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MAS Sets Out Enhanced Disclosure and Reporting Guidelines for Retail ESG Funds

Introduction

Along with the steady rise in investments in Environmental, Social and Governance ("**ESG**")-related financial products, greenwashing has emerged as a significant regulatory concern. In this regard, it has been reported that there has been a spate of greenwashing allegations against financial institutions offering ESG funds.

In Singapore, to combat greenwashing of retail ESG funds and boost investor confidence, the Monetary Authority of Singapore ("**MAS**") issued MAS Circular No. CFC 02/2022 ("**Circular**") on 28 July 2022 setting out enhanced disclosure and reporting requirements/guidelines and shared its expectations on how existing requirements under the Code on Collective Investment Scheme ("**CIS Code**") and the Securities and Futures (Offers of Investment) (Collective Investment Schemes) Regulations 2005 ("**SF(CIS)R**") apply to retail ESG funds. The Circular will take effect on **1 January 2023** ("**Effective Date**").

In this Update, we briefly highlight the key requirements and guidelines concerning retail ESG Funds.

Who and What is covered?

The Circular applies to retail ESG Funds and is relevant to capital markets services licensees carrying out fund management activities and approved trustees under Section 289 of the Securities and Futures Act 2001 ("**SFA**").

An ESG Fund refers to an authorised or recognised scheme under the SFA that:

(a) Uses or includes ESG factors as its key investment focus and strategy (i.e. ESG factors significantly influence the scheme's selection of investment assets); and
(b) Represents itself as an ESG-focused scheme.

Typical ESG investing strategies where ESG factors "significantly influence a scheme's selection of investment assets" include impact investing and ESG inclusionary investing. Examples include broad strategies (such as best-in-class positive screening and ESG tilts) and thematic strategies (such as specific focus on ESG outcomes - for instance, low carbon transition), among others.

Conversely, if the scheme: (i) only uses negative screening, which refers to applying a set of filters to determine which companies, sectors or activities are not eligible to be included in a specific portfolio; or (ii) merely incorporates or integrates ESG considerations in its investment process (e.g. incorporate financial factors (other than ESG factors) in its investment process and therefore ESG is not the "main driver of investment decisions but is just one of the factors considered in the investment process"), MAS will *not* regard such a scheme as having an ESG investment focus for purposes of subparagraph (a) above.

In determining whether a scheme is substantially ESG-focused in terms of its investment portfolio and/or strategy, MAS also elucidated the factors it will take into consideration. These factors include whether the scheme's net asset value is "primarily invested" according to the scheme's investment strategy. Industry practice generally regards the scheme to be "primarily invested" if two-thirds of the scheme's net asset value is invested according to the scheme's investment strategy.

Recognised Schemes

The Circular also applies to recognised schemes that meet the criteria in subparagraphs (a) and (b) above. This is addressed under Part D of the Circular. MAS will assess compliance of a recognised scheme with the requirements set out in the Circular by taking into account the scheme's compliance with the relevant ESG rules in their home jurisdictions, if any. Specifically, UCITS (Undertakings for Collective Investment in Transferable Securities) schemes that are ESG Funds would be considered to have complied with the disclosure requirements in the Circular if they fall within Article 8 or 9 of EU's Sustainable Finance Disclosure Regulation. Do note that the name of the UCITS scheme must still comply with the naming requirements addressed under Section B in the Circular.

Naming Requirements

The Circular addresses naming requirements of ESG funds under Section B. Requirements pertaining to the name of a scheme are set out at Chapter 4.1 of the CIS Code and, among others, the name of the scheme must be "appropriate, and not undesirable or misleading". In the context of ESG Funds, if the scheme's name includes or uses ESG-related or similar terms (for instance "sustainable", "green" etc.), the scheme must reflect an ESG focus in its investment portfolio and strategy in a substantial manner and be in compliance with the guidelines in the Circular. MAS will deem the name "inappropriate" if the name of the scheme uses an ESG-related term but fails to comply with the requirements/guidelines. MAS set out certain factors it will consider in deciding whether or not a scheme is substantially ESG-focused (briefly discussed above). For more details, please refer to Section B of the Circular.

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Enhanced Disclosure and Reporting Requirements

Prospectus Disclosure Requirements and Guidelines
Requirements on information to be disclosed in a scheme's prospectus are set out in the Third Schedule of the SF(CIS)R. Prospectuses of ESG Funds lodged with MAS on or after the Effective Date must also comply with the following requirements and/or guidelines in the Circular:

- ***Clearly define ESG-related terms and disclose information in the prospectus relating to investment focus, investment strategy, reference benchmark and risks associated with investing in the scheme***. Paragraph 11 of the Circular sets out the information along with some examples. Such information includes:

  - Investment focus – (i) the ESG focus of the scheme; (ii) the relevant ESG criteria, methodologies or metrics used to measure whether the ESG focus is achieved.
  - Investment strategy – (i) describe how the sustainable investing strategy is used to achieve the scheme's ESG focus, the binding elements of the strategy in the investment process, and how the strategy is applied in the investment process on a continuous basis; (ii) include relevant ESG criteria, metrics or principles considered in the investment selection process; (iii) the minimum asset allocation into assets used to achieve the scheme's ESG focus.
  - Reference benchmark – (i) (where the scheme references a benchmark index to measure whether ESG focus is achieved) explain how the benchmark is consistent with or relevant to its investment focus; (ii) (where the scheme references a benchmark index for financial performance measurement only) state so.
  - Risks associated with the scheme's ESG focus and investment strategy, for instance, concentration in investments with certain ESG focus, limitations of methodology and data, etc.

  In cases where it is not "possible nor practicable for a manager to determine, at the individual asset level, the proportion of a scheme's net asset value that is invested in accordance with ESG investing approaches", MAS expects the manager to explain in the prospectus/offering documents how the scheme's investments are substantially ESG-focused.

- ***Indicate that the scheme is an ESG Fund in the respective OPERA form***

- ***Provide additional information by date of lodgement and indicate in the prospectus where such additional information may be accessed***. The fund manager or index provider must make the additional information available on the fund manager's website or by other appropriate means. The additional information required to be provided is set out at paragraph 14 of the Circular ("**additional information**") and includes:

- the measurement and monitoring process of the ESG focus as well as related internal or external control mechanisms to monitor compliance with the scheme's ESG focus on a continuous basis;
- where the ESG data is obtained from, how it is used, the assumptions made where data is lacking;
- due diligence regarding ESG-related features of the scheme's investments; and
- stakeholder engagement policies (including proxy voting) that facilitate corporate behaviour of companies that the scheme invests in and contribute to meeting the scheme's ESG focus.

Annual Report Disclosure Requirements and Guidelines

Annual reports of ESG Funds (for financial year ending on or after the Effective Date) must include the following information:

- Details relating to how and the extent to which the scheme's ESG focus is fulfilled during the financial period. This should include a comparison with the previous period (if any);
- The actual proportion of investments that meet the scheme's ESG focus (if applicable); and
- Actions by the scheme to achieve the scheme's ESG focus, for example through engaging with stakeholders.

Please refer to Paragraph 13 of the Circular for more details.

Additional Information

The Circular also sets out additional information which should be made available by the fund manager or index provider on the fund manager's website or by other appropriate means. For details on the additional information, please refer to paragraph 14 of the Circular.

Concluding Words

With an increased focus in ESG investing, regulators globally are treating greenwashing and regulatory compliance seriously. Singapore is no exception, and this is underscored by, among others, MAS' issuance of this Circular setting out enhanced disclosure and reporting guidelines/requirements and its expectations on how relevant existing legal/regulatory requirements apply to retail ESG Funds.

Affected financial institutions should carefully review the Circular and the requirements/guidelines therein and assess how they impact their businesses and take steps to ensure compliance. If you require any assistance or advice, please feel free to contact our team below.

Contacts

Funds and Investment Management

Anne Yeo
Head, Funds and Investment Management

T +65 6232 0628

anne.yeo@rajahtann.com

Jasmine Chew
Deputy Head, Funds and Investment Management

T +65 6232 0454

jasmine.chew@rajahtann.com

Philip Yeo
Deputy Head, Funds and Investment Management

T +65 6232 0487

philip.yeo@rajahtann.com

Arnold Tan
Partner, Funds and Investment Management

T +65 6232 0701

arnold.tan@rajahtann.com

Sustainability

Lee Weilin
Head, Sustainability
Partner, Banking & Finance

T +65 6232 0707

weilin.lee@rajahtann.com

Disa Sim
Partner, Sustainability
Head, Appeals & Issues

T +65 6232 0415

disa.sim@rajahtann.com

Please feel free to also contact Knowledge and Risk Management at eOASIS@rajahtann.com

Our Regional Contacts

RAJAH & TANN | *Singapore*
Rajah & Tann Singapore LLP
T +65 6535 3600
sg.rajahtannasia.com

R&T SOK & HENG | *Cambodia*
R&T Sok & Heng Law Office
T +855 23 963 112 / 113
F +855 23 963 116
kh.rajahtannasia.com

RAJAH & TANN 立杰上海
SHANGHAI REPRESENTATIVE OFFICE | *China*
Rajah & Tann Singapore LLP
Shanghai Representative Office
T +86 21 6120 8818
F +86 21 6120 8820
cn.rajahtannasia.com

ASSEGAF HAMZAH & PARTNERS | *Indonesia*
Assegaf Hamzah & Partners

Jakarta Office
T +62 21 2555 7800
F +62 21 2555 7899

Surabaya Office
T +62 31 5116 4550
F +62 31 5116 4560
www.ahp.co.id

RAJAH & TANN | *Lao PDR*
Rajah & Tann (Laos) Co., Ltd.
T +856 21 454 239
F +856 21 285 261
la.rajahtannasia.com

CHRISTOPHER & LEE ONG | *Malaysia*
Christopher & Lee Ong
T +60 3 2273 1919
F +60 3 2273 8310
www.christopherleeong.com

RAJAH & TANN | *Myanmar*
Rajah & Tann Myanmar Company Limited
T +95 1 9345 343 / +95 1 9345 346
F +95 1 9345 348
mm.rajahtannasia.com

GATMAYTAN YAP PATACSIL
GUTIERREZ & PROTACIO (C&G LAW) | *Philippines*
Gatmaytan Yap Patacsil Gutierrez & Protacio (C&G Law)
T +632 8894 0377 to 79 / +632 8894 4931 to 32
F +632 8552 1977 to 78
www.cagatlaw.com

RAJAH & TANN | *Thailand*
R&T Asia (Thailand) Limited
T +66 2 656 1991
F +66 2 656 0833
th.rajahtannasia.com

RAJAH & TANN LCT LAWYERS | *Vietnam*
Rajah & Tann LCT Lawyers

Ho Chi Minh City Office
T +84 28 3821 2382 / +84 28 3821 2673
F +84 28 3520 8206

Hanoi Office
T +84 24 3267 6127
F +84 24 3267 6128
www.rajahtannlct.com

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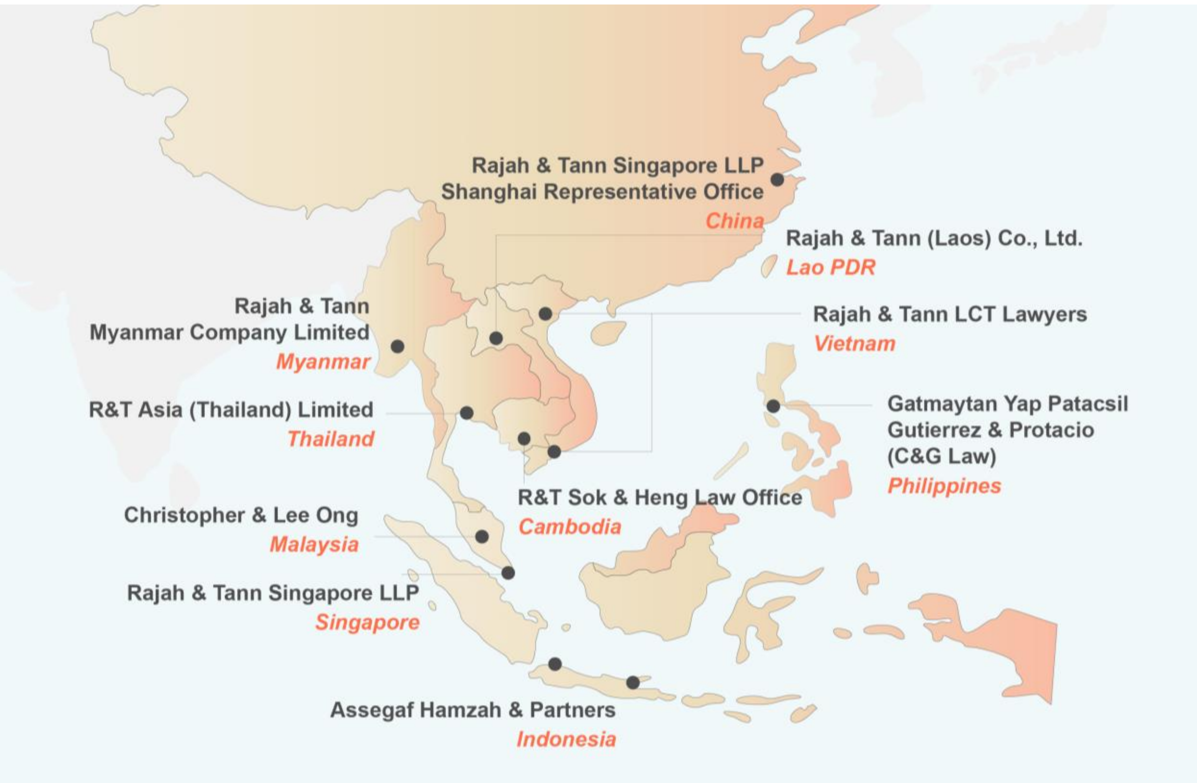

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