

## **EY Comments on SFC Consultation Paper on the Management and Disclosure of Climate-related Risks by Fund Managers (“Consultation”)**

EY is a keen supporter of green finance and has been actively involved in the inclusion and development of Environmental, Social and Governance (“ESG”) considerations within the financial sector. Our Climate Change and Sustainability Services, Wealth and Asset Management and Financial Services Risk Management teams provide dedicated assistance to various industry participants to implement ESG best practices in their operations in order to meet regulatory and investor needs. In this regard EY welcomes the proposals from the Securities and Futures Commission (“SFC”) to strengthen the management and disclosure of climate-related risks for fund managers in Hong Kong (“HK”) and is grateful for this opportunity to provide feedback on this Consultation.

1. We support the broad alignment of the proposals in the Consultation with the framework set by the Financial Stability Board Task Force on Climate-related Financial Disclosures (“TCFD”) Recommendations as this reflects the need for consistency among international regulatory frameworks for sustainable finance.
2. Although climate-related risks are only part of the overall Environmental part of the ESG agenda, we agree that there is an urgent need for the SFC to address climate-related risks during the initial phase. The substantial impact from climate change has also been highlighted by The Network of Central Banks and Supervisors for Greening the Financial System (NGFS) and the Hong Kong Monetary Authority (HKMA). Perhaps subsequent proposals by the SFC may include decarbonisation considerations as well since it will support the HK government’s net-zero carbon emission target by 2050.
3. The proposed transition periods for Large Fund Managers and other fund managers to comply with the proposals are appropriate from our viewpoint as this will allow fund managers to have sufficient time and resources to implement and comply with the proposed requirements.
4. Fund managers are required to assess the relevance and materiality of climate-related risks in order to meet the relevant requirements in the Consultation. Currently, in the absence of a standardized climate risk assessment methodology, evaluating the relevance and materiality of climate-related risks of investment portfolios can be a complex process requiring multiple assumptions. Therefore it will be helpful for the industry if the SFC can provide more qualitative and/ or quantitative guidance to determine materiality and relevance, including examples of assessment methodologies for reference.
5. Fund managers are required to provide justification and appropriate records to explain when climate-related risks are considered irrelevant to their investment and risk management purposes after assessment. It would be helpful for the industry if the SFC can provide further guidance on the type of records required to justify such situations.

6. The SFC is a member of the International Platform on Sustainable Finance (IPSF) Working Group on Taxonomies, co-led by China and the EU, which is developing the Common Ground Taxonomy. The SFC could consider to provide guidance and best practice examples to assist fund managers in HK in getting ready to adopt the Common Ground Taxonomy. This will be helpful for the industry as climate-related risks are subject to different categorizations depending on the type of industry, so a classification system for sustainable activities or projects aligning with the Common Ground Taxonomy can be considered to enhance consistency.
  
7. We understand that the SFC seeks to apply the proposals in the Consultation to all fund managers licensed in Hong Kong. As an international asset management hub, in addition to many global asset managers catering to the retail public, many family office, hedge fund and private equity managers are also based in Hong Kong. Many of these alternative fund managers who serve professional investors and institutions are also SFC licensees. There are key differences between these two groups of managers which may merit the SFC considering providing more guidance or even allowing certain requirements to be out of scope for alternative fund managers.
  - 7.1. Alternative fund managers engage in a wider range of strategies than global fund managers such as macro, loans, derivatives, startups and other bespoke funds. Common investments would include collateralized debt instruments; credit default swaps; options; loans; pre-IPO stocks; debentures; angel investments; cryptocurrencies and; start-up projects. We would recommend more guidance from the SFC on how alternative fund managers can identify, assess, manage and monitor the relevant and material climate-related risks of these types of investments and also of investment strategies that invest in a combination of these investments in order for them to meet the baseline requirements for risk management. Perhaps the SFC may also consider whether funds with these strategies and investments should be scoped out from the risk management requirements in the Consultation.
  
  - 7.2. Alternative fund managers normally have a smaller number of investors per fund and also manage fewer funds compared with global fund managers. Therefore the average alternative manager will have comparatively less internal support with staffing ranging from 6 to 20 personnel even if their assets under management (“AUM”) amount to more than HK\$4 billion. In this regard, we recommend that the SFC consider setting a higher threshold AUM for alternative fund managers to be in scope for additional risk management requirements and disclosures or even allow certain exemptions from the proposals taking into account their limited resources.
  
8. There are concerns about the data quality and accuracy relating to climate-related risks provided by various service providers, especially for the purpose of calculating the weighted average carbon intensity (“WACI”) of Scope 1 and 2 GHG emissions. This could prove to be relatively technical and challenging for fund managers as data availability is also an issue. We suggest that the SFC should provide more guidance in the selection of third-party data providers or alternatively encourage fund managers to obtain third-party verifications or assurances to ensure data reliability, for example by relying on accounting professionals to provide written assurances or audits.

- 8.1 We support a two-tier approach with Large Fund Managers adopting a more robust approach and making more detailed disclosures however it may be impractical or cost-ineffective to apply WACI calculation requirements on very small-sized funds or those which are about to be terminated even if climate-related risks are assessed to be material. Therefore, it will be helpful if the SFC could provide more clarification on disclosures for this type of fund and consider whether any fund with less than a certain minimum amount of AUM would qualify as a small-sized fund and therefore be allowed to be scoped out of the WACI calculation requirements.