

Comments on SFC consultation paper on Management and Disclosure of Climate-related Risks by Fund Managers

Submitted by Carbon Care Asia Ltd.

Date 15 January 2021

Table of Contents

0. General observations.....	1
1. SFC Question 1	2
2. SFC Question 2	3
3. SFC Question 3	4
4. SFC Question 4	5
5. SFC Question 5	5
6. SFC Question 6	6
7. SFC Question 7	6
8. SFC Question 8	7
9. SFC Question 9	8

0. General observations

The development of green finance, the management of climate risk in the finance sector, alignment with targets to achieve global carbon emissions reductions and ESG reporting are all mentioned at the start of the report. While these are connected activities, they are not the same things.

The first is an attempt to contribute positively to the environment. The second is a defensive action to protect financial institutions against risks resulting from climate change. The third represents a commitment to contribute to national and international efforts to reduce global heating. ESG reporting represents an attempt to recognise risks and opportunities in a range of social and environmental area that extend beyond just climate change.

The majority of the report and the recommendations go on to discuss risk reduction rather than development of green finance or contribution to action on climate change. The SFC paper could more clearly demarcate these different activities and objectives.

It is true that ultimately, failure to set a climate target that matches or exceeds local, national or international targets does represent a business risk because governments cannot achieve their emissions reduction commitments without compelling the private sector to align with the same goals and may be forced to mandate these at some point in the future.

If definitions of materiality, proportionality and risk are too narrow, they may fail to take into account the evidence about the overall impact of global heating on the economy, human wellbeing and social stability and the consequent impact on finance sector institutions.

1. SFC Question 1

Do you have any comments on the SFC's proposal to focus on climate change or should a broader spectrum of sustainable finance should be considered in developing the requirements? Please explain your view.

We agree climate change is the most important single issue in terms of economic and social impact. However:

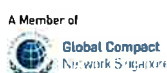
- Related environmental issues can compound economic and social impact of climate change and must be incorporated into reporting requirements: water stress, ocean pollution by phosphorous and nitrogen, land use change, biodiversity loss, plastic pollution in the food chain etc. should also be taken into account. The entire list of environmental constraints, known as 'planetary boundaries' should be accepted as relevant to any risk assessment related to the environment.
- Social issues, broadly set out in a number of the Sustainable Development Goals, are not only relevant elements of sustainability in their own right, but if not addressed could run counter to effective action on climate change or the environment. Therefore it is important to take account of social issues as part of a holistic sustainability strategy. Concurrent environmental and social improvement can be seen in terms of co-benefits rather than trade-offs. The principles of common but differentiated responsibilities (between nations) and just transition (within a nation) are both relevant considerations for financial institutions to understand and take into account when reporting risk.

Carbon Care Asia Limited

🏠 Suite 1908, CC Wu Building, 308 Hennessy Road, Wanchai, Hong Kong
 ☎ (852) 2541 5020 ✉ info@carboncareasia.com 🌐 www.carboncareasia.com

Carbon Care Asia Pte Ltd

🏠 133 New Bridge Road Chinatown Point #10-03 Singapore 059413
 ☎ (65) 6336 8558 ✉ infoSG@carboncareasia.com



- Specifically, we recommend that considerations of the 17 UNSDGs be incorporated in the framework of sustainable finance. At the very least, there should be requirements for any sustainable finance initiative to demonstrate i) the ‘Do No Significant Harm’ principle has been adhered to in regard to SDGs and, ii) quantifiable indicators of positive contributions to SDGs be measured, verified and disclosed wherever appropriate.

2. SFC Question 2

Do you agree that at the initial stage, the SFC’s proposed requirements should apply to the management of CISs but not discretionary accounts?

While it may be realistic to take a phased approach to comprehensive climate risk reporting, the SFC report notes that further warming of the planet “could have disastrous economic and social consequences.” This makes clear that the more thoroughgoing and timely a contribution the finance sector makes to addressing the climate crisis the lower the risk of disaster. We therefore recommend that coverage of climate risk reporting as well as the promotion of green finance be made more comprehensive in breadth and depth as swiftly as possible – before we are overtaken by the tragedy of the horizon.

By the same token, to suggest ESG factors are not integrated into quantitative driven products, other high-turnover parts of portfolios, or passively-managed accounts or strategies (Practice 13) can only be a transitional recommendation to a more holistic approach if banks are seeking methodologies to comprehensively account of the financed emissions and climate impact of their full portfolio and scope three emissions. The average time shares are now held has sharply declined in recent decades, but this reduced concern for the ‘real economy’ that underlies these

investments does not excuse the responsibility of those managing or owning these assets in either ethical or legal terms.

Specifically, we recommend that SFC should announce a clear timetable for its requirements be applied to CIS in the first phase, and discretionary accounts in the second phase.

3. SFC Question 3

Do you agree that the SFC should make reference to the TCFD Recommendations in developing the proposed requirements so as to minimise fund managers' compliance burden and foster the development of a more consistent disclosure framework? Other than the TCFD reporting framework, is there any other standard or framework which in your opinion would be appropriate for the SFC to refer to in developing the proposed requirements?

TCFD recommendations are a solid basis for climate risk reporting. They do not, however represent a standard, and efforts are being made around the world to turn TCFD recommendations into practical standards.

An important element of the TCFD recommendations concerns the forward-looking concept of scenario planning. It is important that SFC examine what this might look like in reporting requirements as this promotes the concept of both protecting against future risk as well as aligning with and contributing towards efforts to reduce damaging impacts of climate change.

Scenarios in this case cannot be limited simply to the impact of different rises in temperature. Scenarios should also explore the impact of transitional risks identified by TCFD such as regulatory change (carbon tax or emissions trading schemes), liability, technological and reputational changes that may occur as the climate crisis deepens. We recommend that SFC examine the PACTA scenario analysis tool.

Reporting standards do not represent targets or goals for climate change or environmental action. It is therefore important to consider how reporting requirements will represent indicators of sufficient contribution to sustainability

targets set locally, nationally or internationally. Failure to align with official climate targets represents a risk, as governments will necessarily require support from the private sector in achieving their target commitments.

Specifically, we recommend that SFC should announce a defined timeline to require the measurement and disclosure of financed emissions by 2022, with full TCFD reporting by 2025.

4. SFC Question 4

Do you have any comments on the proposed basis for determining the threshold for Large Fund Managers, ie, HK\$4 billion, and the basis for reporting? Please explain your view.

The lower threshold the better. There is no room for exceptionalism in preventing what SFC rightly calls ‘the disastrous economic and social consequences’ of further global warming. Smaller funds will not be immune to this disaster; many may actually be more vulnerable. Therefore, these funds should also play their part in a comprehensive effort to bring the entire finance sector into line with decarbonisation targets as soon as possible.

Instead of this proposed two-tiered system of requirements, i.e. “enhanced standards” for “large fund managers” and less stringent “baseline requirements” for all other fund managers, we suggest that SFC apply the same “enhanced standards” for both, but set different timelines. For instance, if large fund managers given 12 months for transition, SFC could give the others a 24-36 months’ transition. Enhanced standards include scenario assessment plans, fund-level scope 1+2 emission quantification and disclosures, which we think are basic requirements in terms of climate risk assessment and reporting for asset managers.

5. SFC Question 5

Do you have any comments on the proposed amendment to the FMCC requirements, baseline requirements and enhanced standards? Please explain your view.

We think the disclosure requirements on risk assessment results (material risks and their financial impacts) are missing here.

6. SFC Question 6

To provide a clear picture to investors on whether a fund manager has integrated climate-related considerations into its investment strategies or funds, do you agree that if the fund manager considers that climate-related risks are irrelevant to certain investment strategies or funds, it should make disclosures and maintain appropriate records to explain the rationale for its assessment?

We agree that it is necessary for the fund manager to justify the how climate-related risks are irrelevant or immaterial for the investment strategy and process. In essence, a “comply or explain” approach should be adopted at a minimum.

7. SFC Question 7

Do you agree that climate-related disclosures (except for the disclosure of WACI) to investors should be made at an entity level at a minimum and supplemented with disclosures at a strategy or fund level to reduce burden on fund managers?

We agree that governance, the process and approach used in investment process and risk management should be disclosed at entity level. But we think that not only the disclosure of WACI, but the risk assessment results should be disclosed as well at fund level, or at least for those funds with more exposure to assets at risk such as infrastructure or utility plants.

Carbon Care Asia Limited

🏠 Suite 1908, CC Wu Building, 308 Hennessy Road, Wanchai, Hong Kong
☎ (852) 2541 5020 ✉ info@carboncareasia.com 🌐 www.carboncareasia.com

Carbon Care Asia Pte Ltd

🏠 133 New Bridge Road Chinatown Point #10-03 Singapore 059413
☎ (65) 6336 8558 ✉ infoSG@carboncareasia.com



8. SFC Question 8

Do you agree that disclosures of quantitative climate-related data such as WACI should only be applicable to Large Fund Managers having regard to the resources required and the size of assets covered? Do you agree that at the initial stage the disclosure of the WACI should be made at the fund level instead of the entity level?

We think it should be applied to all, but different timelines may be considered for different sizes of operation. We agree that disclosure is targeted to its clients at the initial stage. Only if the asset manager is a public company, will shareholders be interested in entity-level reporting.

We restate our belief that the measurement and reporting of financed emissions under scope 3 of the Greenhouse Gas Protocol be as comprehensive as possible.

It is certainly important that the most impactful climate impacts of investments and loans (in terms of size and materiality) be accounted for as quickly as possible. But once the practices have been mainstreamed and the metrics more fully developed, the coverage of measuring and reporting financed emissions should be extended, leaving fewer gaps and exceptions in the reporting landscape.

New tools for the measurement of financed emissions (the how), and new science-based targets for the finance sector (the how much) are being introduced and further developed month by month. SFC should support the application of the best of these tools and standards in order that material and comparable measurements, benchmarks and targets are made across the investment sector within Hong Kong and between Hong Kong and other financial centres. Clear and comparable standards and principles on risks and sustainability will assist the investment community.

We recommend that SFC take account of recent work from PCAT regarding the more accurate measurement of financed emissions within loan and investment portfolios. PCAT work looks at a range of realistic approaches to measuring portfolio

Carbon Care Asia Limited

🏠 Suite 1908, CC Wu Building, 308 Hennessy Road, Wanchai, Hong Kong
 ☎ (852) 2541 5020 ✉ info@carboncareasia.com 🌐 www.carboncareasia.com

Carbon Care Asia Pte Ltd

🏠 133 New Bridge Road Chinatown Point #10-03 Singapore 059413
 ☎ (65) 6336 8558 ✉ infoSG@carboncareasia.com



emissions, and situates the WACI metric in a broader context of possible approaches.

We also recommend that SFC take account of the Science Based Targets Initiative standards for the finance sector announced in October 2020 regarding realistic targets which align financed emissions with the goals of the Paris Climate Agreement.

We are concerned that to exclude Scope 3 GHG emissions from baseline requirements for minimum fund level disclosures (p.39) would appear to cancel out 90% of the discussion in the rest of the document, and to exempt financial institutions from reporting on the activity that has the most material climate impact.

9. SFC Question 9

Do you think the following transition periods are appropriate?

§ a nine-month and a 12-month transition period for Large Fund Managers to comply with the baseline requirements and enhanced standards respectively; and

§ a 12-month transition period for other fund managers to comply with the baseline requirements. If not, what do you think would be an appropriate transition period? Please set out your reasons.

We are all aware of the clock ticking on climate change, the more slowly we act now, the later we peak emissions, the steeper the reduction curve has to become in the run up to 2050 if we are to avoid the fires, heatwaves, droughts, floods and biodiversity extinction brought on by climate change. We would therefore urge maximum realistic speed of introduction of climate risk reporting standards, however painful, to avoid much greater pain in the medium to long term.

-End of text-

Carbon Care Asia Limited

🏠 Suite 1908, CC Wu Building, 308 Hennessy Road, Wanchai, Hong Kong
 ☎ (852) 2541 5020 ✉ info@carboncareasia.com 🌐 www.carboncareasia.com

Carbon Care Asia Pte Ltd

🏠 133 New Bridge Road Chinatown Point #10-03 Singapore 059413
 ☎ (65) 6336 8558 ✉ infoSG@carboncareasia.com

