



Hong Kong

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SFC ANNOUNCES STRATEGIC FRAMEWORK FOR GREEN FINANCE IN HONG KONG

On 21 September 2018, the Securities and Futures Commission (SFC) published its strategic framework¹ for developing green finance in Hong Kong. Building on Hong Kong's green bond initiatives, the SFC is keen to develop green finance opportunities arising from Mainland China's transitioning to a green economy and to position Hong Kong as a connector of green finance flows between the Mainland and the rest of the world.

The green finance strategic framework identifies international regulatory developments geared towards supporting green finance. These include the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) set up by the Financial Stability Board and Mainland China's targeted introduction of a mandatory requirement for listed companies to disclose environmental information by 2020 (**Mandatory Requirement**). The Mandatory Requirement will extend to A/H share issuers listed on the Hong Kong Stock Exchange (HKEx or the Hong Kong Exchange).

The SFC's five-pronged action agenda on green finance development proposes:

- Improving HKEx-listed companies' disclosure of environmental and climate-related information, by aligning disclosure requirements with the TCFD recommendations;

- Engaging with the asset management industry in formulating appropriate guidance and possibly obligations for asset managers on disclosure of how and to what extent environmental factors are taken into account by their investment processes and risk assessments;
- Facilitating the development of a broader range of green investment products, including listed, unlisted, exchange-traded and OTC green products. This would involve providing guidance on disclosure, and developing and promoting the listing and trading of green financial products, such as bonds, indices and derivatives, on HKEx;
- Supporting investor awareness of and capacity building in green finance; and
- Promoting Hong Kong as an international green finance centre through participation in international initiatives.

A cross-divisional working group charged with developing policies to promote Hong Kong as an international green finance hub has also been set up within the SFC.

¹ [https://www.sfc.hk/web/EN/files/ER/PDF/SFCs Strategic Framework for Green Finance - Final Report \(21 Sept 2018....pdf](https://www.sfc.hk/web/EN/files/ER/PDF/SFCs%20Strategic%20Framework%20for%20Green%20Finance%20-%20Final%20Report%20(21%20Sept%202018....pdf)

HKEx-Listed Company Disclosure of Corporate Environmental and Climate Change-Related Information

The SFC outlined its top priority as enhancing the reporting of environmental information with an emphasis on climate-related disclosure by HKEx-listed companies. The SFC will aim to align Hong Kong's requirements with TCFD recommendations and with the Mainland's Mandatory Requirement.

One of the existing challenges to providing a high standard of environmental and climate-related disclosure is that some listed companies treat environmental and climate-related disclosures as a box-ticking exercise and fail to provide the climate-related financial disclosure increasingly demanded by institutional investors. Another difficulty in many jurisdictions is that environmental, social and governance (ESG) disclosure is not required at the same time as financial reporting, which has led to a failure to prioritise environmental and sustainability issues.

Initiatives to improve the quality of environmental and climate-related disclosure include the PRC's Mandatory Requirement and a series of reviews by the French financial services regulator comparing ESG disclosures by domestically-listed companies with those of listed companies in other jurisdictions. In 2016, HKEx upgraded all environmental disclosures from "recommended practice" to "comply or explain", and in 2018 it published the first review of HKEx-listed companies' compliance with its ESG Reporting Guide.

Lack of convergence of reporting standards has also been a significant issue not only between different jurisdictions, but between the various international frameworks as well. The Global Reporting Initiative², Carbon Disclosure Project (or CDP), Climate Disclosure Standards Board and the Sustainability Accounting Standards Board all differ in their recommendations. TCFD has been working to address this and in June 2017 published a framework for climate-related financial disclosures, which aligns with existing international reporting frameworks. The TCFD framework aims to facilitate companies' disclosure of the financial impact of climate change-related risks and opportunities across the following four areas:

- Governance related to climate change risks and opportunities;

² An international independent standards organization which helps businesses and governments to understand and communicate their impact on critical sustainability issues including climate change.

- Strategy – the actual and potential risks and opportunities that climate change may bring for the company's business, strategy and financial planning (TCFD recommends the employment of qualitative and/or quantitative scenario analysis for disclosure of the resilience of companies' strategies and financial plans to different climate change scenarios);
- Risk management – the identification, assessment and management of climate-related risks; and
- Metrics and targets – metrics and targets assessing and managing climate-related risks and opportunities.

The Global Reporting Initiative has already announced that it aims to align its approach with the TCFD recommendations and a number of jurisdictions have implemented initiatives supporting them. A group of Chinese and British financial institutions is piloting the TCFD recommendations with the approval of their home regulators. The European Commission is planning to align its guidelines on non-financial information with the TCFD guidance by the second quarter of 2019. In the UK, the London Stock Exchange's latest ESG Reporting Guidance welcomed the TCFD recommendations, while the UK's Green Finance Taskforce has supported implementing them, and Parliament's Environmental Audit Committee has recommended that a deadline is imposed by the UK Government for all listed companies to report on climate-related risks and opportunities on a comply or explain basis, in accordance with the TCFD guidance, by 2022.

In France, the financial markets regulator assessed that the current disclosure framework is already consistent with the TCFD framework, as the French Energy Transition for Green Growth Act, Article 173, requires disclosure of financial risks related to the effects of climate change, of mitigating measures adopted and of the environmental impact of companies' activities.

Canada's securities regulators conducted a joint analysis of alignment of the existing disclosure requirements with the TCFD recommendations and aim to introduce new disclosure guidance for listed companies on disclosure of climate change-related risks, opportunities and financial effects, possibly along with new disclosure requirements.

Australia's Securities and Investments Commission has publicly encouraged companies and directors to refer to the TCFD recommendations as a key resource for understanding, identifying and managing climate risks and opportunities.

Currently, a review of ASX 300 climate change-related disclosures is being conducted, and a review of the applicable guidance on disclosure for stakeholders has commenced as well.

Singapore's Stock Exchange, as Vice Chair of the TCFD, hosted a conference on the TCFD recommendations in 2018. The Monetary Authority of Singapore has encouraged corporations and financial institutions to apply international standards and guidelines such as the TCFD recommendations.

Hong Kong's SFC has officially supported the TCFD recommendations and is currently working to improve HKEx-listed companies' disclosure of environmental information, particularly in relation to climate change, to align with the TCFD recommendations. Going forward, the SFC's main priority will be to work with HKEx on aligning the requirements for HKEx-listed companies with the TCFD recommendations, with the Mainland's policy direction and with other leading markets. The HKEx Listing Rules may be amended to achieve this.

The SFC plans to work with industry associations, professional bodies and the Investor Education Centre to improve awareness of the TCFD recommendations among companies listed on HKEx and the investing public. The SFC recommends the online TCFD Knowledge Hub³ and the papers by the United Nations Environment Programme Finance Initiative as self-help resources.

Asset managers and sustainable investing

The potential for better risk management and greater returns, and the rising demand from ESG-oriented investors, are all identified as factors that encourage sustainable investing. Hong Kong's Monetary Authority, for example, has been incorporating ESG principles into its investment process.

Among the challenges to further development highlighted are the lack of quality and comparable corporate ESG data, insufficient disclosure of whether and how asset managers conduct sustainable investing, a failure to address clients' ESG preferences when conducting client suitability assessments, lack of clarity on the duty of asset managers to consider environmental factors when making investment decisions, and the risks of "greenwashing" (i.e. where asset managers promote themselves as "green" or "sustainable" but fail to incorporate these factors in the investment process). Authorities in various jurisdictions have sought to address these issues with the following measures:

- Hong Kong's SFC released Principles of Responsible Ownership⁴ in 2016, encouraging dialogue on ESG matters between investors and investees.
- In France, authorised asset managers are required to disclose how they incorporate ESG factors into investment and risk analysis on a "comply or explain" basis under Article 173 of the French Energy Transition for Green Growth Act. Some French businesses already require asset managers located outside France to comply with Article 173. The European Commission is also looking at: (i) requiring disclosure of how ESG factors are implemented in asset managers' risk and investment processes; and (ii) including ESG factors in investment firms' advice to clients.
- In the PRC, the Asset Management Association of China has consulted on proposed voluntary guidelines on green investment practices for public and private securities fund managers.

Hong Kong's agenda includes aligning with the latest regulatory frameworks of the above jurisdictions. The following steps are proposed:

1. A survey of asset managers and asset owners active in the Hong Kong market focused on their sustainable investment practices (including their commitment, investment process, post-investment ownership practices and reporting of ESG performance). This will inform the SFC's direction on the policies to pursue;
2. An enquiry by the SFC's Investment Committee into the extent to which its external managers are incorporating ESG principles into their investment and risk analysis processes; and
3. Further work with the CFA Institute and the United Nations Principles for Responsible Investment on enhancing knowledge of the ways to integrate ESG into the investment process.

Other aspects of green finance

Investment products

³ <https://www.tcfidhub.org/>

⁴ [https://www.sfc.hk/web/EN/files/ER/PDF/Principles of Responsible Ownership_Eng.pdf](https://www.sfc.hk/web/EN/files/ER/PDF/Principles%20of%20Responsible%20Ownership_Eng.pdf)

With continued growth in the range and number of green investment products, regulators are turning their attention to product quality and ensuring market integrity. In France, the financial markets regulator has provided recommendations to the industry based on its review of the disclosure and marketing practices of socially responsible investment funds. It has also issued guidelines for funds that want to qualify for the “Energy and Ecological Transition for Climate” label. In Malaysia, Guidelines on Sustainable and Responsible Investment Funds have been released, while Guernsey has issued Green Fund Rules. The European Commission will be establishing labels for green financial products as part of its Action Plan on Sustainable Finance. Labels aim to make it easier for investors to identify products that comply with green criteria.

Stock Exchange Green Initiatives

Stock exchanges have been exploring green business opportunities:

- Luxembourg’s Green Exchange lists over half of listed labeled green bonds world-wide and also lists sustainable investment funds. Its website clearly displays green financial instruments and explains the requirements for listing and displaying sustainable instruments on the exchange.
- In June 2018, the London Stock Exchange listed its largest ever green bond, the US\$1.58 billion green bond of Industrial and Commercial Bank of China, London branch. Green and sustainable equity capital raised on the exchange grew 197% year-on-year and the number of listed ESG-related ETFs reached 31 with GBP 3.97 billion of assets under management.
- In April 2018, the Shanghai Stock Exchange released its Vision and Action Plan for Supporting Green Development and Promoting Green Finance for 2018-2020 with a dedicated group launched to promote green finance innovation and development.
- There has also been active cross-market cooperation among the exchanges. The Luxembourg Green Exchange has collaborated with the Shanghai and Shenzhen Stock Exchanges on synchronous displays of Chinese green bond indices in Luxembourg and the PRC, and a Green Bond Channel has been set up to display green bonds listed on the Shanghai Stock Exchange on the Luxembourg Green Exchange. The London Stock Exchange has partnered with Japan Exchange Group

in promoting sustainable investment through financial market infrastructure initiatives, while the New Zealand Stock Exchange has entered into agreements with the Hong Kong Exchange and the Singapore Exchange on collaborating on green finance and sustainability initiatives.

The SFC is considering producing guidance on product disclosure and reporting compatible with international guidelines to support the credibility of green investment products offered in Hong Kong. It also plans to work with HKEx to promote the listing and trading of green financial products, including bonds, indices and green derivatives.

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