New Risk Management Requirements in Hong Kong’s Corporate Governance Code

“More than Just a Box to Tick”

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Abstract

On 1 January 2016, Hong Kong’s listed entities will be regulated by an amended Corporate Governance Code and Corporate Governance Report. The core changes contain the re-situating and revamping of risk management requirements along slide internal control systems from the recommended best practices to code provisions. Whilst the proposed changes seem to be in line with international trends, new risk management obligations should not be treated as another set of procedures and processes for the board. The code provisions oblige the board to manage and monitor the company’s risks. This code also expects risk management to be embedded in the issuer’s organization. Failure to comply not only attracts sanctions from the exchange, but has legal implications for directors under statutory duty of care. Therefore, any omissions by directors in the managing and monitoring of the company’s risk will find themselves exposed to legal risks.

Keywords

corporate governance code – risk management – internal control systems – directors’ duty of care

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Introduction

The recent Global Financial Crisis (GFC) has left a clear mark in people's minds about the vulnerability of international financial markets and the interconnectedness as well as interdependency of markets around the world. More importantly, the bad governance of a few companies in one corner of the world could have a tsunami effect on economies around the globe. Furthermore, financial crisis has long lasting effects on the international community as a whole. In particular, it unsettled investors' confidence in international equity markets, which would have wider socio-economic implications. Whilst there are many causes leading to the GFC, one of the symptoms was that company boards had been complacent in managing corporate and related risks.

Following a review of the Code on Corporate Governance Practices and Associated Listing Rules in 2010 and 2011, in June 2014 HKEx published a consultation paper to sought comments on proposed amendments to the Hong Kong corporate governance code (Code) relating to risk management and internal controls. The conclusions to the consultation on the review of the Code were published in December 2014. According to for the proposed amendments the current Code seems to lag behind international developments in the area of corporate risk management. The HKEx will amend the Code to be in line with international best practices so as to secure its position as an international financial centre.

Yet, risk management is not as simple and straightforward as a matter of putting in place procedures and processes. Corporate risks in the 21st century can be a challenge given that risk, uncertainty, and threats are not always predictable. It can be said that risk management is like trying to foresee and manage the unforeseen and capricious. The report, *Global Risks 2015* published by the World Economic Forum, now in its tenth edition examines economic, societal, geopolitical, technological, and environmental risks. It notes that risk identification alone might not reveal the interconnection and the potentially cascading effects of global risk. The 2015 Global Audit Committee Survey drew its conclusions from 1,500 audit committee members. The survey finds that the top five risks pose the greatest challenges for companies are: 1. uncertainty and volatility (economic, regulatory, political); 2. government regulation/impact of public policy initiatives; 3. legal/regulatory compliance; 4. operational risk/control environment; and 5. talent management and development. A year earlier the 2014 Global Audit Committee Survey finds that the top five risks

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