Explanatory Memorandum

Exposure Drafts HKFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and HKFRS S2 *Climate-related Disclosures*

Hong Kong Institute of
Certified Public Accountants
香港會計師公會

Contents

I. Introduction

1. The HKICPA (or Institute) is the sustainability reporting standard setter in Hong Kong.[1] It is publishing this explanatory memorandum to provide background information to the exposure drafts of HKFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and HKFRS S2 *Climate-related Disclosures* (HK EDs).

2. There has been a growing demand globally in recent years for a set of comprehensive, global baseline standards for sustainability disclosures. This has stemmed from widespread calls from leading investors, analysts, securities regulators, policymakers and other stakeholders for more consistent and comparable sustainability disclosures to facilitate capital allocation decisions.

3. In response to this call, the IFRS Foundation (IFRSF) established the International Sustainability Standards Board (ISSB) in November 2021. The ISSB published the inaugural IFRS Sustainability Disclosure Standards (ISSB Standards)—IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and IFRS S2 *Climate-related Disclosures* in June 2023, which marked a significant milestone in global sustainability reporting. In July 2023, the International Organization of Securities Commissions (IOSCO) endorsed the ISSB Standards as being fit for purpose in serving the needs of the capital market following its comprehensive review of the standards.

4. The IFRSF's objective is to set IFRS Standards that result in the provision of high-quality, transparent and comparable information in financial statements and sustainability disclosures that is useful to investors and other participants in the world's capital markets in making economic decisions. The ISSB Inaugural Jurisdictional Guide issued in May 2024 sets out that the targeted entities for application of the ISSB Standards are publicly accountable entities (PAEs), which are –

    (a) entities whose securities are traded in a public market or entities in the process of issuing securities for trading in a public market (sometimes called listed entities or public entities); and

    (b) entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses (for example, banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks) and have a significant weight in the jurisdiction, regardless of their ownership structure or listed status.

5. The ISSB Inaugural Jurisdictional Guide makes it clear that PAEs do not include –

    (a) entities whose securities are traded in private markets;

[1] Paragraph 8 of the Vision Statement on Turning Obligations into Opportunities in Developing the Sustainability Disclosure Ecosystem in Hong Kong published by the Financial Services and the Treasury Bureau on 25 March 2024.

(b) entities whose securities are traded in relatively small public securities markets;

(c) entities that are generally characterised by small shareholder bases or low liquidity, or that are not subject to extensive corporate governance disclosure requirements;

(d) entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of their primary businesses and do not have a significant weight in the jurisdiction; or

(e) other entities such as private entities and entities without public accountability that are often referred to as SMEs.

6. In light of the rising international momentum in sustainability reporting, the HKSAR Government announced in the 2023 Policy Address that it will work with financial regulators and relevant stakeholders to develop a roadmap on the appropriate adoption of the ISSB Standards in Hong Kong (HK Roadmap). This commitment was reaffirmed in March 2024 by the Financial Services and the Treasury Bureau (FSTB) in the *Vision Statement on Turning Obligations into Opportunities in Developing the Sustainability Disclosure Ecosystem in Hong Kong* (Vision Statement). The Vision Statement sets out Hong Kong's aim to be among the first jurisdictions to align the local sustainability disclosure requirements with the ISSB Standards. The HKICPA will develop a set of local sustainability disclosure standards (HK Standards) aligned with the ISSB Standards for cross-sectoral observance. The Vision Statement also promulgates FSTB's target to launch the Roadmap within 2024, to provide a transparent and well-defined pathway on sustainability reporting for businesses in Hong Kong as well as sufficient time for making preparations and developing readiness for the pragmatic implementation of the HK Standards.

7. The HKICPA is proposing full convergence of HKFRS S1 and S2 with IFRS S1 and S2, which is described by the ISSB Inaugural Jurisdictional Guide as 'full alignment', thus the HK EDs are the same as IFRS S1 and IFRS S2 subject to only having an effective date of 1 August 2025. The decision of full convergence was reached by the HKICPA after a holistic assessment of relevant factors, including views from various stakeholders from the technical feasibility study (TFS) on the application of the ISSB Standards in Hong Kong conducted between March to June 2024. As an international financial centre (IFC), Hong Kong's full convergence with the ISSB Standards has global significance as it would bolster the connection of global capital with local businesses as well as those in mainland China[2] and other regions.

8. The Institute is now seeking comments on the accompanying HK EDs by **27 October 2024**. The HK EDs have been prepared on a full convergence basis with IFRS S1 and S2, with a proposed effective date of 1 August 2025.

9. Part II of this explanatory memorandum sets out the development journey of the HK EDs; Part III sets out the consultation questions and Part IV sets out next steps.

[2] The Ministry of Finance of the People's Republic of China has published a consultation on 'Corporate Sustainability Disclosure Standard—Basic Standard' on 27 May 2024 (Chinese only). The draft standard was developed based on the ISSB Standards while aligning with China's context and showcasing Chinese characteristics.

II. The development journey of the HK EDs

10. This part sets out how international and local developments over the past few years have informed the HKICPA in formulating its proposal for full convergence with the ISSB Standards. It starts with the global call for consistent sustainability disclosures; the subsequent establishment of the ISSB and publication of IFRS S1 and S2; and moves onto how the results of various local bodies' engagements with stakeholders on the ISSB Standards from 2022 to 2024 have provided strong evidence to support full convergence. All this is underpinned by robust, ongoing capacity building efforts.

(a) Global momentum for sustainability reporting and establishment of the ISSB

11. The HKICPA has been closely monitoring the developments in the international sustainability standard setting arena for several years, with a particular focus on the developments at the IFRSF since 2020. During this period, a global consensus among leading investors, analysts, securities regulators, policymakers and other stakeholders around the world emerged, advocating for enhanced consistency and comparability in sustainability disclosures to facilitate capital allocation decisions. This momentum led to the IFRSF's public consultation on whether it should establish a sustainability standards board to help consolidate the then fragmented sustainability reporting landscape. The HKICPA had consulted the public and expressed strong support for such an initiative. The establishment of the ISSB was announced at the 26th United Nations Climate Change Conference (COP26) in November 2021.

(b) ISSB EDs—baseline standards that benefit investors

12. Responses to the IFRSF consultation in 2020 confirmed the growing and urgent demand for a common set of global sustainability reporting standards. In March 2022, the ISSB issued exposure drafts of IFRS S1 and IFRS S2 (ISSB EDs). IFRS S1 sets out the general disclosure requirements designed to enable entities to disclose material information about sustainability-related risks and opportunities that could reasonably be expected to affect the entity's cash flows, access to financing, or cost of capital over the short, medium and long term. As climate change is a global concern and focus, the ISSB had also proposed its first thematic standard, IFRS S2, to provide specific requirements for climate-related disclosures. The ISSB EDs were built on the principles of the Task Force on Climate-related Financial Disclosures (TCFD) which helps to enhance their interoperability with other sustainability reporting frameworks such as the Global Reporting Initiative and European Sustainability Reporting Standards. The G20 Leaders have welcomed this programme of work and it has garnered support from market regulators, multilateral institutions, investors and companies worldwide.

(c) HKICPA's involvement in the ISSB Standards

13. The Institute conducted extensive outreach from March to July 2022 to gather the perspectives of local stakeholders across different sectors on the ISSB EDs. These

stakeholders included bankers, insurers, asset managers, investors, property developers as well as energy and transport companies. The outreach activities encompassed the following:

(i) Issuing an invitation to comment and conducting an online survey to gather feedback from stakeholders;

(ii) Establishing an in-house working group comprising senior-level sustainability specialists from diverse backgrounds to seek their input;

(iii) Seeking input from experienced preparers of sustainability reports in Hong Kong; and

(iv) Organising a public roundtable discussion with the ISSB staff which attracted participation from over 80 attendees.

14. The comments and feedback received from local stakeholders were thoroughly analysed and incorporated into the HKICPA's comment letter to the ISSB in July 2022. Overall, there was overwhelming support locally and internationally for the ISSB to establish a comprehensive global baseline of sustainability disclosures designed to meet the information needs of investors. Local stakeholder comments generally revolved around the availability and quality of data concerning scope 3 GHG emission disclosures, whether qualitative disclosures could substitute for quantitative ones with regard to anticipated financial effects and scenario analysis, as well as the need for more time and capacity building initiatives to support the proper application of the standards.

15. In June 2023, the ISSB issued its inaugural standards - IFRS S1 and IFRS S2, ushering in a new era of sustainability-related disclosures in capital markets worldwide. In July 2023, IOSCO endorsed these two standards[3] and called on its more than 130 members, including the Securities and Futures Commission (SFC) of Hong Kong, to consider ways in which they might adopt, apply or otherwise be informed by IFRS S1 and S2 within the context of their jurisdictional arrangements.

16. In finalising its two inaugural standards, the ISSB took into account feedback from stakeholders. Specifically, the ISSB acknowledged that entities around the world have varying capabilities and levels of maturity in terms of sustainability reporting. To address this, the ISSB has made a number of notable changes to the proposals and incorporated proportionality mechanisms into the final standards. The proportionality mechanisms allow entities to use 'reasonable and supportable information that is available without undue cost or effort' and to consider 'its own skills, capabilities and resources' when preparing certain types of disclosures (e.g. to prepare a scenario analysis and estimate anticipated financial effects using a method that is commensurate with the entity's circumstances) (see FAQ 5 in Appendix 1).

17. Overall, the Institute considers that the majority of local stakeholders' comments could be effectively addressed by the transition reliefs, built-in proportionality mechanisms and other

[3] IOSCO's report of its technical assessment of IFRS S1 and S2 is available here.

enhancements made to the original ISSB proposals.[4] Be that as it may, the HKICPA acknowledges that further guidance remains essential to support proper implementation of the standards and recognises the importance of ongoing capacity building to augment expertise and provide assistance in addressing practical issues. To this end, the Institute has issued two pieces of education guidance[5] in early 2024 to enhance awareness and understanding of the concepts of proportionality and scalability.

18. In addition, the HKICPA and other relevant parties have either initiated or will initiate a series of actions to address local stakeholder concerns raised in the various ISSB Standards-related consultations in recent years. See Appendices 3 and 4 as well as FAQ 4 in Appendix 1.

(d) HKEX's initiatives to enhance its climate rules

19. In support of the global sustainability reporting initiative as well as to meet investors' information needs and maintain Hong Kong's competitiveness as an IFC, Hong Kong Exchanges and Clearing Limited (HKEX) launched a consultation in April 2023 to enhance the climate-related disclosure requirements under its ESG regulatory framework by incorporating the key requirements of IFRS S2 into Appendix 27 (now renamed as Appendix C2) to the Listing Rules.

20. Respondents to the HKEX's consultation paper were generally supportive of HKEX's proposal to introduce mandatory climate-related disclosures. All proposed disclosures received support from a majority of the respondents, while a number of respondents called for phased implementation of the new requirements and wider alignment with the ISSB Standards, including the proportionality reliefs and reporting principles under the ISSB Standards.[6]

21. After considering market feedback, HKEX finalised the new climate-related disclosure requirements and published the consultation conclusions in April 2024. The enhanced HKEX climate rules together with the accompanying implementation guidance[7] (HKEX April 2024 IG) are closely aligned with the ISSB Standards.

22. As indicated in HKEX's consultation conclusions, the final enhanced climate disclosure rules serve as an interim step to prepare listed entities for the eventual adoption of the HK Standards which are expected to align with the ISSB Standards. When the HK Standards are available, HKEX will consider how to transition towards sustainability reporting in

[4] See Appendix 2 for a high-level analysis of local stakeholders' comments on the ISSB EDs and how they have been addressed in the final ISSB Standards.
[5] Two important ideas in IFRS S1 and IFRS S2 to facilitate proportionality and scalability; and Considerations of Skills, Capabilities and Resources in Climate-Related Scenario Analysis.
[6] Adapted from paragraph 7 of the HKEX's Consultation Conclusions on Enhancement of Climate-related Disclosures under the ESG Framework (consultation conclusions) published in April 2024.
[7] Implementation Guidance for Climate Disclosures under HKEX ESG reporting framework.

accordance with the HK Standards, including whether to replace its current ESG regulatory framework (which primarily comprises Appendix C2) with a straightforward Listing Rule requirement directing listed issuers to publish sustainability reports in accordance with those HK Standards. This approach is consistent with the approach HKEX currently adopts for financial reporting more generally.[8]

(e) Other regulatory actions in response to sustainability-related disclosures

23. Apart from the public consultations conducted by the Institute and HKEX, a number of local and international organisations and regulators have also conducted their own public consultations or sought input from their constituents regarding climate- and/or sustainability-related disclosures:

    (i) Basel Committee on Banking Supervision (BCBS) consulted banks on the Basel Committee's disclosure framework for climate-related financial risk from December 2023 to Q1 2024.

    (ii) International Association of Insurance Supervisors (IAIS) has begun its public consultation on climate risk supervisory guidance in July 2024 which will remain open for comments until the end of Q3 2024.

    (iii) Hong Kong Monetary Authority (HKMA), Insurance Authority (IA), SFC and Mandatory Provident Fund Schemes Authority (MPFA) have also been engaging with their respective constituents and relevant stakeholders to explore potential enhancements to sector-specific regulatory requirements relating to climate and other sustainability topics as initiated by their respective international regulators viz. BCBS, IAIS, IOSCO and International Organisation of Pension Supervisors since the publication of the ISSB Standards.

(f) Engagement with the CASG and the technical feasibility study

24. The Green and Sustainable Finance Cross-Agency Steering Group (CASG) was established in May 2020 and is co-chaired by the HKMA and SFC.[9] The CASG co-ordinates the management of climate and environmental risks to the financial sector, accelerates the growth of green and sustainable finance in Hong Kong and supports the HKSAR Government's climate strategies. In particular, the CASG has established a Working Group on Sustainability Disclosures[10] (WGSD) to develop the HK Roadmap.

25. Since the publication of IFRS S1 and S2, the HKICPA has been engaging in regular discussions in the WGSD to enable further deliberation at the CASG to support the development of a sustainability disclosure ecosystem for Hong Kong. Specifically, the HKICPA was tasked to conduct a TFS to identify areas where entities may need more assistance in terms of guidance, market infrastructure and/or time to get ready in applying

[8] Adapted from paragraphs 5 and 17 of the HKEX's consultation conclusions.
[9] The other members of the CASG are the Accounting and Financial Reporting Council, Environment and Ecology Bureau, FSTB, HKEX, IA and MPFA.
[10] Members of the WGSD include the CASG members and HKICPA.

the ISSB Standards in Hong Kong. The results of the TFS have been used to inform the development of the HK Standards.

26. The Institute started preparing for the TFS together with HKEX and relevant financial regulators in late 2023. This included developing various questionnaires[11] based on the feedback received from stakeholders during the 2022 HKICPA consultation on the ISSB EDs. The questionnaires also sought views from participants on the key revisions and proportionality mechanisms that had been incorporated into the final ISSB Standards in response to stakeholders' comments on the ISSB EDs.

27. During March to June 2024, the HKICPA engaged with over 80 listed entities, financial institutions, investors and industry associations to obtain substantive evidence of the practical benefits and challenges of applying the ISSB Standards in Hong Kong. Various sustainability specialists, HKEX and financial regulators also participated in the TFS meetings to share their insights and collect feedback from their respective regulatees.

28. At the TFS meetings, investors emphasised the importance for Hong Kong to align in full with the ISSB Standards in order to stay relevant at the international level and remain competitive in global trade, especially when transacting with entities in jurisdictions that impose requirements on supply chain due diligence and/or have a strong climate focus, such as the EU, US, Australia and New Zealand. Nevertheless, some preparers expressed repeated concerns about data availability and quality, challenges associated with scope 3 GHG emission disclosures, scenario analysis and anticipated financial effects, and asked for more comprehensive capacity building activities.

29. The comments raised in the TFS are consistent with those raised in the 2022 HKICPA consultation on the ISSB EDs and the 2023 HKEX consultation on enhanced climate disclosures. The HKICPA believes that many of the concerns raised by TFS participants can be adequately addressed by the changes made by the ISSB including the proportionality mechanisms introduced by the ISSB in the final standards, as well as ongoing capacity building and data and technology initiatives currently or to be undertaken by the CASG together with other relevant parties. The Vision Statement has outlined that capacity enhancement programmes will be developed for preparers, reporting and assurance professionals and sustainability-related service providers, and active efforts will be made to improve data availability, support data collection and reporting, and promote the use of green and sustainable financial technology solutions.

[11] The Institute prepared four customised versions of the questionnaire to cater to the specific circumstances of different financial industries and to include new questions in response to the publication of the HKEX's consultation conclusions in April 2024.

(g) Capacity building initiatives

30. Achieving a global baseline necessitates a strong focus on supporting implementation so that all local stakeholders can access the associated benefits. As such, the Institute has proactively launched initiatives to prepare local stakeholders for sustainability reporting over the past few years. The efforts focused on building awareness of the importance of sustainability reporting and explaining key sustainability reporting and assurance concepts. The Institute offers a wide range of trainings, workshops and publications to prepare stakeholders for the implementation of the ISSB Standards. The Institute has also enhanced the HKICPA Qualification Programme to include sustainability-related topics across different examination modules. Further details of the Institute's capacity building activities are set out in Appendix 4.

31. As a member of the ISSB's Capacity Building Partnership Framework (Partnership Framework), the Institute can leverage the implementation support activities and guidance materials of the ISSB and supplement them with local initiatives to meet local stakeholder needs. One of the key outputs of the Partnership Framework is the ISSB's Knowledge Hub which hosts a repository of case studies, good practice guidance, webinars and other useful materials designed to help preparers get ready for applying IFRS S1 and S2.

(h) Reasons for full convergence

32. The Institute is proposing to develop HKFRS S1 and S2 on a full convergence basis with IFRS S1 and S2. This decision was reached after a holistic assessment by the HKICPA of relevant factors, including local and international developments as well as substantive evidence gathered from the Institute's extensive stakeholder engagement with over 150 entities in the past two years, starting with the publication of the ISSB EDs in early 2022 and culminating in the completion of the TFS in June 2024 as detailed in the above sections.

33. The key reasons for full convergence are as follows:

    (i) The final ISSB Standards include proportionality and scalability mechanisms that cater to entities with varying capabilities and levels of maturity in sustainability reporting (see Part II(c));

    (ii) There is robust support both locally and internationally for applying the ISSB Standards, including areas which Hong Kong stakeholders find challenging (see Part II(c), (f), (g));

    (iii) The enhanced HKEX climate rules together with the HKEX April 2024 IG published in April 2024, which are highly aligned with the ISSB Standards, received broad support from the market (see Part II(d));

    (iv) Investors have emphasised the need for Hong Kong to align in full with the ISSB Standards to remain competitive and to maintain Hong Kong's status as an IFC. As the ISSB Standards sets the global *baseline* of sustainability disclosures, it is imperative for Hong Kong to meet the baseline requirements to provide global investors with consistent and comparable information for capital allocation purposes (see Part II(f)); and

(v) IOSCO has endorsed the ISSB Standards as a global framework for capital markets (see Part II(c)). IFRSF found that, as at the end of May 2024, more than 20 jurisdictions, representing nearly 55% of global GDP, over 40% of global market capitalisation and over half of global greenhouse gas emissions, have already decided to use or are taking steps to introduce ISSB Standards in their legal or regulatory framework.

34. The proposal for full convergence relates to IFRS S1 and S2 only and does not extend to any future ISSB Standards. When the ISSB publishes any new standards in the future, the Institute will engage with relevant stakeholders to decide on the potential adoption of those new standards in Hong Kong as appropriate.

(i) Proposed effective date of the HK Standards

35. The HKICPA proposes an effective date of 1 August 2025 for HKFRS S1 and S2.

36. The proposed effective date takes into account the expected time needed to finalise the HK Standards. It also strikes a balance between the urgency and importance for Hong Kong to align with global baseline sustainability disclosures, the demands of investors versus the capacity of preparers, as well as providing relevant authorities with certainty as soon as practicable for them to phase in their own reporting requirements in accordance with the HK Standards.

III. Comments requested

37. The HKICPA is requesting comments on the HK EDs by **27 October 2024**. Stakeholders are strongly encouraged to read the FAQs in Appendix 1 before submitting any comments.

38. The HKICPA is conscious of the fact that:

    (a) Hong Kong stakeholders have undergone multiple consultations on ISSB-related sustainability disclosures in recent years, especially those that are PAEs on climate-related disclosures. Past consultations have indicated that the market is generally supportive of the adoption of the ISSB Standards and the issues raised in various stakeholder engagements over the years have remained largely consistent;

    (b) stakeholders have finite capacity and there is diminishing incremental value to stakeholders to provide comments on the full set of HK EDs – which are fully converged with IFRS S1 and S2 – given all the previous related consultations;

    (c) the HKICPA, CASG and other relevant parties have already put in place a series of measures to address concerns gathered from previous consultations (see Part II(f) and (g) as well as Appendices 2 to 4); and

    (d) the consultation should encourage comments that are in addition to those previously raised (see Appendices 2 and 3) which have been or will be addressed through ongoing capacity building coupled with data and technology initiatives (see Appendices 3 and 4) to enhance efficiency and maximise value for Hong Kong stakeholders.

39. Balancing the above factors and the need for further consultation, the Institute has set a 6-week consultation period for the HK EDs and encourages respondents to take account of the overall developments on the Hong Kong sustainability disclosures ecosystem including capacity building efforts and the close alignment between the enhanced HKEX climate rules and the ISSB Standards as explained in FAQ 2 in Appendix 1 when providing any comments to this consultation.

40. Please provide a rationale for your comments to the following questions, explaining why you agree or disagree with the proposed requirements. If you disagree, kindly specify the parts of the requirements with which you disagree, provide reasons for your disagreement and propose alternative solutions if applicable.

    Question 1: Do you agree with the proposal to issue HKFRS S1 and S2 on a fully converged basis with IFRS S1 and S2 with an effective date of 1 August 2025?

    Question 2: Do you have any other comments on the HK EDs?

IV. Next steps

41. The HKICPA aims to publish the final HKFRS S1 and S2 by the end of 2024, subject to undergoing the Institute's standard-setting due process which includes an analysis of comments received on the HK EDs.

42. A public briefing in webinar format will be conducted by the Institute during the consultation period to explain the background, scope and application of the HK EDs. Further information on enrolment details will be provided in due course.

Appendices

Appendix 1 FAQs

The HKICPA has prepared the following FAQs for stakeholders' information. The HKICPA strongly encourages stakeholders to read through these FAQs before submitting comments to this consultation. The list of questions are as follows:

1. Which entities must apply the HK Standards and by when?
2. What are the main differences between the enhanced HKEX climate rules and the ISSB Standards?
3. Does full convergence with IFRS S1 and S2 mean the HKICPA has adopted a full convergence policy with all future ISSB Standards?
4. What has been done to address concerns raised by stakeholders in various ISSB Standards-related consultations in recent years?
5. What are the proportionality mechanisms in the ISSB Standards and are they included in the HK EDs?

1. Which entities must apply the HK Standards and by when?

The ISSB Inaugural Jurisdictional Guide issued in May 2024 sets out that the targeted entities for application of the ISSB Standards are PAEs. The Vision Statement states that the application of HKFRS S1 and S2 will prioritise PAEs including listed entities and regulated financial institutions in Hong Kong such as banks, fund managers, insurance companies and MPF trustees.

Relevant authorities/regulators including the HKEX, HKMA, SFC, MPFA and IA will conduct their own consultations soon to determine the approach and timing of adopting HKFRS S1 and S2, with reference made to the ISSB Inaugural Jurisdictional Guide that a jurisdiction's process completion date of the adoption or other use of ISSB Standards should be no later than end-2029. Entities that are required to prepare sustainability disclosures will continue to report in accordance with the rules, regulations or guidelines specified by relevant authorities/regulators.

Until further decisions are made by the relevant authorities/regulators, entities preparing sustainability disclosures have the sole discretion to decide whether sustainability disclosures should be prepared in accordance with the HK Standards or other frameworks.

2. What are the main differences between the enhanced HKEX climate rules and the ISSB Standards?

The HK EDs are fully converged with IFRS S1 and S2, including sustainability and climate reporting requirements.

In relation to the enhanced HKEX climate rules, there are four main differences between them and the ISSB Standards.

Participants in the TFS generally did not have any major concerns about these four aspects. Details of these four aspects, TFS participants' feedback and the HKICPA's related recommendations are summarised in the table below.

Aspects	Feedback in TFS
IFRS 1	
1. Reporting boundary: **Enhanced HKEX climate rules:** entities may decide which entities or operations to include in their ESG report. **ISSB Standards:** all entities covered by the consolidated financial statements must be included in the ESG report. *[IFRS S1.20]*	Many entities commented that their current ESG reports incorporate only those group entities and operations that are material. At first they were concerned that expanding the reporting boundary to cover all the consolidated group entities would significantly increase the number of entities within the scope of reporting. However, after clarification, they agreed that many of the currently excluded entities/operations may not be exposed to climate risks and opportunities that are reasonably expected to affect an entity's prospects or have any material information to disclose about those risks and opportunities, hence the level of additional work might not be as substantial as initially anticipated. At any rate, these participants acknowledged that they will need to review and make any necessary adjustments to their reporting scope to align with their financial statements when adopting the ISSB Standards. In addition, the HKICPA has recommended that further guidance on materiality be provided to address this issue. See Appendix 3.
IFRS S2 (the enhanced HKEX climate rules *encourage* but do not *require* the following disclosures)[12]	
2. Industry-based metrics, including certain specific disclosures for commercial banks, asset managers and insurers on financed emissions *[IFRS S2.32 and IFRS S2.29(a)(vi)(2)]*	Investors particularly supported the disclosure of industry-based metrics as they provide insights into how climate risks and opportunities affect entities within specific sectors and enable meaningful comparisons. Critics have raised concerns about the Sustainability Accounting Standards Board (SASB) classification systems, particularly regarding how to determine which sector guidance should be used and the international applicability of some metrics. However, they generally do not view these concerns as critical and recognise the ongoing efforts of the ISSB to address them. The ISSB has completed its targeted work to enhance the international applicability of the SASB standards in December 2023. Further enhancements will be made as the ISSB develops new topical standards. This is a high priority project in the ISSB's work plan for the next two years.

[12] Appendix V of the HKEX's consultation conclusions contains a table that maps the enhanced HKEX climate rules to the requirements of IFRS S2. The main differences are summarised in the 'aspects' column.

Aspects	Feedback in TFS
	Besides, while the ISSB requires that industry-based disclosures be provided and that additional information about financed emissions be provided for particular financial activities, the ISSB has changed the ‘requirement’ to follow the SASB disclosure topics and metrics in the ISSB EDs to ‘refer to and consider the applicability [there]of’ in the final standard. If these topics and metrics are deemed irrelevant, there is no requirement to apply them. This should address the concerns about SASB’s not being internationally applicable. In addition, the HKICPA has also made relevant recommendations regarding more guidance on the disclosure of industry-based metrics in the TFS report.
3. Separate disclosure of scopes 1 and 2 GHG emissions for the consolidated group from other investees *[IFRS S2.29(a)(iv)]*	This is a matter of disaggregation which is not expected to be a significant problem.
4. % of remuneration linked to climate considerations *[IFRS S2.29(g)(ii)]*	Stakeholders acknowledged that the inclusion of performance metrics in remuneration policies brings transparency to how companies incentivise management to achieve climate-related metrics and targets. On listed companies, the HKEX April 2024 IG already includes guidance on how such disclosures may be made when the remuneration linked to climate cannot be separately identified from other sustainability topics/considerations.

3. Does full convergence with IFRS S1 and S2 mean the HKICPA has adopted a full convergence policy with all future ISSB Standards?

No. The proposal for full convergence relates to IFRS S1 and S2 only and does not extend to any future ISSB Standards. When the ISSB publishes any new standards in the future, the Institute will engage with relevant stakeholders to decide on the potential adoption of those new standards in Hong Kong as appropriate.

4. What has been done to address concerns raised by stakeholders in various ISSB Standards-related consultations in recent years?

The HKICPA and various local regulators have gathered invaluable feedback from stakeholders in, amongst others:

- the 2022 HKICPA consultation of the ISSB EDs;
- the 2023 HKEX consultation on enhanced climate disclosures;

- various financial regulators' engagements with their constituents since the publication of the final IFRS S1 and S2; and
- the 2024 TFS conducted by the HKICPA together with HKEX and relevant financial regulators.

As explained in Part II of this explanatory memorandum, similar comments have been raised in these stakeholder engagements. Many of these concerns have been addressed by the ISSB through amending their original proposals (see Appendix 2) – most notably through embedding proportionality mechanisms in the ISSB Standards to cater to entities with different capabilities and maturities in sustainability reporting (see FAQ 5) – as well as ongoing capacity building coupled with data and technology initiatives currently undertaken by the CASG and other relevant parties (see Appendix 3).

The Vision Statement has outlined that capacity enhancement programmes will be developed for preparers, reporting and assurance professionals and sustainability-related service providers, and active efforts will be made to improve data availability, support data collection and reporting, and promote the use of green and sustainable financial technology solutions. The Institute has also issued two pieces of education guidance[13] in early 2024 to enhance awareness and understanding of the concepts of proportionality and scalability.

In addition, the HKICPA has a holistic capacity building framework ranging from pre-qualification education to post-qualification training and publication of guidance materials to assist stakeholders in applying the HK/ISSB Standards (see Part II(g) and Appendix 4).

5. **What are the proportionality mechanisms in the ISSB Standards and are they included in the HK EDs?**[14]

The HKICPA's proposal of full convergence with IFRS S1 and S2 means that the full range of proportionality mechanisms embedded in the ISSB Standards are available in the HK EDs.

In deliberating stakeholder comments on the ISSB EDs, the ISSB acknowledges that entities have different levels of readiness as well as skills, resources and capabilities to apply the ISSB Standards. In order to make the ISSB Standards truly scalable to cater to different entities' ability to make sustainability disclosures, the ISSB has introduced two key proportionality mechanisms into the ISSB Standards, namely:

(i) The 'reasonable and supportable information that is available at the reporting date without undue cost or effort' mechanism; and

(ii) the 'skills, capabilities and resources available to the entity' mechanism.

The concept of 'reasonable and supportable information that is available at the reporting date without undue cost or effort' is intended to help entities provide the disclosures required by the ISSB Standards in areas in which there is a high level of measurement or outcome uncertainty.

[13] Two important ideas in IFRS S1 and IFRS S2 to facilitate proportionality and scalability; and Considerations of Skills, Capabilities and Resources in Climate-Related Scenario Analysis.

[14] The information in this FAQ is adapted from paragraphs 18 to 23 of the ISSB Inaugural Jurisdictional Guide.

The concept, which has previously been used by the International Accounting Standards Board, will support entities by guiding them to consider information that is reasonably available and by clarifying that they need not carry out an exhaustive search for information.

The concept of 'skills, capabilities and resources available to the entity' allows entities to apply qualitative approaches (instead of quantitative approaches) in several instances in IFRS S1 and S2. This concept was introduced to ensure that entities are able to apply the requirements in a way that is proportionate to their circumstances while still providing useful information to investors.

The table below summarises the proportionality mechanisms in IFRS S1 and S2:

	Information used limited to what is reasonable, supportable and available without undue cost or effort	**Qualitative approaches allowed if an entity lacks skills, capabilities or resources**
Determination of anticipated financial effects	Yes	Yes
Climate-related scenario analysis	Yes	Yes
Measurement of scope 3 GHG emissions	Yes	N/A
Identification of risks and opportunities	Yes	N/A
Determination of the scope of the value chain	Yes	N/A
Calculation of metrics in some cross-industry categories	Yes	N/A

The introduction of proportionality mechanisms in IFRS S1 and S2 is intended to assist entities particularly when the ISSB Standards are first applied. Guidance on key requirements (including illustrative examples) is provided in the ISSB Standards to aid application. These mechanisms are likely to be particularly helpful for those entities that might be less able to comply with the disclosure requirements in the Standards.

Appendix 2 High-level analysis of HKICPA comments on the ISSB EDs v. final ISSB Standards

A high-level analysis of whether the final IFRS S1 and S2 have addressed the major comments of Hong Kong stakeholders raised on ISSB EDs in 2022 is set out below.

Overall, we consider that the major comments of local stakeholders have been considered and addressed where appropriate. Nevertheless, we recognise that further guidance on certain aspects of the standards would be helpful, e.g. issues relating to data availability and quality in particular for scope 3 GHG emissions disclosures, scenario analysis and anticipated financial effects. These issues are consistent with those raised in the TFS. Details of these comments and our recommendations for addressing them are set out in Appendix 3.

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
1	Materiality	It is highly subjective and judgmental in terms of how to determine materiality for disclosing sustainability-related information. The ISSB is recommended to specify the factors that an entity should consider when determining materiality, e.g. the likelihood and impact of the event, its frequency of occurrence, duration, etc.	The ISSB confirmed that IFRS S1 uses a definition of materiality that is aligned with that used in IFRS Accounting Standards. The ISSB is committed to providing guidance to help entities identify material information for disclosure purposes. Comments were addressed. Key recommendations on capacity building activities with respect to materiality are set out in Appendix 3.
2	Comparative information	Adjustment for all changes in estimates retrospectively will create a disconnection between prior year sustainability information and financial statements information. The ISSB is recommended to distinguish between different types of changes in estimates and depending on the nature of change, adjust for it retrospectively or prospectively as appropriate.	The ISSB has provided further guidance in the final standard (IFRS S1.B50-53) specifically to address the following circumstances where an entity is required to provide revised comparative information: • When an entity identifies new information related to the estimated amount disclosed in the preceding period, and this new information provides evidence of circumstances that existed during that period. • When an entity redefines or replaces a metric in the reporting period.

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
			• When an entity introduces a new metric in the reporting period. In addition, the ISSB revised the proposed requirement, stating that an entity would not need to disclose a revised comparative amount for a metric if the metric is forward-looking (IFRS S1.B51(b)). Comments were addressed.
3	Current and anticipated financial effects	The [draft] IFRS S2 requires an entity to disclose quantitative information unless it is unable to do so. However, it is unclear what "unable to do so" means. In addition, while it may be appropriate to provide quantitative information for short- to medium-term expectations, it may be more appropriate to provide qualitative information for long-term expectations due to the lack of reliable data for the long term. Besides, there are concerns about the usefulness of isolating the anticipated effects of climate-related risks and opportunities from other risks and opportunities as many of the ESG risks are interlinked and it is difficult to isolate one assumption/input from another to estimate each risk's standalone effect. The end result of any arbitrary disaggregation could potentially be misleading.	Although an entity is required to provide both quantitative and qualitative information about current and anticipated financial effects (IFRS S1.35 and IFRS S2.16), the ISSB established criteria for when an entity need not provide quantitative information about the financial effects of a sustainability-related risk or opportunity (IFRS S1.38 and IFRS S2.19). In particular, quantitative information on anticipated financial effects is not required if an entity lacks the skills, capabilities or resources to do so (IFRS S1.39 and IFRS S2.20). Furthermore, an entity need not provide quantitative information for current or anticipated financial effects of a climate-related risk or opportunity if (a) those effects are not separately identifiable; or (b) if they are subject to such a high level of estimation uncertainty that the resulting disclosure would not be useful (IFRS S2.19). If an entity is unable to provide quantitative information, it would be required to provide qualitative information and other information, including an explanation for why it was unable to provide quantitative information (IFRS S1.40 and IFRS S2.21). Comments were largely addressed. Since it would be challenging to isolate climate effects from other factors,

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
			making it difficult to determine the specific impact of climate-related events on financial outcomes, further guidance would be developed in this aspect to help address this issue. Key recommendations on capacity building activities with respect to anticipated financial effects are set out in Appendix 3.
4	Scenario analysis	Climate scenario analysis requires a large amount of data and resources depending on the methodology used, and this may be difficult for entities with limited access or knowledge on related topics. The ISSB is recommended to specify how many and which type of scenarios should be disclosed citing the more common and publicly available scenarios as examples, as well as include the drivers/factors that each scenario should consider to increase comparability between entities and facilitate application of the requirements. Furthermore, the ISSB should require disclosure of significant drivers, methodologies, estimates and assumptions used in the scenario analysis.	The ISSB clarified that the method of climate-related scenario analysis might range from solely qualitative scenario narratives to sophisticated quantitative modelling. An entity could use a method of scenario analysis commensurate with its skills, capabilities and resources, and the degree to which the entity is exposed to climate-related risks and opportunities. (IFRS S2.B1-B18) The ISSB has decided: • not to specify the particular scenarios that an entity would be required to use in its climate-related scenario analysis because the relevant scenarios would depend on the entity's facts and circumstances. The ISSB considered that specifying which scenarios an entity should use would not be practical, might quickly become outdated and could lead to the disclosure of information that does not reflect the entity's specific circumstances or management's view of what is plausible (IFRS S2.BC67). • not to require the use of scenarios consistent with the latest international agreement on climate change or particular science-based scenarios (IFRS S2.BC67).

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
			• to require disclosure of the key assumptions made in the analysis, as well as relevant judgments and measurement uncertainties (IFRS S1.74-82). In addition, the ISSB is committed to developing guidance to assist entities in applying the requirements and putting entities on a path to develop their capabilities and strengthen their disclosures over time as needed. Comments were largely addressed. Key recommendations on capacity building activities with respect to scenario analysis are set out in Appendix 3.
5	Scope 1 and scope 2 GHG emissions for associates, joint ventures, unconsolidated subsidiaries or affiliates (non-controlling investments)	There are many known challenges in terms of financial reporting where information from non-controlling investments is not easy to obtain due to a lack of control. For greenhouse gas emissions, the challenges could be further complicated by the investee's (i) using a societal value approach; (ii) using a method that is not "GHG Protocol aligned"; (iii) using an operational control method while the reporting entity uses equity share method; and (iv) having a different period-end as that of the reporting entity. Furthermore, the ISSB is recommended to consider requiring the use of consistent methodologies, such as measurement approach, by the reporting entity and its non-controlling investments, similar to IFRS Accounting Standards requiring associates and	For scopes 1, 2 and 3 GHG emissions, the ISSB has decided to allow a reporting entity to use information from value chain entities for a different reporting period if those entities have a different reporting period from that of the reporting entity, subject to certain conditions (IFRS S2.B19). Apart from the above, the practical challenges listed alongside were not addressed by the ISSB. As these issues have existed for a long time in financial reporting, the Institute considers that entities should establish a consistent methodology and reporting timeline to collect information from their non-controlling investments for sustainability reporting purposes.

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
		joint ventures to use consistent accounting policies as the group.	
6	Scope 3 GHG emissions	It is difficult to obtain high-quality and reliable source data for scope 3 GHG emissions as they fall outside an entity's direct management. The ISSB is recommended to allow a phased approach for the relevant disclosure and require quantitative information only when the practice becomes more mature and information becomes more reliable. Furthermore, the ISSB should provide guidance to assist entities in determining how many levels up and down the value chain they should disclose for scope 3 GHG emissions or refer stakeholders to relevant existing literature.	The ISSB introduced reliefs and guidance to address the data availability and data quality challenges raised by stakeholders: <u>Reliefs</u> • a transition relief that exempts entities from disclosing scope 3 GHG emissions in the first annual reporting period (IFRS S2.C4(b)). • relief to address challenges associated with data from entities in the value chain that have different reporting periods from that of the entity, subject to certain conditions (IFRS S2.B19). <u>Guidance (IFRS S2.B32-B57)</u> The ISSB acknowledged that scope 3 measurements are expected to be imperfect and will invariably have to rely on estimation. To assist with the estimation process, the ISSB has developed a scope 3 measurement framework (part of the application guidance in IFRS S2) with extensive guidance in the final standards on how an entity should categorise and prioritise the inputs used to measure scope 3 GHG emissions. By requiring entities to prioritise the use of measurement approaches, inputs and assumptions that possess particular characteristics, the ISSB believes that it would enable entities to faithfully represent their scope 3 GHG emissions. The ISSB also decided that an entity is required to use "all reasonable and supportable information that is available to

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
			the entity at the reporting date without undue cost or effort" to measure its scope 3 GHG emissions (IFRS S2.B39). In other words, it doesn't have to be an exhaustive search. Comments were largely addressed. Furthermore, the ISSB will develop additional guidance, particularly regarding the use of estimation in providing scope 3 information and determining the extent to which entities should disclose emissions levels up and down the value chain for scope 3. Key recommendations on capacity building and data and technology activities with respect to scope 3 are set out in Appendix 3.
7	Financed emissions and facilitated emissions	Draft IFRS S2 proposed financed and/or facilitated emissions disclosure requirements for activities associated with four industries in the financials sector: asset management, commercial banks, insurance and investment banking & brokerage. Stakeholders' concerns are as follow: • Data availability of financed emissions: Stakeholders commented that the proposal assumes that emissions information can be obtained during due diligence or loan drawdown, although there may be a time lag. However, reporting ongoing scope 3 GHG emissions from borrowers alongside financial statements may be impractical due to the volume of data. • Whether associated emissions are within the scope of financed emissions: This	On financed emissions, the ISSB confirmed the proposed requirements for entities participating in activities associated with three industries—Asset Management, Commercial Banks and Insurance—to disclose specific information about financed emissions as part of their scope 3 GHG emissions disclosures. Being part of scope 3 GHG emission disclosures, the reliefs and guidance introduced by the ISSB to address the data availability and quality issues, as mentioned above, would also apply to financed emissions. The ISSB further clarified that IFRS S2 requires financed emissions disclosure only for insurance-related financial activities associated with an insurer's assets. In other words, IFRS S2 does not require disclosure of the "associated emissions" of underwriting portfolios in the insurance and reinsurance industries. (IFRS S2.BC129) On facilitated emissions, the ISSB decided not to proceed with the proposed requirement for an entity participating in

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
		relates to the disclosure of scope 3 GHG emissions associated with underwriting portfolios for insurers and reinsurers (i.e. the liability side). Stakeholders are seeking clarity on whether these associated emissions should be included in the broader category of financed emissions for disclosure purposes. • Definition of facilitated emissions: This relates to the disclosure of scope 3 GHG emissions from activities such as underwriting, securitisation and financial advisory services (i.e. typically off-balance sheet activities). Stakeholders would like the ISSB to provide clarification on the definition of "facilitated emissions" to determine the scope of disclosure. • Lack of established methodologies for estimating financed emissions, facilitated emissions and associated emissions.	investment banking & brokerage activities to disclose its facilitated emissions. The ISSB made this decision citing the lack of a widely accepted calculation methodology and the additional work needed to establish one based on respondents' feedback. Besides, the ISSB considered the application guidance in IFRS S2.B58-B63 would enable the market to converge on measurement methodologies for different asset classes as they emerge and gain acceptance, such as those developed by the Partnership for Carbon Accounting Financials (PCAF). Although the requirements support the use of different measurement approaches, they also provide users of general purpose financial reports with the information necessary to understand an entity's exposures and the approaches the entity has used to measure its financed emissions (IFRS S2.BC125). Comments were addressed. The Transition Implementation Group on IFRS S1 and S2 will be having further discussions on practical questions submitted by stakeholders on financed, facilitated and insurance-associated emissions at its September 2024 meeting.
8	Appendix B of [draft] IFRS S2 (Industry-based disclosure requirements)	Certain metrics in Appendix B might still not be applicable in many jurisdictions even though attempts have been made to internationalise them. This might hinder international adoption of the standard as entities might be prevented from asserting compliance with IFRS S2 given Appendix B is an integral part of the standard. It is recommended that Appendix B not be made mandatory until the ISSB has conducted	The industry-based disclosures in Appendix B of the draft IFRS S2 are no longer mandatory in the final ISSB Standards. Instead, the ISSB now requires entities to "refer to and consider the applicability of" the industry-based disclosure topics and industry-based metrics described in the industry-based guidance on implementing IFRS S2 in identifying risks and opportunities and preparing its industry-based disclosures (IFRS S2.12 and 32). In other words, if the

#	Area	Major comments on the ISSB EDs	High level analysis against the final ISSB Standards
		further industry-wide consultations and made relevant updates thereto to ensure the metrics in Appendix B can truly serve as an international baseline for global adoption.	industry-based metrics included in IFRS S2 are not considered to be applicable, they need not be disclosed and alternative industry-based information can be provided. The ISSB is also committed to continuing to enhance the international applicability of and to update the SASB standards (which form the basis of the ISSB industry-based guidance) as part of its 2024-2026 work plan. Comments were addressed.
9	Effective date	It is recommended that a phased approach be allowed for certain disclosures such as scope 3 GHG emissions, scenario analysis as well as emissions for non-controlling investments and financed emissions. If an entity takes this approach, it should explain why certain requirements have not been complied with and the expected timeline for compliance. This may encourage more uptake by entities and allow an earlier effective date for the other requirements of the standards.	Instead of a phased approach, the ISSB has decided to enable entities to focus their initial efforts on providing climate-related information specifically tailored to investor needs. As a result, a temporary relief has been provided, allowing entities to choose to report only on climate-related risks and opportunities in their first year of reporting. In addition, the ISSB has incorporated several transition reliefs relating to the timing of reporting, the GHG Protocol, and scope 3 GHG emissions. Comments were addressed. Furthermore, as regards when the HK Standards will be mandatory for Hong Kong stakeholders, it will be a decision to be made by relevant authorities in Hong Kong. See FAQ 1 in Appendix 1.

Appendix 3 Observations from the technical feasibility study and recommendations

A summary of the key comments raised by TFS participants is set out in the table below. While some comments have already been addressed, others require additional attention through various capacity building coupled with data and technology initiatives in Hong Kong. The HKICPA has made various recommendations (denoted by an '**R**' in the table below) to the CASG in August 2024 to address these challenges. Furthermore, given the proposed full convergence with the ISSB Standards, Hong Kong stakeholders can leverage the ISSB's Transition Implementation Group on IFRS S1 and IFRS S2 which will provide ongoing technical advice on the implementation of IFRS S1 and S2.

#	Comments	Details
1.	Data availability and quality; incremental value of additional guidance	Participants were concerned that Hong Kong lacks critical HK-specific emission factor and physical climate risk scenario databases which are essential for scope 3 disclosures and performing scenario analysis. They also struggle with identifying relevant guidance and trainings as there are too many overlapping generic materials in the market at the moment. **R:** Centralised resource centres have been set up by different organisations such as CASG members, large accounting firms and the Institute amongst others. Resource Centre for Sustainability Standards by the HKICPA provides centralised technical publications and reference materials relevant to sustainability reporting, assurance and ethics.
2.	Interoperability	Participants were concerned about the interoperability between different jurisdictions' sustainability standards. Having interoperability is crucial for businesses with a global footprint, those that are listed in various jurisdictions and those that are subject to regulatory reporting requirements e.g. financial institutions. **R:** The full convergence of HK Standards with ISSB Standards would address this concern effectively.
3.	Different perceptions amongst different stakeholders about the purpose of	There are varied views about the purpose of sustainability disclosures: • *Preparers* prioritise data availability, accuracy and precision to achieve favourable ESG ratings and regulatory compliance. • *Investors* place greater emphasis on high-quality narratives on an entity's responses to identified risks and opportunities rather than precise quantitative numbers.

#	Comments	Details
	sustainability disclosures	• *ESG rating agencies* leverage AI to scan sustainability reports for specified quantitative and qualitative disclosures. Failure to include key words would result in AI's not picking up the disclosure, leading to a lower rating. This pushes entities towards generic disclosures. As a result, there is a disconnection between disclosures, ESG ratings, investment decisions and regulatory objectives. **R:** To relieve this concern, there should be more multilateral discussions between preparers, investors, regulators and ESG service providers to align priorities and expectations. Talents in carbon accounting and sustainability reporting must also be cultivated in Hong Kong.
4.	Misconception about the ISSB Standards	There is a misconception that there is still a big gap between the enhanced HKEX climate rules and the ISSB Standards. Participants are also not aware of the proportionality reliefs in the ISSB Standards. **R:** It is important for listed entities to note that the current requirements under the enhanced HKEX climate rules are closely aligned with IFRS S2. Also, enhancing market awareness of the proportionality reliefs in ISSB Standards is vital.
5.	Demand for phased approach	Participants found it imperative to take a phased approach for any potential adoption of the ISSB Standards (i.e. climate-first and more resourceful entities-first) and the requirement of scope 3 disclosures, to allow time for the data infrastructure to mature as well as for preparers and other professionals to build up experience. **R:** This concern would primarily be addressed through the following measures: • The Vision Statement indicates that the application of HKFRS S1 and S2 will prioritise PAEs such as listed entities and regulated financial institutions in Hong Kong. • The implementation of the enhanced HKEX climate rules will be phased in to cater to different entities' ability to make sustainability disclosures. These rules serve as an interim step to prepare listed entities for the eventual adoption of the HK Standards when they are available, subject to further consultation by HKEX. • The transition reliefs and proportionality mechanisms in the HK Standards through the proposed full convergence with the ISSB Standards will further address this concern.

#	Comments	Details
		The ISSB is also developing guidance on proportionality mechanisms which can be leveraged by local stakeholders.
6.	Materiality	The concerns revolve around: • Identifying material information effectively. • Transitioning from the reporting boundary concept in the enhanced HKEX climate rules to that in the ISSB Standards by applying the materiality concept. • Aligning the materiality threshold used for sustainability reporting with that used in the financial statements. • Conducting a thorough materiality assessment that can: (i) identify material information for disclosure, and (ii) provide sound justifications for not disclosing certain information deemed immaterial. **R:** Targeted training and development of industry relevant best practice is crucial to address the above concerns. The ISSB is also developing guidance on materiality and decision-useful information which can be leveraged by local stakeholders.
7.	Scenario analysis	There are concerns regarding the absence of the following: • HK-specific physical climate risk scenarios; • HK-specific transition risks; and • Industry-specific climate scenarios. It is worth noting that the HKMA has launched a beta version of the Physical Risk Assessment Platform. This platform comprises an analytical tool which allows users to assess the potential impact of physical risks on residential and commercial buildings in Hong Kong under different climate scenarios and a database of more than 40 public data or data sources related to physical risk. **R:** Industry associations can play a key role in sharing best practices amongst industry members and how peers have overcome or are overcoming sustainability reporting challenges that may be unique to that industry, as well as in developing industry-specific guidance as they possess the necessary industry expertise to ensure the resulting guidance would be fit-for-purpose. Other recommendations include:

#	Comments	Details
		• Promoting the value of scenario analyses to an entity; • Increasing awareness of the relevant guidance from the HKEX April 2024 IG and their Guidance on Climate Disclosures (November 2021) amongst others on physical and transition climate risks; and • Guiding stakeholders to identify HK-specific transition risks for their businesses and their potential financial effects. The ISSB is also developing guidance on climate-related scenario analysis which can be leveraged by local stakeholders.
8.	Anticipated financial effects	Participants' key concerns are summarised below: • As some participants doubt the credibility of scenario models and hence their outputs, they are hesitant to disclose quantitative results as they might deter investors from investing in the entity; • Challenges in isolating climate effects from other factors when trying to quantify the financial impact; • Changes in business practice may turn what was once a climate opportunity into a business-as-usual case over time so it may be difficult to distinguish between them when forecasting into the future, not to mention trying to quantify their anticipated financial effect; and • General scepticism about forecasting financial impacts accurately. **R:** Multilateral discussions between preparers, investors, regulators, ESG rating agencies and other relevant stakeholders would be key to align expectations and understanding between the various parties so as to create a 'safe space' for preparers to explore with new disclosures. Similar to the recommendation for scenario analysis, industry associations can play a key role in sharing best practices amongst industry members and in developing relevant trainings and industry-specific guidance as they possess the necessary industry expertise to ensure the resulting guidance would be fit-for-purpose. These could include: • Highlighting the ISSB webcasts and the HKEX April 2024 IG which illustrates what to disclose when quantitative information is not available or when high-level quantitative information would suffice; • Case studies on how to work out anticipated financial effects by using publicly available scenarios;

#	Comments	Details
		• Strategy for achieving internal alignment between the finance team and sustainability team when performing financial and climate projections; • Approach to integrating climate risks and mitigation activities into the overall enterprise risk management; • Methods to isolate climate factors from other factors and how to make relevant disclosure if distinction is not possible; and • How to determine anticipated financial effects from net zero commitments and other targets, as well as the way in which the resulting disclosures of anticipated financial effects connect with the amounts recognised or disclosed in the financial statements.
9.	Scope 3 GHG emission disclosures and data quality	There are three layers to the scope 3 problem: 1) Many companies mistakenly believe they must gather direct emission data. They struggle to obtain direct carbon data from suppliers and customers especially when dealing with state-owned entities or individuals like farmers and mine owners. Obtaining data from associates is also a challenge as the group has no control over them. 2) Companies that are using raw operational data to derive GHG emission estimates instead of direct emissions are hindered by the laborious internal processes of collecting and reporting data internally. Training frontline staff in various locations, often with limited education levels, to record specific data is time-consuming and is met by resistance due to the additional workload without apparent benefits. 3) For those who have overcome the hurdle of collecting raw operational data, they are hesitant to rely on the estimates used to determine scope 3 GHG emissions due to lack of comparability and consistency: a) The absence of HK- and PRC-specific emission factor databases means entities have to use foreign data that may not accurately reflect the emission profiles from Hong Kong or the PRC; b) Discrepancies in emission factors across databases for similar goods or services; c) Incomplete or outdated coverage in some databases, impacting accuracy;

#	Comments	Details
		d) Varied methodologies such as spend-based v. activity-based factors causing different emission results for the same goods or services; and e) Different assumptions among companies can lead to the inconsistency and incomparability of emissions calculations. **R:** Trainings, sharing best practices amongst industry players and developing technology solutions would be key to addressing the above concerns: 1) In terms of the three layers to the scope 3 problem: a) Emphasise there is no need to use direct emissions. b) Internal processes: remind stakeholders it is the initial set-up that takes time as with all new processes. Once staff are trained it will be less onerous. Stress the need to set up workflows and processes; templates for data collection; develop systems, procedure manuals with screenshots; conduct internal trainings throughout the group; and make a habit of regular reporting. c) Use of estimates: encourage stakeholders to adopt best practices and remind them to be transparent and consistent with the use of methodologies, inputs and assumptions; disclose how and why management has changed them and the impact. Reiterate that data challenges will remain for some time so the use of proxy data is not only inevitable but acceptable.[15] Share that investors take data reliability seriously and they take it upon themselves to perform robust due diligence on the proxy data or estimates obtained to reduce data quality risks to an acceptable level. Remind stakeholders that they have been using estimates, proxy data and statistical modelling for financial reporting purposes so there is no need for such concern over their use in carbon accounting. 2) Train preparers to do things step by step (even banks and other large financial institutions take this approach): a) Use spend-based data to identify GHG emission hotspots;

[15] IFRS S1.79 states that 'the use of reasonable estimates is an essential part of preparing sustainability-related financial disclosures and does not undermine the usefulness of the information if the estimates are accurately described and explained. Even a high level of measurement uncertainty would not necessarily prevent such an estimate from providing useful information.'

#	Comments	Details
		b) For identified hotspots, use activity-based data to determine more precise GHG emissions for those activities; c) For major emission-generating activities, target the largest suppliers and customers for mutual sharing of information on emissions (some value chain entities may already be disclosing such data publicly); d) Consider collecting direct data from more suppliers and customers when disclosures and market infrastructure are more mature. 3) Emphasise that spend-based and activity-based data are available from an entity's own activities and expenditure records, i.e. no need to collect data from suppliers. 4) Remind stakeholders they can use a range for scope 3 estimates: there is no need to disclose a single amount. 5) Encourage the development of technology solutions to support the needs of preparers in data collection. 6) Enhance awareness and access to key PRC emission factors.[16] 7) Explore ways to increase awareness and usage of the GHG emissions calculator and estimator, as well as to enhance the SME Questionnaire to make it more relevant to a typical SME in Hong Kong. This would help entities in the value chains of PAEs to report GHG emission data to the latter thereby assisting PAEs in their scope 3 reporting obligations.
10.	Financed emissions and facilitated emissions	The financial sector, including banks, fund managers, insurance companies and MPF trustees, expressed the following concerns about scope 3 financed and facilitated emissions: 1) Limited emissions data from investees: There is currently no mandatory carbon reporting requirement for many investees, especially unlisted ones and those in the South-East Asian region. Where data is available, they may be incomplete, outdated or inaccurate.

[16] - 2021 national, regional and provincial CO_2 emission factors for electric power published by the PRC Ministry of Ecology and Environment (MEE) in April 2024;
- Average emission factor of purchased electricity in China published by the MEE;
- Emission factors of purchased electricity in China by region published by the MEE; and
- Emission factors of fuel used in mobile combustion published by the NDRC.

#	Comments	Details
		2) Lack of established methodologies: There are no standardised approaches for calculating financed or facilitated emissions. Specifically: a) insurers and reinsurers are concerned about estimating financed emissions associated with underwriting portfolios, especially for policyholders that are individuals (as opposed to corporates). b) banks are concerned about estimating facilitated emissions from off-balance sheet activities such as underwriting, securitisation and financial advisory services. 3) Data credibility and reliability issues: There is a general concern about the credibility and reliability of data sourced from data vendors due to the different methodologies and statistical models used by them, as well as the fact that many of the raw data from publicly available sources may not be assured or are subject to different levels of assurance as defined in different assurance standards. **R:** We have the following observations and recommendations to address these issues: 1) The enhanced HKEX climate rules could alleviate the data availability concern to a certain extent by mandating scope 1 and 2 GHG emission disclosures and adopting a comply-or-explain approach for scope 3 disclosures from 2025, transitioning to mandatory scope 3 disclosures for large-cap issuers from 2026. 2) There are collaboration between various stakeholders globally such as PCAF, climate scientists, financial institutions and regulators to develop credible methodologies to estimate financed emissions. 3) Collaboration between regulators and industry associations to align expectations and explore developing industry-specific guidance. 4) Promoting the observance of the principles in the draft Code of Conduct for ESG ratings and data products providers.[17] 5) In terms of insurance-associated emissions (for underwriting portfolios) and facilitated emissions, IFRS S2.BC129 notes that the standard does not require such disclosures citing a lack of established methodologies. The ISSB's Transition Implementation Group will discuss this issue in its September 2024 meeting and the HKICPA will monitor the discussions and engage with relevant parties as appropriate.

[17] The consultation period for the draft Code ended in June 2024 and it is now being finalised.

#	Comments	Details
11.	Lack of capacity and resources in SME financial institutions	Smaller asset managers, banks, insurers and MPF trustees, especially those not forming part of global networks, face practical difficulties in meeting the technical requirements in the ISSB Standards due to limited capacity, resources and data availability. The challenges are particularly acute for the Hong Kong insurance industry due to the predominance of SMEs in that industry. Many of those SMEs claim that they are not exposed to significant climate risks or opportunities and believe that the costs of implementing the ISSB Standards would outweigh the benefits. This issue is exacerbated by the potential of having to prepare sustainability disclosures at the same time as other statutory and regulatory reporting obligations, such as the preparation of financial reports and risk-based capital disclosures. **R:** The Vision Statement indicates that the application of HKFRS S1 and S2 will prioritise PAEs such as listed entities and regulated financial institutions in Hong Kong. As stated in the ISSB Inaugural Jurisdictional Guide, PAEs should have a significant weight in the jurisdiction.

Appendix 4 Capacity building activities at the HKICPA

The HKICPA has established a comprehensive, three-tiered sustainability training curriculum which will be rolled out in phases:

- First tier: builds awareness of the importance of sustainability reporting, the role of the ISSB and its standards;
- Second tier: teaches the key sustainability reporting and assurance concepts; and
- Third tier: focuses on the technical details of IFRS S1 and S2.

The HKICPA formulates the sustainability curriculum to provide trainings that align with market developments. For example:

- **Before the establishment of the ISSB in November 2021:** the HKICPA has established a Sustainability Information Centre to share thought leadership articles and offered various ESG-related trainings before November 2021, including HKEX ESG reporting requirements. The ESG Information Centre is updated regularly to reflect local and international developments.
- **HKEX's consultation on enhanced climate-related disclosures and the publication of IFRS S1 and S2 in H1 2023:** the HKICPA organised five deep-dive workshops around that time (with re-runs) covering topics such as sustainability governance and risk management, TCFD scenario analysis, carbon accounting, decarbonisation strategy, as well as reporting and assurance. These workshops have been recognised as eligible programmes in the Pilot Green and Sustainable Finance Capacity Building Support Scheme established by the HKSAR Government.
- **October 2023 Policy Address and March 2024 Vision Statement's message to align with ISSB Standards:** a series of webinars on detailed aspects of IFRS S1 and S2 per the three-tiered sustainability training curriculum were held in Q2 2024.
- **Publication of enhanced HKEX climate rules and the Mainland Stock Exchanges' ESG guidelines in April 2024:** a series of webinars and workshops have been organised since June 2024 and will continue to be held to take stakeholders through these new requirements.
- **In anticipation of the publication of the HK Standards and to address observations from the 2022 HKICPA's consultation on the ISSB EDs and TFS:** the HKICPA will hold a series of public briefings, webinars and workshops from H2 2024 onwards on an ongoing basis to discuss the application of the standards specifically in the Hong Kong context, covering topics where stakeholders have repeatedly raised concerns such as identifying material information, the reporting entity boundary concept, industry-based metrics, anticipated financial effects, scenario analysis and scope 3 GHG emissions. See Appendix 3 for details.

The HKICPA will review the sustainability training curriculum periodically when key events occur (e.g. when new rules/standards are published) and adjust it as appropriate to align with the evolving landscape. This will help prepare Hong Kong stakeholders for the implementation of HK Standards in a gradual and progressive manner.

In addition to trainings, the HKICPA will continue to identify implementation issues of HKFRS/IFRS S1 and S2 through submissions to the implementation support platform (amongst other means) for potential guidance and/or trainings as appropriate. The platform is scheduled to be launched in Q4 2024.

The HKICPA also launched the Sustainability Community in phases starting in June 2024 to engage with stakeholders beyond accountants to share knowledge, raise awareness of best practices and provide education.