

## Delving deeper into the baseline requirements and enhanced standards of Hong Kong's climate-related risks framework under its Fund Manager Code of Conduct (FMCC)

A more detailed look, following on from the article "Hong Kong enters into a client friendly era for investment funds"

### Baseline Requirements (for all fund managers)

These apply to Fund Managers that oversee the overall investment management function of a collective investment scheme, or investment fund. These may comprise criteria across the governance, and investment and risk management functions of a fund, even if it is not distributed in Hong Kong.

The extent of compliance should be determined by the principle of proportionality, such as the complexity, size, nature and risk profiles of the fund manager, as well as each individual fund's investment strategy. For instance, if a Fund Manager is in charge of investment for just a segment of a fund, it will not be expected to comply with requirements spanning the entire entity; compliance should in this event be restricted to the section of the assets under its management, as well as the role assigned to it.

However, a Fund Manager retains the responsibility of ensuring that baseline requirements are complied with even if it delegates investment or risk management competencies to a subsidiary or third party.

### Enhanced Standards

These apply to Large Fund Managers that manage AUMs of at least HK\$8 billion. Apart from complying with baseline requirements, these managers – due partly to their bigger sizes and corresponding resources – will also need to follow more stringent standards.

### i. Governance:

#### Baseline Requirements

This defines the board/board committee and management's roles in presiding over the implementation of climate-linked considerations into a fund's investment and risk management processes.

Among other things, a board/board committee should set out a framework to execute this work, including when and how it should be kept abreast of climate-related issues.

Management should assign senior roles and responsibilities for managing climate-related risks as well as how such efforts are tracked, including the setting of goals and action plans. It should also allocate competent and sufficient human and technical expertise toward the discharging of such duties, such as relevant training and the adoption of climate-related data from external sources.

### ii. Investment Management:

#### Baseline Requirements

This refers to the identification of material climate-linked risks in the investment strategy of each fund that a Fund Manager oversees; where relevant, such risks should be factored into the investment management process and reasonable steps taken to assess the impact of these risks on fund performance. Exceptions should be disclosed and records appropriately maintained.

### iii. Risk Management

#### Baseline Requirements

Fund Managers should factor in climate-linked risks into risk management processes and ensure that reasonable steps are taken to identify, assess, manage and monitor them based on each fund strategy. They should also notify the board about climate-related concerns on a regular basis, and use appropriate tools and metrics to appraise and quantify such risks.

#### Enhanced Standards

Large Fund Managers should assess the relevance and utility of scenario analysis in evaluating the resilience of investment strategies to climate-related risks under different pathways. They should then develop a plan to implement an analysis if the assessment result is deemed material and relevant. In such a case, where data is available or reasonably derived, reasonable steps should then be taken to identify portfolio carbon footprints of the Scope 1 and Scope 2 greenhouse gas (GHG) emissions – the use of Scope 3 is encouraged as well if data allows for it - tied to the funds' underlying investments, among other things.

Large Fund Managers can refer to the [PCAF Standard](#) which provides guidance on methods to estimate and calculate the GHG emissions of various asset classes.

### iv. Disclosures:

The need for disclosures at entity Fund Manager level aims at reducing the compliance burden if the same policies and processes apply consistently across individual strategies and funds; Fund Managers may yet disclose at fund level if it is more appropriate.

#### Baseline Requirements

As indicated earlier, disclosures on governance at entity Fund Manager level should describe the governance structure as well as salient issues such as the board and management's roles and responsibilities; the process and regularity of climate-linked reports made to the board or board committee; and how management plans to monitor efforts to manage climate-related risks.

Again, disclosures on investment and risks management at entity Fund Manager level should include steps taken to integrate material climate-linked risks into the investment management process; as well as describe processes for

identifying, assessing, managing and monitoring such risks, including key tools and metrics used. Exceptions, at entity or fund level, should be disclosed if climate-linked risks are deemed to be irrelevant following assessment, and records appropriately maintained.

#### Enhanced Standards

This refers to disclosures on risk management, which, at entity or fund level, should among other things set out engagement policy and how it is managed, including examples of how material climate-linked risks are managed on a practical basis. It should also at the very least provide portfolio carbon footprints of Scope 1 and Scope 2 GHG emissions – Scope 3 is encouraged in the event of suitable data - linked to a fund's underlying investments, as mentioned above.

#### When does it take effect

Large Fund Managers have 12 months till August 20, 2022, and 15 months till November 20, 2022, before they need to comply with baseline requirements and enhanced standards, respectively. Other Fund Managers have 15 months till November 20, 2022, before they need to comply with baseline requirements.

### Contact us



**Penelope Shen**

Partner, Hong Kong

T: +852 3166 6936

E: [penelope.shen@shlegal.com](mailto:penelope.shen@shlegal.com)