
ADM CAPITAL

The Securities and Futures Commission
54F One Island East
18 Westlands Road
Quarry Bay
Hong Kong

Attention: Consultation Paper on the Management and Disclosure of Climate-related Risks by Fund Managers

By email to: 2020_Climate_Consultation@sfc.hk

16 December, 2020

Dear Sir / Madam,

Re: SFC Consultation Paper on the Management and Disclosure of Climate-related Risks by Fund Managers

We are writing to express our support with regard to amending the Fund Manager Code of Conduct (FMCC) to require fund managers to take Climate-related risks into consideration in their investment and risk management processes as well as to make appropriate disclosures to meet investors' growing demand for Climate risk information and to combat greenwashing.

There are several recommendations, however, that we would contribute to this exercise. First, science shows that our fast-changing Climate is an existential threat to the global economy and that we should instead of "climate change," refer to "climate emergency" (IPCC). In order to keep global temperature rise to 1.5 degrees above pre-industrial levels, the science suggests we must embark on swift and transformative change to decarbonize our economies and appropriate labeling is an important first step.

With regard to Hong Kong, the HK 2050 is Now report released in June, "Pathways to Net Zero Emissions by 2050," showed that ambitious action on Climate is needed now, as current policies won't take us to deep decarbonisation by 2050. Achieving this goal requires an average annual decline in absolute emissions of 9 per cent between 2030 and 2050, against 6.6 percent if we are more ambitious now. In her recent policy address, our chief executive said the city would strive toward carbon neutrality by 2050 and promised a policy roadmap by next year.

This means that all sectors must do their part to support this transition to a decarbonized economy. What is needed is rapid and large-scale transformation in energy consumption, land use and urban infrastructure, including transportation, construction and industry, leading to a decline in global net anthropogenic carbon dioxide (CO₂) emissions of 45 per cent from 2010 levels by 2030 and net zero emissions around 2050.

The change will require careful planning, new technology and buy-in with respect to the costs and behavioural change that will need to be embraced. It will involve transforming our lifestyles to consume and waste less and make better use of resources we have. Addressing the climate emergency could also help us reverse the unsustainable depletion of our natural resources, our water, our marine life, our biodiversity and our forests.

And the related challenge, the social impact of inequality will also be exacerbated by the climate crisis consequences - drought, extreme weather events and rising seas, which typically flood lower lying,

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poorer areas and Hong Kong is no exception. This inequality has been laid even more bare through this recent period of pandemic and consequent economic upheaval.

Clearly, then, environmental and social sustainability as expressed in the Sustainable Development Goals (SDGs) is essential for a healthy, functioning society, and therefore also critical for the long-term success of any investor. Any fund management firm, considering portfolio risks, should take into account this critical moment that impacts economic resilience, factoring in Climate - and other environmental and social risks into investment decision-making. It is hard, then, to consider Climate alone as a factor.

We applaud the SFC for this consultation and would encourage more action from the SFC to promote the integration of other Environmental, Social and Governance (ESG) risks beyond climate risks into fund investment and risk management processes. It is difficult to assess climate risk alone, without considering ESG broadly.

Our answers to the consultation questions are below:

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 be considered in developing the requirements? Please explain your view

We welcome as a first step to introduce Climate risk into the FMCC, but believe that the other inter-related ESG challenges that we face should follow as they are integrally related to Climate risks.

We face broad resource depletion from poor management and overuse, pollution from inadequate environmental management, inequality from again poor management and these are only exacerbated by the consequences of our changing climate. Biodiversity and forest loss are the consequences of our resource overuse and inevitably also a contributor to climate emergency. Loss of our carbon sinks is a major factor in a warming planet and their protection a potential substantial mitigator. We believe that sustainable finance more broadly ought to be considered in developing the requirements. All indications are that we don't have many years to adjust finance to our new reality. We must use correct and consistent language that reflects the difficult reality we face.

Additionally, the terminology used in the SFC paper seems to move between Climate and ESG without clarity in several places, indicating a potential confusion in terms of what is relevant to monitor and what is material.

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?

Most other parts of the FMCC risk management framework are applicable to discretionary accounts managed under an investment mandate or pre-defined portfolio, and the role of a fund manager typically extends to the assessment and supervision of portfolio related risks in all types of portfolio whether discretionary or non-discretionary. The difference between each lies in the level of control available to the fund manager in responding to such risks within their investment mandate.

However, even where the investment mandate is pre-defined or non-discretionary, we believe the fund manager should still have any obligation to monitor and report on portfolio related climate risks so that these are clearly disclosed to the investor.

As the SFC has acknowledged, non-discretionary accounts make up a significant proportion of the AUM held by licensed corporations in Hong Kong. If we truly want to contribute to decarbonizing our economies, and enhance market awareness and investor reporting in respect of Climate risks then these

non-discretionary accounts should also be included within the scope of the new Climate change requirements.

Climate and environmental risk affects all portfolios equally so to monitor negative consequences in these non-discretionary portfolios and ensure proper reporting to investors, the same requirements ought to apply.

Finally, we could argue that regardless of account type, there is an opportunity to educate investors on the risks of climate and other material environmental and social challenges that may impact their portfolio investments. Given the urgency and the desire to integrate these considerations, we should not lose this opportunity to enhance investor reporting, regardless of account type.

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?

Yes, we strongly support the reference to the TCFD recommendations as the basis for reporting. It is important that the various guidelines and standards being developed and introduced are consistent and clear in a globalized world where fund managers and investors often operate in multiple regions. The use of a consistent reference point also helps with international comparison of portfolios and will avoid confusion and undue burden for fund managers.

TCFD has gained wide acceptance, is integrated into the UN PRI reporting, into stock exchanges' expectations (e.g. HKEx), referred to in certain regulations, and can easily be adopted broadly as it built on existing frameworks (e.g. ISO, GRI, SASB, the principles of management systems). There is no other standard or framework being discussed at international or other levels for such purpose.

We would also recommend paying attention to the Task Force on Nature-Related Financial Disclosure for similar clarity in any later enhancements to FMCC since this is likely to be introduced as an important biodiversity standard.

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.

We believe that this respects the FMCC Principle of Proportionality and thus is consistent. That said, the points above stand and the substantial environmental and social challenges we face are the same and relevant regardless of portfolio size. That means a fund manager's duty to consider climate, the substantial environmental and social challenges of Climate change. It also means that fund managers - large or small - cannot ignore the physical, transition and liability risks when seeking to supervise and monitor risks in an asset portfolio. Similar thresholds have, however, been set in other jurisdictions so following a similar approach to EU on proportionality seems to make sense.

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 believe "relevance" and "materiality" shown in the flow chart of Appendix 3 are not clearly defined and their process explained in the Paper.

Under paragraph 73 of the Consultation Paper, we would like to reiterate that we believe that Climate-related risks are, at a sector level, systemic risks that are interlinked with all other extra-financial risks.

In terms of governance and fund management, we would agree with the proposed requirements that climate related risks should be taken into account in investment management process for funds and that the board and management should naturally oversee the integration process. It should then also follow that managers should incorporate climate-related risks into existing frameworks and then be subject to climate related disclosures that are in line with the materiality of the risks they have assessed during their internal analysis. Such materiality analysis process should follow good international practices such as those laid by SASB or the GRI. It is understood that organisations may be looking at short-term financings but are supposed to be managed as if they were to be operational forever, making the medium to long-term climate-related risks relevant.

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?

Yes, since integrating climate-related impacts into transaction assessments should be considered part of regular portfolio risk management and reporting, then any fund manager that has decided climate-related risks are irrelevant should still be required to explain its rationale for making this conclusion and provide this report to investors. It is quite possible that the underlying rationale for such a conclusion change over time, or that investors wish to seek further clarity on these conclusions from the fund manager.

The question also arises as to the materiality triggers for determining whether Climate risks are relevant or not. As with most portfolio risks, the usual approach is for these to be assessed, managed and reported on to investors so that the investors can gain a clear picture of the relevance of these risks to the portfolio.

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?

Yes, agreed, this is a good place to start. This helps capture the reporting required for investors in different entity level funds on climate risks impacting their specific portfolio, as well as a broader view of the fund manager's overall strategy on climate-related impacts.

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 believe that this respects the FMCC Principle of Proportionality and thus is consistent.

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.

Under paragraph 84 of the Consultation Paper, we would highlight the fact that the Asian region is particularly at risk of Climate-related impacts.

We believe the transition timelines to comply with baseline requirements and enhanced standards are appropriate.

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Should you have any questions on the foregoing, please feel free to contact us at [redacted] or telephone -

Yours faithfully,