[Speech by SFST at Hong Kong Institute of Chartered Secretaries 11th Biennial Corporate Governance Conference (English only)]

Following is the speech by the Secretary for Financial Services and the Treasury, Mr James Lau, at the Hong Kong Institute of Chartered Secretaries 11th Biennial Corporate Governance Conference today (September 14):

Professor King (Chairman of the International Integrated Reporting Council, Professor Mervyn King), David (President of the Hong Kong Institute of Chartered Secretaries, Mr David Fu), distinguished guests, ladies and gentlemen,

Good morning. I am delighted to be here with you at this conference organised by the Hong Kong Institute of Chartered Secretaries. As the theme of today's conference suggests, we are indeed seeing a new horizon for corporate governance, both in Hong Kong and around the world. Let me share briefly with you a few thoughts on the issues and challenges arising from two global trends. First, there are the challenges for corporate governance associated with emerging and innovative sectors in the new economy. The second relates to green investing as many corporates embrace environmental, social and governance (ESG) standards in their business.

To begin with, one of the major reforms I have been involved with in my tenure as Secretary has been the new listing regime for emerging and innovative companies. This came into effect on April 30 this year, permitting new economy firms with a weighted voting rights (WVR) structure to list on the Main Board of the Stock Exchange of Hong Kong. Aside from the elevated requirements for market capitalisation and revenue, the company must also be an innovative company and demonstrate a track record of high business growth.

One of the main arguments in support of the WVR structure is that the enhanced voting rights given to companies' founders allow them to focus more on long-term performance and less on short-term market pressures. They also allow founders to maintain control over the strategic direction of the company and prevent unwanted takeover attempts.

There are, however, concerns that there could be abuse of the voting powers of those shareholders with WVR. It is therefore necessary to put in place safeguards to address these concerns. In fact, Hong Kong is the first jurisdiction to have a full-fledged regulatory regime governing the listing of WVR companies, or in some cases they called them dual-class shares, and we have a comprehensive package of safeguards for the investing public.

I will just briefly outline them for you. The first safeguard we have put in place is ring-fencing to permit only new applicants to list with a WVR structure. After listing, issuers with a WVR structure will be prohibited from increasing the proportion of WVR shares in issue.

Secondly, an issuer with a WVR structure must establish a corporate governance committee that comprises only independent non-executive directors. This committee will review and monitor potential conflict of interest between the issuer, its subsidiary or shareholders on the one hand and any beneficiary of weighted voting rights on the other. The board of directors needs to consider the recommendations of the corporate governance committee fully, and they need to comply or they have to explain.

Thirdly, enhanced disclosure. WVR stock counters must have a name suffixed with the marker "W". There must also be disclosure and health warning on the front page of all listing documents, periodic financial statements, circulars, notifications and announcements.

Fourthly, protection of non-WVR shareholders' right to vote. Non-WVR shareholders must be able to convene an extraordinary general meeting and add resolutions to the agenda. The minimum stake required to do so must be no higher than 10 per cent of the voting rights on a one-share, one-vote basis.

Fifthly, a number of key matters must be decided on a one-share, one-vote basis. These include changes to the listed issuer's constitutional documents, variation of rights attached to any class of shares, the appointment or removal of independent non-executive directors, the appointment or removal of auditors and the voluntary winding-up of the issuer.

Sixthly, WVR beneficiaries must be an individual who has an active executive role within the business, and is contributing to a material extent to the growth of the business. WVR beneficiaries must be directors of the issuer at listing and remain as directors afterwards.

Seventhly, any class of shares conferring WVRs must not entitle the beneficiary to more than 10 times the voting power of ordinary shares.

Lastly, we have built in event-based sunset clauses. The WVR rights attached to a beneficiary's shares will cease upon transfer of the beneficial ownership of those shares or the control over the voting rights attached to them. Such rights will also lapse permanently if a beneficiary dies, ceases to be a director, or is deemed by the Stock Exchange to be incapacitated or no longer meet the requirements of a director as set out in the listing rules.

Among the above safeguards, a question has been raised as to whether WVR beneficiaries can be corporate entities. This is a complex subject, raising governance issues such as whether this would mean perpetual WVR rights; whether there should be further restrictions on the exercise of corporate WVR rights; sunset clause arrangements; or other ring-fencing measures. All these are important issues that are currently under in-depth examination. If it is decided that changes on this front need to be pursued, there will be public consultation to ensure proper safeguards to protect the balance of rights among the stakeholders.

Now, let me turn to my second topic. There is an encouraging trend for more corporates to follow the UN Principles for Responsible Investing, and commit to ESG reporting and ESG investing. ESG encompasses a wide range of important issues, including carbon footprint reduction, tackling climate change, sustainable investing, impact investing and so forth.

Talking about climate change and given this fair weather, I like to digress a bit and point out that, just this week, Hong Kong sees two typhoons in our city – one just left Hong Kong yesterday which is good for this conference, but another super typhoon is expected to hit us squarely on Sunday. In fact, there are currently nine typhoons forming roughly a straight line in what-is-called the intertropical convergence zone over the Pacific and Atlantic. There are three typhoons in the West Pacific, two in the East Pacific and four in the North Atlantic. Several of these are major hurricanes, or typhoons as we call them in this part of the world. It is a very rare occurrence for so many typhoons to appear at the same time, usually they appear sequentially, and some experts believe that this is due to ocean warming and possibly climate change.

While there are some that tend to downplay the importance of combating global climate change, many scientists, government officials, civic groups and corporates think that it is important to do their part in protecting our environment. Corporates are becoming more and more conscious of their carbon footprint and impact on the environment. This is taking place alongside developments in the investment community, where ESG investing is gaining traction in mainstream financial markets.

Our government is committed to developing Hong Kong into a sustainable city and combating global climate change. Given my portfolio as Secretary for Financial Services and the Treasury, I like to focus now on green investing and how Hong Kong's capital markets can be a fundraising platform for green projects. We are committed to developing Hong Kong into a regional hub for green finance.

To facilitate green debt issuance in Hong Kong and elsewhere, our Hong Kong Quality Assurance Agency (HKQAA) launched in January this year its Green Finance Certification Scheme, which provides third-party conformity assessments for green debt instruments. The HKQAA developed the Scheme with reference to a number of international and national standards on green finance. Two types of certification are available – Pre-issuance and Post-issuance Certification. From a broader perspective, the enhanced transparency and accreditation standard of green financial products would help to strengthen market confidence in green finance and avoid greenwashing.

According to reports issued by Climate Bonds Initiative and China Central Depository and Clearing Co Ltd, China's green bond issuance was US$36.2 billion in 2016, accounting for 39 per cent of the global total. This comprised US$23.6 billion aligned with international definitions and the rest aligned with China's green definitions. For 2017, China's total green bond issuance was US$37.1 billion, of which US$22.9 billion was aligned with international definitions. China was the largest global green bond issuer in 2016 and the second largest in 2017.

I am pleased to note that we are seeing good momentum for Hong Kong to develop as a green finance hub, notably with the Financial Secretary announcing in February this year the upcoming launch of a Government Green Bond Programme with a borrowing ceiling of HK$100 billion. In fact, in the first half of 2018, we already saw at least 15 green bond issuances in Hong Kong, with an aggregate size reaching US$8 billion. The issuers of these green bonds included the likes of the World Bank and the European Investment Bank, and also corporations from Hong Kong, the Mainland and beyond. This attests to the strengths of Hong Kong as a major green finance hub in the region.

In June this year, we also announced the launch of our Green Bond Grant Scheme which reimburses, up to HK$800,000 per eligible green bond issue, the issuance expenses incurred to obtain certification from the HKQAA's Green Finance Certification Scheme.

Ladies and gentlemen, we are currently seeing an unstoppable wave of innovation and technology as well as an increased recognition of the importance of environmental, social and governance standards. The new economy and the green economy raise fresh issues and challenges for corporate governance. I have shared with you some of our experience in Hong Kong and hope we can benefit from your insightful deliberation. And I wish you all a very successful conference today. Thank you.