

Part 1

The Board:

Role, what it did during the year and how



Summary of relevant sections of the Corporate Governance Code (“Code”) (Appendix 14 Main Board and Appendix 15 Growth Enterprise Market Listing Rules)

Code Section A.1 – The Board: Principle

An issuer should be headed by an **effective board** which should assume responsibility for its **leadership** and **control** and be collectively responsible for promoting its success by **directing** and **supervising** its affairs. Directors should take decisions objectively in the best interests of the issuer.

- **Code Provisions:**

There are detailed **Code Provisions under the above Principle**, prescribing (i) elements of the board process, including frequency of board meetings, the setting of the agenda, preparation of minutes, and the need for physical meetings (rather than written resolutions) in conflict of interest situations; (ii) procedure enabling board members to seek independent professional advice; (iii) appropriate insurance arrangements for directors (A.1.1 - A.1.8).

- **Corporate Governance Report (“CG Report”):**

An issuer’s CG Report must include a narrative statement explaining **how** the issuer has **applied** the **Principles** in the Code, enabling its shareholders to evaluate how the principles have been applied (G.(a)). In addition, various, more specific, disclosures are required, e.g., number of board meetings held during the year (I.(b)), attendance by directors at board and general meetings (I.(c)) and a statement of the board’s and management’s respective responsibilities and accountabilities (I.(e)).

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1. Analysis: Key themes underlying the Code requirements

1.1 Under the **Code Principle in section A.1**, two aspects of the board's leadership role are stressed.

Firstly, “**directing**” the affairs of the company; secondly, “**supervising**” the same. The “**directing**” role is a broad concept, which is interpreted to encompass, among other things, **setting the issuer's strategic aims**, and ensuring (including by way of establishing appropriate policies) that the necessary financial and human resources are in place for the issuer to meet its objectives and implement the agreed strategies. Meanwhile, the “**supervisory**” aspect seems to refer to the board's role in **monitoring the performance of management**.

1.2 In addition, some specific responsibilities of the board are elaborated **elsewhere in the Code** – including, determination of remuneration, financial reporting, internal controls and risk management, corporate governance, and communications with shareholders. (The Appendix sets out, in the form of a chart, various aspects of the board and its work, as addressed in other Code Principles.)

1.3 Under the above Code Principle, there are detailed **Code Provisions** setting out aspects of the **board process**. Underlying these is the **effective and active participation by board members together**. They must also **work together collectively**. How does the board process facilitate their working together?

1.4 It is important to note that the concept of **directors' collective responsibility** for the company and their duties as directors are addressed under other Listing Rules:

For example: Rule 3.08: “The **board** of directors of an issuer is **collectively responsible** for its management and operations. The Exchange expects the directors, both collectively and individually, to fulfil **fiduciary duties** and **duties of skills, care and diligence** to a standard at least commensurate with the standard established by Hong Kong law...” [emphasis added]



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1.5 To sum up, our interpretation of the key themes underlying the Code Principle in section A.1 are:

A. The board’s key roles are setting the issuer’s strategy and monitoring the management’s performance.

B. A good board process facilitates the operation of the board.

1.6 In addition, report users, including investors, would be interested in understanding, in broad but clear terms:

C. The board’s work during the year and how it is linked to the issuer’s strategy and focus.

2. A closely-related topic is board effectiveness (addressed under other Code Principles)

2.1 A discussion on the board’s roles is inevitably linked to other aspects of the board. (The Appendix gives an overview of the various topics.) The board’s **effectiveness**, in particular, is relevant. Report users would want to see that the board has the appropriate skills and balance to discharge its duties:

- The board should have the appropriate **balance of skills, experience and diversity** of perspectives to enable it to discharge its duties and responsibilities effectively. (See the Code Principle under section A.3 of the Code – Board composition.)
- **Board independence** (Code Principle, section A.3) generally, is an area of investor focus, particularly in the context of family-controlled companies in Hong Kong. What steps have been taken to ensure board independence? Issuers may have taken different paths, in light of their own circumstances; for example, voluntarily adopting a schedule of significant matters that require independent director approval.



- There should be a formal, considered and transparent procedure for the **appointment of new directors** (and re-appointment of existing directors) to the board. (See the Code Principle under section A.4 – Appointments, re-election and removal.)
- **Board succession** is also an area of investor focus in Hong Kong, in the context of family-controlled companies. (See the Code Principle under section A.4.)

2.2 Board evaluation

- Board evaluation should also help to ensure the effectiveness of a board. Currently, it is a **Recommended Best Practice** (“RBP”) under the Code (B.1.9) that the board should conduct a regular evaluation of its performance. It is, however, a widely accepted international best practice.
- For example, under the Corporate Governance Code in the United Kingdom (“UK”), board evaluations should consider the balance of skills, experience, independence and knowledge of the company reflected on the board, its diversity, and how the board works together. Individual director performance, in terms of contribution and commitment, should also be covered. The issuer should then act on the results of the evaluation by recognising the strengths and weaknesses of the board. The relevant part of the annual report should explain how the performance evaluation has been conducted. (See UK Corporate Governance Code - Main Principle B.6.)



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3. How to provide meaningful disclosure in relation to the key themes

This section considers what disclosure in an issuer’s report, users, including investors, would consider “meaningful”. **It is possible to disclose useful information while providing reasonably high-level statements**, without having to divulge commercially-sensitive information.

Under each theme, we have included **brief commentary** and also **examples** to illustrate and highlight the relevant issues, where appropriate.

Theme A: The board’s key roles are setting the issuer’s strategy and monitoring the management’s performance.

The board has **two key roles**: that of setting strategy and monitoring management performance. How does the board **work with management** in performing these two roles, particularly in setting strategy?

Pursuant to these two broad roles, what are **the board’s specific responsibilities**? How did the board reach an understanding on this? Some boards may set out a **formal board mandate**. As we have seen in the earlier section, some specific responsibilities of the board are expressly stipulated elsewhere in the Code (e.g., internal controls and risk management (see Code Principle and Provisions, section C.2)). In addition to these, are there any other specific responsibilities of the board? For instance, corporate values and ethics are also crucial in building success and avoiding failure. Does the board set the right tone at the top?

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Theme A: Example

The following company clearly sets out the board's roles and responsibilities:

The Board's role is to provide leadership of the Company and direction for management. It is collectively responsible and accountable to the Company's shareholders and stakeholders for the long term success of the Group. While the management is delegated to run the Group's day-to-day business (as more specifically described on page ●), the Board focuses on and reserves powers in the most significant matters of the Group, including:

- formulating long and short term strategic directions of the Group, including development strategy, major investments, acquisitions and disposal of major assets;
- preparing and approving financial statements, annual and interim reports, and making judgements that are fair and reasonable in the preparation of the Company's disclosure statements;
- approving the Group's annual budgets and forecasts;
- approving changes in accounting policies;
- approving changes to the Company's capital structure;
- setting dividend policy;
- authorising material borrowings and expenditures;
- approving the appointment of Directors for election and/or re-election in general meetings;
- performing corporate governance functions in accordance with the CG Code, including determining the Group's corporate governance policies, and reviewing and monitoring the corporate governance practices of the Group; and
- overseeing and reviewing the effectiveness of the risk management and internal control systems of the Group through review of reports from Audit Committee and the Group Management Committee

(The Hongkong and Shanghai Hotels, Limited, Annual Report 2012)



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Theme B: A good board process facilitates the operation of the board.

Apart from understanding the board's roles and responsibilities, report users would like to understand how the board is working together to achieve these. Is the board working together effectively? A good board process will greatly facilitate the board's working. What steps have been taken, for instance, to facilitate constructive discussions?

Theme B: Example

The following international example addresses how various aspects of the board process help to facilitate board functioning – ranging from setting of agenda, provision of information, and a general focus on constructive debates and discussions. Feedback from board evaluation also helped in further enhancing the board process:

The Board agenda focuses on our themes of driving our strategy, developing strong leadership and succession, monitoring execution, protecting our trusted brand and our strong relationships with customers, employees and other stakeholders.

While we recognise the importance of compliance, we try to avoid spending time on box-ticking and gold-plating legislation, choosing instead to focus on the long-term plans for our business and its execution.

Following our external Board evaluation last year, we further reviewed all information sent to Board members. We also moved to electronic distribution of our Board papers by iPad – a contribution, albeit small, towards supporting our Plan A objective to reduce the use of printed paper across our business, but one which clearly demonstrates the Board's willingness to embrace new technology and more efficient methods of communication.

Our Board agendas today allow more time for debate and long-term strategic discussion, with two Board away-days held during the year. Our forward planner gives Board members visibility of what is on future agendas for their consideration. We also schedule time during every meeting for ad hoc feedback as well as giving the non-executive directors an opportunity for private discussion.

(Marks and Spencer Group plc, Annual Report 2012)

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Theme C: The board's work during the year and how it is linked to the issuer's strategy and focus.

Apart from understanding the roles and responsibilities of the issuer's board in general terms, report users would be interested in knowing about the linkages to the issuer's strategy and objectives during the year. **What were the board's objectives during the year? Have these changed from previous years?**

Issuers need to find a **balance** between making **meaningful disclosures and safeguarding commercial sensitivity**. The example below shows how **fairly high-level statements** can be used to bring out meaningful information, without divulging commercially-sensitive information.

The description of the board's work in the annual report is an important section and should be reviewed by the board thoroughly before publication.



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Theme C: Example – Roles of the board and focus during the year

In this example, the roles of the board are set out – being strategic planning, internal controls and risk management, culture and values, capital management, corporate governance, and board succession. The specific actions taken by the board during the year under various key headings are then specifically listed.

What the Board has done during 2011

During the year, 4 Board meetings were held. The focus of these meetings included the following topics of discussion and yielded the following results:

1. Leadership

- appointment of Non-executive Chairman
- appointments of new Board members who bring new insights to the Board
- reviewed composition of Board Committees

2. Strategy

- reviewed strategic plans for the Group's core leasing (Office, Retail, and Residential segments) to meet short-term objectives and to strengthen medium-term competitiveness
- ongoing assessment of Hysan Place project, with a view to enabling it to take the Group to another level of commercial success and sustainability
- reviewed the positioning of our core property portfolio in Causeway Bay as a choice location for work and play; and management's plan to further strengthen its branding and marketing
- reviewed further opportunities in our core property portfolio with management

Roles of Board

- Strategic Planning
- Internal Controls and Risk Management
- Culture and Values
- Capital Management
- Corporate Governance
- Board Succession

3. Risk Management

- Audit Committee received presentation on best practices in risk management and endorsed management's plans to further strengthen the risk identification and assessment process, and to adopt more frequent and structured reporting to the Audit Committee and the Board
- assessed effectiveness of financial controls, and other internal controls (Please refer to separate "Internal Controls and Risk Management Report")
- legal and regulatory compliance added as standing item for each Board meeting

4. Relations with Shareholders

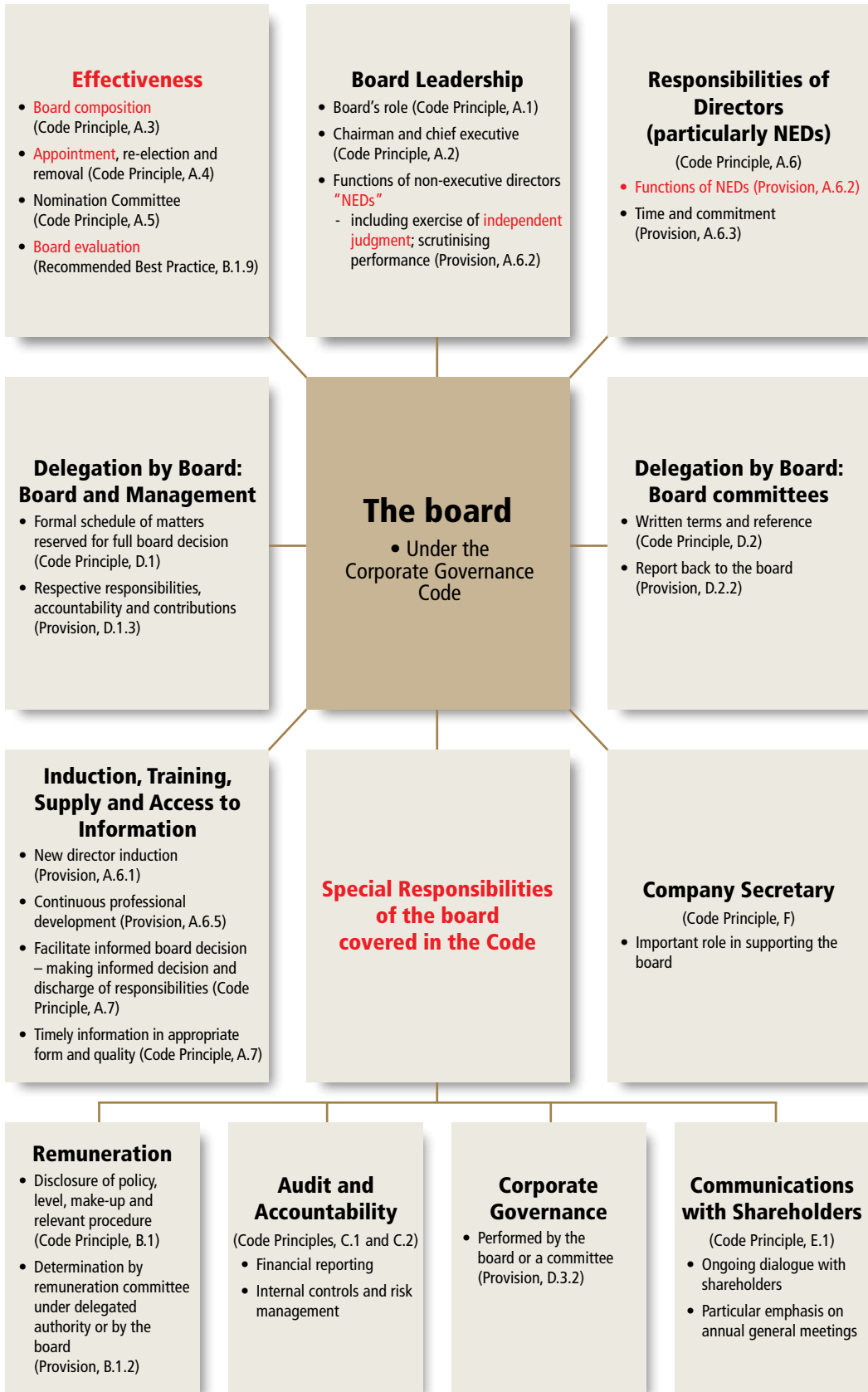
- investor relations added as standing item for each Board meeting
- investor relations reports describing investor and analyst opinions are provided regularly to the Board
- enhanced investor relations programme to expand coverage by analysts

(Hysan Development Company Limited, Annual Report 2011)



Appendix

Overview of CG Principles applicable to the board



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This chart gives an overview of various areas of the Code applicable to the board, setting the context for discussion of board roles. (N.B. Areas seen as particularly relevant to board roles are highlighted in red)