

MEMO# 34070

March 10, 2022

Asia ESG: Recap of HK SFC Industry Workshop on ESG Funds

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TO: ESG Task Force

Global Regulated Funds Committee - Asia RE: Asia ESG: Recap of HK SFC Industry Workshop on ESG Funds

On 4 March 2022, the Hong Kong Securities and Futures Commission (SFC) hosted an industry workshop on ESG fund applications. During the workshop, SFC staff shared observations and regulatory expectations for how a fund could demonstrate its compliance with the Circular to management companies of SFC-authorized unit trusts and mutual funds - ESG funds ("ESG Fund Circular").[\[1\]](#)

The SFC has published the [workshop presentation materials](#) of the workshop on their website.[\[2\]](#)

Some key takeaways from the SFC workshop are:

- **Definition of ESG Funds.** The SFC reiterated that an ESG fund should incorporate ESG factors as its key investment focus, i.e., ESG factors have a significant influence on the fund's selection of underlying assets. Similarly, only UCITS funds that incorporate ESG factors as the key investment focus are eligible as ESG funds in Hong Kong ("UCITS ESG funds"). This is irrespective of whether the fund is an Article 8 or 9 fund under the EU Sustainable Finance Disclosure Regulation (SFDR). The SFC further noted that SFDR Article 8 or 9 funds should observe the naming requirement set out in the ESG Fund Circular, i.e., not naming or marketing itself in HK as ESG fund if it is not authorized as ESG funds in HK.
- **Deemed Compliance for UCITS ESG Funds.** While the UCITS ESG funds that meet disclosure requirements for SFDR Article 8 or 9 funds will be deemed to have generally complied with the disclosure requirements set out in the ESG Fund Circular, the SFC may request clarification on any unclear disclosure. The SFC noted that the delay of SFDR Level 2 requirements would not have a material impact on complying with the disclosure requirements under the ESG Fund Circular, given that UCITS funds, in any event, are required to comply with the periodic disclosure requirements set out in the SFDR Level 1 text, which apply as of 1 January 2022. The SFC also noted that the European Supervisory Authorities (ESAs) published a supervisory statement[\[3\]](#) in

February 2021 that recommends using the draft Regulatory Technical Standards for SFDR as a reference for the purpose of preparing periodic reports.

- Investment Threshold for ESG Thematic Strategy. An ESG fund adopting thematic strategy should primarily invest in ESG-themed investments - at least 70% of net asset value as required under the Code on Unit Trusts and Mutual Funds for funds representing a particular strategy/region/market.^[4]
- Influence of ESG Assessment Outcome for Positive Screening Strategy. ESG funds that adopt best-in-class/positive screening strategy should demonstrate that the ESG assessment outcome has a significant influence on the stock selection process. In particular, for stock selection based on ESG ratings, the fund should primarily invest in companies with high ESG ratings within the investment universe.
- Reduction of Investment Universe for Positive Screening Strategy. ESG funds should disclose the proportion (at least 20%) of companies that are removed from the investment universe. Acknowledging that the ESG space is still evolving, the SFC will monitor the effectiveness of the 20% threshold and communicate any possible changes to that threshold with the industry as soon as possible.
- Comparable Reference Benchmark. Where an ESG fund compares its ESG rating against a reference benchmark, the benchmark should be comparable and relevant to the fund's particular geographical/sector focus. The benchmark does not necessarily need to be an ESG-focused benchmark. For instance, an Asia-focused ESG fund compares the average ESG score of its portfolio to the MSCI Asia index.
- Measurable ESG Impact for Impact Investing. The investments of an impact fund should generate positive ESG impact, e.g., investment in green bonds. Such impact should be measurable and disclosed as part of the fund's periodic assessment in order to demonstrate how the fund has attained its ESG-related objectives.

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endnotes

[1] See Circular to Management Companies of SFC-authorized Unit Trusts and Mutual Funds - ESG Funds, available at

<https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/products/product-authorization/doc?refNo=21EC27>. Also See ICI Memorandum [33665], dated 7 July 2021, available at <https://www.ici.org/memo33665>.

[2] See SFC workshop presentation, available at

<https://www.sfc.hk/-/media/files/PCIP/FAQ-PDFS/Industry-workshop-on-ESG-fund-applications-4-March-2022.pdf>

[3] See Joint ESA Supervisory Statement on the application of the Sustainable Finance Disclosure Regulation, dated 25 February 2021, available at

https://www.esma.europa.eu/sites/default/files/library/jc_2021_06_joint_esas_supervisory_statement_-_sfdr.pdf.

[4] See Code on Unit Trusts and Mutual Funds, at Chapter 7, paragraph 7.42, available at

<https://www.sfc.hk/-/media/EN/assets/components/codes/files-current/web/codes/section-ii-code-on-unit-trusts-and-mutual-funds/section-ii-code-on-unit-trusts-and-mutual-funds.pdf>.

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