

# HONG KONG SECURITIES AND FUTURES COMMISSION:

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## CONSULTATION PAPER ON THE PRINCIPLES OF RESPONSIBLE OWNERSHIP

### RECOMMENDATIONS

The PRI strongly supports the objectives of the Principles of Responsible Ownership, which we believe will promote active, engaged ownership of companies over the long-term. The Principles of Responsible Ownership will contribute to high standards of transparency and governance in Hong Kong's equity market, and ultimately, sustainable long-term growth.

The PRI reporting and assessment framework demonstrates that, globally, many investors already achieve the standards proposed by the Securities and Futures Commission. The guidelines will standardise ownership expectations for both domestic and foreign investors, and are consistent with international initiatives, including the UK and Japanese Stewardship Codes.

The PRI encourages the Securities and Futures Commission to require institutional investors to report annually on compliance with the Principles of Responsible Ownership. To minimise reporting time and costs for investors, the PRI would encourage the Securities and Futures Commission to reference the PRI reporting framework and clearinghouse, which supports collaborative shareholder engagement.

As achieved by Japan's Financial Services Agency, foreign investors should be encouraged to commit, and report, to the Principles of Responsible Ownership, as should voting services agencies. The Securities and Futures Commission should ensure that asset owners have the tools and resources necessary to hold asset managers to account on their stewardship obligations.

The Securities and Futures Commission is well-placed to learn from existing global comply-or-explain stewardship guidelines, and in particular must ensure lasting and meaningful implementation – including rewarding investors for full compliance. The PRI recommends that the Commission reviews effectiveness of the Principles of Responsible Ownership on an annual basis, starting with the number of investors that have subscribed to the Principles, as well as analysis of actions taken and outcomes achieved.

## ABOUT THE PRINCIPLES OF RESPONSIBLE OWNERSHIP

On 2 March 2015, the Hong Kong Securities and Futures Commission published a consultation paper on the Principles of Responsible Ownership. The Principles are as follows:

**Principle 1:** Investors should establish and report to their stakeholders their policies for discharging their ownership responsibilities.

**Principle 2:** Investors should monitor and engage with their investee companies.

**Principle 3:** Investors should consider and establish clear policies on when they will escalate their engagement activities.

**Principle 4:** Investors should have clear policies on voting guidance.

**Principle 5:** Investors should be willing to act collectively with other investors where appropriate.

**Principle 6:** Investors should report to their stakeholders on how they have discharged their ownership responsibilities.

**Principle 7:** When investing on behalf of clients, investors should have policies on managing conflicts of interest.

The full consultation document is available online<sup>1</sup>. PRI signatories may find the following statements of interest:

As a leading financial market, it is important that in Hong Kong we play our part as a world citizen and encourage proactive ownership engagement between investors and publicly listed companies (page 2).

Responsible shareholders carry out a function that is essential for effective capital allocation that contributes to economic growth of a society (page 2).

Active participation by shareholders will improve the governance and performance of investee companies that will, in the long-term, enhance operation of our capital markets (page 4).

The Principles are non-binding, and operate on a “comply-or-explain” basis (page 4).

Clients should hold asset managers accountable for how they fulfil ownership responsibilities (page 5).

There may be certain categories of investors ... where there should be a requirement for ... a comply-or-explain obligation (page 5).

Companies listed in Hong Kong are disproportionately dominated by family and state-controlled ownership ... there is evidence to support the view that investors will often find it more productive to engage the controlling shareholder rather than the board (page 6).

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<sup>1</sup> <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/openFile?refNo=15CP2>

Institutional investors may decide to outsource voting decision to a proxy advisor. As there are two proxy advisors that dominate the market, issues put to votes are dominated by just two views instead of attracting the views of a wide spread of investors (page 13).

We recommend that foreign investors should be encouraged to commit to the Principles (page 14).

## ABOUT THE PRI

The United Nations-supported Principles for Responsible Investment (PRI) is a global network of over 1360<sup>2</sup> asset owners, investment managers and financial service providers from 54 countries, with total assets under management of \$45 trillion.

PRI signatories commit to the following Six Principles<sup>3</sup>:

**Principle 1:** We will incorporate ESG issues into investment analysis and decision-making processes.

**Principle 2:** We will be active owners and incorporate ESG issues into our ownership policies and practices.

**Principle 3:** We will seek appropriate disclosure on ESG issues by the entities in which we invest.

**Principle 4:** We will promote acceptance and implementation of the Principles within the investment industry.

**Principle 5:** We will work together to enhance our effectiveness in implementing the Principles.

**Principle 6:** We will each report on our activities and progress towards implementing the Principles.

## REPORTING AND ASSESSMENT FRAMEWORK

PRI signatories that manage assets are required to report publicly and annually on their responsible investment activities. In 2014, 830 signatories responded. In 2015, 936 signatories responded. A transparency report is published for each signatory<sup>4</sup>, which anyone – including non-signatories and policy-makers – can access.

The PRI has analysed data to demonstrate reported investor practice that is relevant to the Principles of Responsible Ownership. Further details of the PRI reporting framework can be found here: <http://www.unpri.org/areas-of-work/reporting-andassessment/reporting-framework/>.

Signatory, by region:

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<sup>2</sup> As of May 2015

<sup>3</sup> <http://www.unpri.org/about-pri/the-six-principles/>

<sup>4</sup> <http://www.unpri.org/areas-of-work/reporting-and-assessment/reporting-outputs/>

<i>Region</i>	<i>AO</i>	<i>IM</i>	<i>Total</i>
Asia, Hong Kong		6	6
Asia, Other	6	27	33
Oceania	39	70	109
<b>Asia + Oceania Total</b>	<b>45</b>	<b>103</b>	<b>148</b>
Rest of World	200	588	788
<b>Grand Total</b>	<b>245</b>	<b>691</b>	<b>936</b>

The PRI's module "Selection, Appointment and Monitoring" (SAM) is voluntary for PRI asset owner signatories that use third party investment managers, and hence there is a smaller data pool. The module SAM 7 asks: "When appointing managers, indicate which of the following responsible investment considerations your organisation typically includes in investment management agreements / contracts for your listed assets":

	<i>Asia + Oceania</i>	<i>Europe</i>	<i>North America</i>
Engagement - Specific requirements relating to engagement	7	19	
Specific requirements relating to (proxy) voting	17	28	5
Acting in accordance with your organisation's overall investment beliefs or policy on responsible investment and ESG issues	25	69	16
Specific requirements relating to the incorporation of ESG issues into investment decision-making	12	36	9
Reporting on the ESG characteristics of the portfolio	9	30	3
Reporting on the impact of ESG issues on financial performance	7	19	4

The PRI's module "Overarching Approach", OA 2.1, asks: "Indicate if your responsible investment policy is publicly available". An overwhelming majority of PRI signatories make their responsible investment policy publicly available.

	<i>(Proxy) voting policy</i>	<i>Engagement/active ownership policy</i>	<i>Specific guidelines on corporate governance</i>
<b>Asia</b>	21	19	22
<b>Oceania</b>	73	74	69
<b>Africa</b>	30	28	30
<b>Europe</b>	237	345	301
<b>North America</b>	111	88	96
<b>South America</b>	12	21	33

The PRI's module "Listed Equity Active Ownership", LEA 15.3, asks: "Indicate what engagement information your organisation proactively discloses to clients, beneficiaries and the public."

	<i>Number of engagements</i>	<i>Breakdown of engagements by type/topic</i>	<i>Breakdown of engagements by region</i>
<i>Asia</i>	12	9	0
<i>Oceania</i>	26	21	6
<i>Africa</i>	16	14	2
<i>Europe</i>	126	105	69
<i>Latin America</i>	3	2	0
<i>Middle East</i>	0	0	0
<i>North America</i>	35	35	11
<b><i>Grand Total</i></b>	<b>218</b>	<b>186</b>	<b>88</b>

	<i>Details of the selections, priorities and specific goals of engagement</i>	<i>An assessment of the current status of the engagement</i>	<i>Outcomes that have been achieved from the engagement</i>
<i>Asia</i>	13	4	10
<i>Oceania</i>	19	17	23
<i>Africa</i>	10	8	13
<i>Europe</i>	84	73	103
<i>Latin America</i>	4	0	4
<i>Middle East</i>	0	0	0
<i>North America</i>	39	31	40
<b><i>Grand Total</i></b>	<b>169</b>	<b>133</b>	<b>193</b>

	<i>Disclosed quarterly</i>	<i>Disclosed annually</i>
<i>Asia</i>	4	11
<i>Oceania</i>	14	18
<i>Africa</i>	10	4
<i>Europe</i>	58	71
<i>Latin America</i>	2	4
<i>Middle East</i>	0	0
<i>North America</i>	23	23
<b><i>Grand Total</i></b>	<b>111</b>	<b>131</b>

## FOR FURTHER INFORMATION ON THE PRI, REPORTING AND ASSESSMENT, AND PUBLIC POLICY, PLEASE CONTACT:

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