, a director may be liable to compensate an investor if he or she has consented to or connived about the company's commission of the relevant act related to market misconduct (which includes misleading disclosures). Finally, under Section 307Z of the SFO, investors can sue the company (or its directors) to claim compensation by way of damages for the losses they have sustained as a result

85 Companies (Directors' Report) Regulation, 2019 read with Companies Ordinance (Cap 622), s. 452(3).

86 HKEX, 'Guidance on Climate Disclosures: Reporting on TCFD recommendations' (November 2021) <https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/guidance_climate_disclosures.pdf?la=en>; HKEX, 'Corporate Governance Guide for Boards and Directors' (December 2021) < https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Corporate-Governance-Practices/guide_board_dir.pdf?la=en>.

87 Companies Ordinance (Cap 622), s. 388-9 and Schedule 5.

88 Re Tysan Holdings Ltd [2013] 4 HKC 425, 35, per Mimmie Chan J, 38.

89 Companies Ordinance (Cap 622), s. 388(7).

of the breach committed by the company (or its directors).[90]

Failure to comply with the 2025 ESG Code's climate disclosure regime would constitute a breach of the Listing Rules.[91] This may result in HKEX initiating a disciplinary action and could, if serious enough, lead HKEX to suspend or cancel a listing.[92] The director may also potentially be disqualified or subject to compensation orders by the SFC if they are found to have breached their duties of reasonable care, skill, and diligence.[93]

3.2. *Climate-related disclosures in financial statements*

3.2.1. *Climate-related disclosures in financial statements*

Climate change's impact on businesses is increasingly scrutinized by stakeholders. The Hong Kong Financial Reporting Standards (the **HKFRSs**) do not explicitly mention climate-related issues.

However, the HKFRS are based on the IFRS standards, which encourage reporting entities to consider climate-related issues when materially relevant. In July 2023, the IFRS Foundation issued educational material 'Effects of Climate-Related Matters on Financial Statements', in accordance with IFRS Standards. This guidance highlighted various accounting standards that may require consideration of climate-related matters. It outlined potential financial implications of climate risks, including asset impairment, changes in asset lifespans and valuations, impacts on impairment calculations, adjustments to provisions for onerous contracts, changes in provisions and contingent liabilities related to fines and penalties, and alterations in expected credit losses for debt financial assets.

Financial statements prepared under the HKFRS should explain the financial effects of climate-related matters such as the effect of climate change or climate change action on inventories, taxes, assets, impairments, provisions, liabilities, financial instruments, fair value measurements, and insurance contracts.[94] Entities must also disclose any significant judgments, estimates, or assumptions related to climate matters that could lead to material future adjustments.[95] This approach ensures comprehensive reporting of climate-related financial impacts within the existing HKFRS framework.

The HKEX 2021 Guidance on Climate Disclosures as well as the new climate disclosure rules that take effect in 2025 emphasize and related implementation guidance emphasize the linkage between a company's climate-related indicators and its financial performance and position, as well as the translation of indicators into financial impacts.[96] The HKEX ESG Code

90 Securities and Future Ordinance (Cap. 571), s. 307Z.

91 See, Hong Kong Stock Exchange, Consultation Paper: Enhancement of Climate-Related Disclosures under the Environmental, Social and Governance Framework (April 2023) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/April-2023-Climate-related-Disclosures/Consultation-Paper/cp202304.pdf>, Paragraph 142.

92 Consequences of breach of listing rules arise from Main Board Listing Rules 2A.9-2A.10 and GEM Listing Rules 3.120-3.11. These rules stem from Hong Kong Stock Exchange, 'Amendments to the Main Board Listing Rules: Update No.132' (2021) <https://en-rules.hkex.com.hk/rulebook/update-no-132>; Hong Kong Stock Exchange, 'Amendments to the GEM Listing Rules: Update No.68' (2021) <https://en-rules.hkex.com.hk/rulebook/update-no-68>.

93 E de Wit et al., 'Review of climate-related financial disclosure regimes around the world' (Norton Rose Fulbright, June 2024) <https://www.nortonrosefulbright.com/de-de/wissen/publications/9261bbcf/review-of-climate-related-financial-disclosure-regimes-around-the-world>.

94 EY, Hong Kong Listed Limited – Illustrative Report of the Directors and Financial Statements for the year ended 31 December 2023, <https://assets.ey.com/content/dam/ey-sites/ey-com/en_cn/topics/assurance/ey-dec-2023-hk-listed-ltd-ifs-external.pdf>.

95 ibid.

96 Hong Kong Stock Exchange, 'Guidance on Climate Disclosures: Reporting on TCFD recommendations' (November 2021) <https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/guidance_climate_disclosures.pdf?la=en>; Hong Kong Stock Exchange, 'Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework' (19 April 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/April-2023-Climate-related-Disclosures/Conclusions-Apr-2024/cp202304cc.pdf>; Hong Kong Stock Exchange, 'Implementation Guidance for Climate Disclosures under HKEX ESG Reporting Framework' (April 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-

requires companies to disclose the current and anticipated effects of climate-related risks and opportunities on the issuer's financial position, financial performance and cash flow.[97] Like the ISSB standards, these disclosures complement and should cross-reference and align with related information reported in the issuer's financial statements.[98]

3.2.2. Directors' duties regarding climate-related disclosures in financial statements

Directors are required to prepare financial statements that comply with Section 380 (and also Section 383) of the *Companies Ordinance* for each year.[99] Section 380 requires that annual financial statements reflect the 'true and fair view' of the financial performance of the company for the financial year.[100] Further, this requirement needs to be confirmed by the auditor in the auditor's opinion.[101] These provisions make it imperative for directors to consider climate-related risks (particularly those that materially impact business operations), in order to discharge their duty to provide a 'true and fair view' of the financial position of the company in the financial statements.

There is no publicly available legal opinion on the consideration of climate risks in accounting in Hong Kong. However, a top accounting firm in its illustrative representation of the annual accounts has stated that due consideration of climate risks is required while accounting for key matters within the financial statements.[102]

3.2.3. Liability risk arising from financial statements

Directors may be held liable for breaching their duty of care if the financial statements that they approve fail to disclose significant climate-related risks, violating accounting standards' "true and fair view" requirement.[103] This liability can arise from neglecting to consider material climate risks (e.g., omitting stranded asset disclosures) or failing to properly assess climate impacts on financial items (e.g., understating bad debts due to climate-affected loan repayment abilities).[104] Additionally, depending on their severity, violations regarding accounting for climate-related risks could also attract private enforcement and public enforcement measures (including enforcement action by regulatory authorities for the financial sector).

As discussed in Section 2.2. above, all directors are expected to make appropriate inquiries and to consider climate risks' materiality in financial reporting to fulfil their duty of care.

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and-Governance/Exchanges-guidance-materials-on-ESG/guidance_enhanced_climate_dis.pdf>.

97 ESG Code, Part D, para. 24-25, in Hong Kong Stock Exchange, 'Enhancement of Climate-related Disclosures under the Environmental, Social and Governance Framework' (19 April 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/April-2023-Climate-related-Disclosures/Conclusions-Apr-2024/cp202304cc.pdf>.

98 Hong Kong Stock Exchange, 'Implementation Guidance for Climate Disclosures under HKEX ESG Reporting Framework' (April 2024) <https://www.hkex.com.hk/-/media/HKEX-Market/Listing/Rules-and-Guidance/Environmental-Social-and-Governance/Exchanges-guidance-materials-on-ESG/guidance_enhanced_climate_dis.pdf>.

99 Companies Ordinance (Cap 622), s. 379.

100 Companies Ordinance (Cap 622), s. 380.

101 Companies Ordinance (Cap 622), s. 406.

102 EY, Hong Kong Listed Limited – Illustrative Report of the Directors and Financial Statements for the year ended 31 December 2023, <https://assets.ey.com/content/dam/ey-sites/ey-com/en_cn/topics/assurance/ey-dec-2023-hk-listed-ltd-ifs-external.pdf>.

103 See Ernest Lim, Commonwealth Climate and Law Initiative, Directors' Liability and Climate Risk: White Paper on Hong Kong (10 December 2021) <https://ccli.ubc.ca/resource/directors-liability-and-climate-risk-white-paper-on-hong-kong/>. Companies Ordinance (Cap 622), s. 387 (directors) and 408 (auditors).

104 Deloitte, "Climate Risk and Financial Statement Impacts" (2020) https://www2.deloitte.com/content/dam/Deloitte/au/Documents/risk/deloitte-au-risk-climate-risk-financial-statement-impacts200720.pdf.

Biodiversity risk

Hong Kong boasts a relatively high biodiversity despite its area coverage, including one third of the total bird species in China.[105] The CCLI has published a report on how companies in Hong Kong and other jurisdictions may depend on biodiversity for the functioning of their business models.[106] Biodiversity risks may constitute material financial risks which boards are required to consider within the purview of their duties and disclosure obligations.

Regulatory expectations in relation to biodiversity loss may be increasing. HKEX views governance of environmental issues as inextricably linked to good corporate governance. With TCFD recommendations becoming mandatory for listed issuers and for companies in Hong Kong's banking, asset management, insurance and pension fund sectors by 2025, adoption of the Taskforce on Nature-Related Financial Disclosure (TNFD) framework into regulations may follow.[107] More ESG related policy and regulatory initiatives, which may include biodiversity issues, are expected as Hong Kong pursues its ambition to be the global ESG investment hub of Asia.

ESG and climate litigation is not common in Hong Kong. However, in light of the increased environmental litigation in other parts of the world and its likelihood in Asia, there is a possibility of environmental lawsuits in Hong Kong.[108] If biodiversity risks were to intersect with and affect the best interests of a company, their relevance may be similar to that of climate risks, prompting biodiversity related litigation against a company or its directors, including for failure to disclose transition risk, or for greenwashing.[109] These factors may have a bearing on the relevance of biodiversity risk to the discharge of directors' duties.

Practical Implications for Directors

Hong Kong's regulators have become increasingly emphatic regarding the need for companies and their directors to adopt climate resilience measures in business practices and disclosure. As discussed above, the HKMA will be making TCFD disclosure mandatory for its supervised entities by 2025; the HKMA and SFC co-chair the Steering Group, and HKEX has introduced the new ESG Code, with specific attention to climate-related disclosure. Given these developments, well-counselled boards should:

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105 Hong Kong Government, The Natural Environment, Plants & Animals in Hong Kong (accessed 27 March 2023) <https://www.gov.hk/en/residents/environment/conservation/naturalenvplantsanimals.htm>.

106 CCLI, Biodiversity Risk: Legal Implications for Companies and their Directors (December 2022) <https://commonwealthclimatelaw.org/wp-content/uploads/2022/12/CCLI_Biodiversity_risk_paper_2022.pdf>.

107 Task Force on Nature-Related Financial Disclosure (TNFD), 'About,' <https://tnfd.global/ >; HKMA, Cross-Agency Steering Group Launches its Strategic Plan to Strengthen Hong Kong's Financial Ecosystem to Support a Greener and More Sustainable Future (17 December 2020) <https://www.hkma.gov.hk/eng/news-and-media/press-releases/2020/12/20201217-4/>.

108 Ernest Lim, Commonwealth Climate and Law Initiative, Directors' Liability and Climate Risk: White Paper on Hong Kong (10 December 2021) <https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Directors-liability-and-climate-risk-White-paper-on-HK-FINAL.pdf>.Jolene Lin and Douglas Kysar (eds.), Climate Change Litigation in the Asia Pacific (CUP, 2020).

109 Alexander Stock SC and Jennifer Fan, Legal Opinion on Directors' Duties and Disclosure Obligations under Hong Kong Law in the Context of Climate Change Risks and Considerations (19 October 2021) < https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Legal-Opinion-Hong-Kong-Directors-obligations-and-climate-change.pdf>; Ernest Lim, Commonwealth Climate and Law Initiative, Directors' Liability and Climate Risk: White Paper on Hong Kong (10 December 2021) <https://commonwealthclimatelaw.org/wp-content/uploads/2022/05/CCLI-Directors-liability-and-climate-risk-White-paper-on-HK-FINAL.pdf>.

a) delegate climate risk identification and evaluation to an identified team in management which reports directly to the CEO and board;

b) put on the agenda for the board within 3 or 6 months a process to start developing a climate transition roadmap to 2050 with transparent carbon neutrality or emissions reduction targets, with clear interim targets to 2040, 2030, and within the current rolling multi-year strategic plan, and require periodic reporting on progress against those targets to the board;

c) delegate to the appropriate committee(s) of the board, such as risk, audit, legal and governance, scenarios/strategy, nominations/remuneration, or sustainability/corporate responsibility committee(s), the task of translating the long-term strategy into a clear decision-making process for each aspect that is relevant to each committee; and

d) discuss with disclosure counsel the development of an external engagement and communications plan and oversight of rigorous climate-related disclosure and accounting processes.

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