10 POINTS ON CLIMATE-RELATED COMPLIANCE AND DISCLOSURE FOR FUND MANAGERS IN HONG KONG

30 Days Series 21 by Zhang Kaihui

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1. It starts with understanding the applicability of the current climate-related regulatory regime for fund managers …

The current SFC regulatory focus is on the environmental aspect (ie the "E" in the ESG framework), particularly on climate-related issues. The requirements apply to fund managers which manage collective investment schemes with investment discretion ("In-scope Fund Managers"), but are not mandatory for fund managers managing discretionary accounts.

2. …on governance, investment and risk management, and disclosure…

One of the two core requirements is that In-scope Fund Managers are required to identify and assess the relevance and materiality of climate-related risks to their managed funds, and incorporate such risks into their investment and risk management frameworks with continuous monitoring.

The other core requirement is for In-scope Fund Managers which are responsible for the overall operation of funds (eg having day-to-day management of the funds) to make adequate disclosures of their governance frameworks and investment and risk management processes, focussing on how they assess and monitor climate-related risks. The purpose is to enhance transparency and accountability to investors. Where climate-related risks have been assessed to be irrelevant to an In-scope Fund Manager's investment strategies, such exceptional circumstances should also be disclosed.

There is flexibility as to how the disclosure is made and it is **not** mandatory to make the disclosure in a private placement memorandum. We have seen disclosure made on an In-scope Fund Manager's website or in a notice directly emailed to investors. The key is to draw fund investors' attention to the information.

3. …with the principles-based and proportionality approaches.

While the climate-related governance/management and disclosure requirements are principles-based (to address the constantly evolving global climate situation), In-scope Fund Managers are expected to adopt a proportionate approach – in terms of their risk management governance structures and procedures, as well as the extent and frequency of climate-related risk disclosures - so that the level of disclosure is commensurate with the relevant In-Scope Fund Managers' nature, size, complexity and risk profiles.

The Fund Manager Code of Conduct sets out the high-level principles, with the details set out in the Circular and FAQs.

4. It is important to engage experts on climate-related issues.

To fulfil the abovementioned governance/management and disclosure requirements, In-scope Fund Managers are expected to conduct due diligence to assess how climate risks are relevant to their investment strategies and managed funds. Whether you engage internal or external experts, the key is to ensure the experts have the technical capability to analyse and assess climate-related data, risks and impacts.

5. If you operate in multiple jurisdictions, check your group wide policy…

The focus points of regulators around the world on climate-related issues are quite similar. In-scope Fund Managers with global operations may adopt their group policy locally, but should be mindful that group-level standards must meet or exceed applicable local regulatory requirements.

*Any reference to "Hong Kong" shall be construed as a reference to the "Hong Kong Special Administrative Region of the People's Republic of China".

6. …while making reference to international standards.

When formulating the management and disclosure requirements, the SFC made reference to the Task Force on Climate-Related Financial Disclosures' (TFCD) Recommendations. These are widely-endorsed international standards which provide a framework for the types of data that must be analysed and disclosed regarding the impact of climate-related risks and opportunities.

7. Allocating sufficient resources to address climate-related issues, from the board and senior management …

The board should have overall oversight of climate-related issues, setting the tone from the top, and deciding on an appropriate governance structure suitable to the In-scope Fund Manager's activities and operations.

8. …down to the operational level.

In-scope Fund Managers are also required to devote sufficient human, budget and technical resources as part of its climate-related risk management efforts, and to provide training to staff members on the applicable regulatory requirements and internal policies relating to climate-related issues.

9. Review regularly…

In-scope Fund Managers are expected to conduct evaluations of the relevance of climate-related risks and review disclosures at least annually and to update their disclosures as soon as practicable when there is any material change.

10. …and keep an eye out for the way forward.

Beyond the current SFC regulatory focus on the environmental aspect of climate-related issues, generally SFC also encourages fund managers to consider the broader spectrum of sustainability risks in their investment and risk management processes. Fund managers should also continue to monitor international and local trends in social and corporate governance matters (eg personal information protection, the growing demand for a common standard about business and human rights, etc), and consider how their operations in other jurisdictions may impact their governance and disclosure obligations locally.

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