



Hong Kong

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HONG KONG SFC REQUIRES ENHANCED DISCLOSURE FOR GREEN OR ESG RETAIL FUNDS

Hong Kong's Securities and Futures Commission (the **SFC**) published a Circular to management companies of SFC-authorized unit trusts and mutual funds¹ on 11 April, 2019, setting out enhanced disclosure requirements for SFC-authorized green or environmental, social and governance (**ESG**) funds.

1. Background

Green or ESG-related investment products are regarded as sustainable investments and asset managers are increasingly taking climate change, green, ESG or sustainability factors into consideration when making investment decisions and offering products that fit green or ESG-related investment mandates. They are gaining ground in foreign markets and various overseas jurisdictions are imposing disclosure requirements and regulatory frameworks to assist investors' understanding and assessment of whether particular investment products meet their investment expectations and needs.

There are currently a number of SFC-authorized funds focused on investing in climate, green, environmental or sustainable development. Having evaluated the disclosures made by these funds, the SFC notes that while a majority of the funds disclosed the green or ESG factors in their investment objective or strategy, most fail to stipulate how their managers incorporate and screen these factors in the investment selection process. Given the wide variation in the quality of disclosure, the SFC has set out in the Circular how the current Code on Unit Trusts and Mutual Funds (**UT Code**) and disclosure guidelines on

SFC-authorized funds apply to green and ESG funds. The aim is to enable investors to more easily compare similar types of SFC-authorized green or ESG funds to facilitate informed investment decisions.

2. Application of the Circular

The Circular applies to SFC-authorized unit trusts and mutual funds which incorporate one or more of the internationally recognised green or ESG criteria or principles (set out in Annex 1² to the Circular) as their key investment focus, and reflect this in their name and investment objective or strategy.

3. Scheme Name

A green or ESG fund should invest primarily in investments reflecting the fund's particular green or ESG investment focus. In particular:

- a) funds adopting screening or thematic investment strategies should demonstrate that they have invested at least 70% of their total net asset value in securities or other investments reflecting the stated green or ESG-related investment focus; or
- b) funds adopting other investment strategies, such as ESG integration or impact investing, will need to be able to demonstrate to the SFC, on a case-by-case basis, how they comply with this requirement.

¹ <https://www.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=19EC18>

² <https://www.sfc.hk/edistributionWeb/gateway/EN/circular/openAppendix?refNo=19EC18&appendix=0>

4. Disclosure requirements

Offering documents for SFC-authorized funds are required to contain the information necessary to enable investors to make informed decisions. The SFC expects the offering documents, including the product key fact statements, of green and ESG funds to disclose at least the following:

- a) a description of the key investment focus (e.g. climate change, green, sustainability, etc.) and targeted objective (e.g. financial return, mitigating climate change or environmental damage, etc.) of the green or ESG fund, and where applicable, how the key investment focus is considered as green or ESG-related;
- b) a description of the investment strategies adopted by the green or ESG fund, including but not limited to:
 - i) the relevant green or ESG criteria or principles considered;
 - ii) the anticipated exposure to the securities or other investments that reflect the stipulated green or ESG investment focus;
 - iii) the investment selection process and criteria adopted by the green or ESG fund, such as:
 - A assessment criteria of the underlying investments;
 - B ESG analysis and evaluation methodology; and
 - C reference ESG benchmark being tracked and the characteristics and general composition of the benchmark;
- c) a description of whether an exclusion policy is adopted by the green or ESG fund and types of exclusion (e.g. sectors, countries or activities);
- d) a description of risks associated with the green or ESG fund's investment theme; and
- e) other information considered necessary by the manager.

5. Ongoing monitoring

Managers of green or ESG funds are required to regularly monitor and evaluate the funds' underlying investments to ensure they continue to meet the investment objective and requirements set out in the SFC Circular.

6. Dedicated Green or ESG funds webpage

A central database of green or ESG funds will be launched before the end of 2019. The new database will be accessible through the SFC's website and is aimed at enhancing the visibility of these funds.

7. Implementation

7.1. Initial confirmation of compliance

Managers of existing SFC-authorized funds or of new funds that are seeking SFC authorisation which fall within the scope of the Circular must provide to the SFC one of the confirmations stipulated in Annex 2,³ being either a self-confirmation of compliance or a confirmation demonstrating compliance supported by an independent third party certification or fund label.

7.2. Existing SFC-authorized funds

For an existing SFC-authorized fund to be classified as a green or ESG fund pursuant to the Circular, its manager should review the fund's offering documents against the disclosure requirements set out in paragraph 9 of the Circular (as summarised under paragraph 4 above), and make any necessary updates and revisions as soon as practicable, and no later than 31 December 2019.

Where the fund's offering documents require updates or revisions, managers should assess whether the SFC's prior approval is required under 11.1 of the UT Code and the applicable post-authorisation application requirements. The green or ESG fund will be posted on the dedicated webpage once the SFC is satisfied that it complies with the Circular's requirements.

³ <https://www.sfc.hk/edistributionWeb/gateway/EN/circular/openAppendix?refNo=19EC18&appendix=1>

7.3. New funds seeking SFC authorisation

In order to obtain classification as a green or ESG fund under the Circular, managers should ensure that the requirements of the Circular and applicable provisions of the SFC Handbook for Unit Trusts and Mutual Funds Investment-Linked Assurance Schemes and Unlisted Structured Investment Products (including the UT Code) and other relevant SFC circulars and guidelines are met. The new green or ESG fund will be posted on the dedicated webpage once its authorisation takes effect.

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