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ESG for Asset Managers



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Introduction

The role of environmental, social and governance (ESG) matters in the operations and investment management activities of asset managers has long been a subject of discussion. In recent years, however, the conversation has become more urgent and focused, driven by the growing evidence of the global impact of climate change. These concerns underlie the United Nations 2030 Agenda for Sustainable Development and 2015 Paris Agreement on Climate Change (**Paris Agreement**), the latter seeking to combat climate change and to direct finance flows towards low greenhouse gas emissions and climate-resilient development. The Paris Agreement was the impetus for a growing body of law and regulation in the European Union (EU) focused on ESG concerns and, in particular, ESG and sustainable investment. In other jurisdictions, including the United States (US), Hong Kong and Singapore, regulators have either adopted, or proposed to adopt, regulations or guidelines focused on similar concerns, although their scope and purpose may differ in significant ways from the EU.

At the same time, the conversation relating to ESG has become much more political and nuanced, particularly in the US. For example, in the US, private litigants, “red state” attorneys general and other US government officials have been increasingly critically scrutinising ESG-related investment activities. By contrast, certain investors, “blue state” officials and regulators continue to advocate for the inclusion of ESG factors in asset managers’ investment decision-making and proxy voting practices.

These conversations and controversies, which reflect differing attitudes on ESG and its role in asset management, will likely continue for the foreseeable future. For global asset managers, it is becoming increasingly difficult to navigate the differing regulatory approaches to and investor views on ESG in the jurisdictions in which they seek to offer and manage investment products.

In this chapter, we will discuss the primary regulatory framework relating to ESG and sustainable finance in several key jurisdictions, namely the EU, the United Kingdom (UK), Hong Kong, Singapore and the US.

EU

The EU has been leading the way in adopting rules and regulations focused on sustainable investment – with the EU Commission taking the decision in 2016 to make sustainable development a political priority – and ESG has remained front and centre of legal and regulatory developments ever since.

For the EU, sustainable finance is about reorienting investment towards sustainable technologies and businesses, recognising that major public and private investment is needed to

make the EU’s financial system sustainable and ensure European Member States are climate-neutral by 2050. To achieve this, in 2018, the EU launched its Action Plan on Sustainable Growth (**Action Plan**),¹ which set out 10 action points² with the key objectives of: (i) reorienting capital flows towards sustainable investment, in order to achieve sustainable and inclusive growth; (ii) managing financial risks stemming from climate change, environmental degradation and social issues; and (iii) fostering transparency and long-termism in financial and economic activity.

Based on the Action Plan, the EU Commission set out three building blocks as the foundation for building a sustainable financial framework in the EU: (1) a classification system, or “taxonomy”, of sustainable activities; (2) a disclosure framework for non-financial and financial companies; and (3) investment tools, including benchmarks, standards and labels, which are discussed below in detail.

Since 2018, the EU Commission’s position with regard to what is needed to meet the sustainability goals has evolved, and the global context has changed. In July 2021, the EU Commission launched a new phase of the EU’s sustainable finance strategy,³ which identified four main areas where the EU Commission considers additional actions are needed for the financial system to support the transition of the economy towards sustainability. These are: (1) financing the transition of the real economy towards sustainability; (2) developing a more inclusive sustainable finance framework; (3) improving the financial sector’s resilience and contribution to sustainability (the “double materiality perspective”); and (4) fostering global ambition as global efforts are key to tackling the financial stability implications of climate and environmental risks.

Other notable developments include the EU Commission’s launch in December 2020 of the Green Deal,⁴ described as a “*new growth strategy. It will help us cut emissions while creating jobs*”.

In April 2021, the EU Commission reached a provisional agreement on the European Climate Law,⁵ which “*enshrines the EU’s commitment to reaching climate neutrality by 2050 and the intermediate target of reducing net greenhouse gas emissions by at least 55% by 2030, compared to 1990 level*”.

On 11 February 2022, the European Securities and Markets Authority (ESMA) published its sustainable finance roadmap for 2022–2024 (dated 10 February 2022),⁶ which identifies three priorities for its sustainable finance work: (1) tackling greenwashing and promoting transparency; (2) building national competent authorities’ and ESMA’s capacities in the sustainable finance field; and (3) monitoring, assessing and analysing ESG markets and risks. These priorities are likely to drive the ESG agenda in the financial services sector in Europe for the immediate future.

But What Does This Mean in Practice?

The focus of recent years has been to integrate (i) ESG considerations into the investment decision-making processes of EU-based investment managers and investors, and (ii) ESG factors into the non-financial data that is tracked and reported on by European businesses. The most significant measures adopted to date are the following building blocks:

- The Taxonomy Regulation,⁷ which entered into force on 12 July 2020, which essentially created a classification system for sustainable economic activities, and the majority of its operative provisions took effect on 1 January 2022. This regulation establishes the concept of a “taxonomy-aligned investment”, which, in essence, is an investment that contributes substantially to certain specified environmental objectives, does not significantly harm those objectives, and complies with certain minimum safeguards and technical asset-level screening criteria.
- The Sustainable Finance Disclosure Regulation (**SFDR**)⁸ came into effect on 10 March 2021, and was subsequently amended by the Taxonomy Regulation. It seeks to provide for (i) a harmonised understanding of what constitutes “sustainable investment”,⁹ and (ii) a uniform, mandatory set of disclosure and reporting obligations relating to sustainability issues in connection with investment activity, including in the offering documentation and annual accounts for investment products. The EU views the SFDR as a tool that will trigger changes in behavioural patterns in the financial sector, discouraging greenwashing and promoting investors to make sustainable investments.¹⁰ At a more granular level, it requires in-scope entities to radically change the way they act and how they assess and document their approach to sustainability. It also provides for the designation of green investment products, including dark-green or “Article 9” products, which pursue a sustainable investment objective, and light-green or “Article 8” products, which promote environmental and social characteristics, amongst others, provided that the companies in which they invest follow good governance. The SFDR is supplemented by regulatory technical standards (**RTS**)¹¹ that specify the content, methodologies and presentation of information to be provided pursuant to various provisions of the SFDR. The RTS have applied since 1 January 2023. The RTS were subsequently amended to, amongst other things, require financial market participants to disclose the extent to which their portfolios are exposed to gas and nuclear-related activities that comply with the Taxonomy Regulation, with the amendments taking effect on 20 February 2023.¹² Even though the RTS only came into force on 1 January 2023, they are already under review, with the European Supervisory Authorities (**ESAs**)¹³ issuing a consultation paper proposing amendments to certain specific aspects of the RTS.¹⁴ The consultation period closed on 4 July 2023 and the ESA’s Final Report detailing the outcome of the consultation and the ESA’s final recommendations is expected at the end of October 2023. In addition, on 14 September 2023, the EU Commission issued both public¹⁵ and targeted¹⁶ consultations on the implementation of SFDR, to gather information on certain potential shortcomings of SFDR related to legal certainty, the usability of SFDR and its ability to play its part in tackling greenwashing.
- The new Corporate Sustainability Reporting Directive (**CSRD**) entered into force on 5 January 2023, and Member States have until 6 July 2024 to implement its provisions

into national law. The rules will start to apply on a phased basis between 2024 and 2028, with “large public interest companies” (with over 500 employees) the first to come in scope of these requirements. The CSRD aims to ensure that companies report reliable, comparable and consistent sustainability information that investors and other stakeholders need in order to, for example, comply with the SFDR and the Taxonomy Regulation. The CSRD revises and strengthens rules introduced by the Non-Financial Reporting Directive,¹⁷ significantly expanding the scope of EU listed and established entities which are in scope of the reporting obligations. The intention is that the CSRD will increase transparency and the disclosure of sustainability information, making the comparison of different financial products easier.

The Taxonomy Regulation, SFDR and CSRD complement each other and cannot be viewed in isolation. While the obligations imposed by the Taxonomy Regulation are limited, the implications of its text are broad, as it establishes the vocabulary underlying the EU’s sustainable development agenda and, in this context, informs the content of the disclosure obligations under the SFDR. The CSRD is an important mechanism for ensuring that the data needed to report on the degree of sustainability under both SFDR and the Taxonomy Regulation is available.

Some other important measures introduced to make the financial sector even more sustainable include:

- The Climate Benchmarks Regulation,¹⁸ in force since 23 December 2020, which introduced two new types of benchmarks:
 - an EU Climate Transition Benchmark, with a “decarbonisation trajectory” evidenced by a measurable, science-based and time-bound movement towards alignment with the objectives of the Paris Agreement (e.g., the 2°C limit on global warming); and
 - an EU Paris-Aligned Benchmark, where the resulting reference portfolio’s carbon emissions are aligned with the objectives of the Paris Agreement (e.g., in essence, the carbon emission savings of each underlying asset exceed its carbon footprint).
- In August 2022, ESMA voiced support for the introduction of an EU ESG benchmark label,¹⁹ stating that ESG-labelled benchmarks should be subject to supervision in order to ensure that benchmark administrators comply with regulatory requirements. This may result in changes to the existing regulations.
- The EU Taxonomy Climate Delegated Act,²⁰ which classifies which activities best contribute to mitigating and adapting to the effects of climate change for the purpose of the Taxonomy Regulation, has applied since 1 January 2022. This Act has subsequently been amended the Amending Taxonomy Climate Delegated Act.²¹
- The Environmental Delegated Act which sets out the other environmental objectives set out in the Taxonomy Regulation, namely: the sustainable use and protection of water and marine resources; the transition to a circular economy; pollution prevention and control; and the protection and restoration of biodiversity and ecosystems. It will apply from 1 January 2024.²²
- The Complementary Climate Delegated Regulation (**CCD Regulation**),²³ which sets out the conditions under which nuclear and natural gas energy activities can be included in the list of economic activities covered by the Taxonomy Regulation (amending the EU Taxonomy Climate Delegated Act). The CCD Regulation also amends the EU Taxonomy Article 8 Delegated Regulation (see below) to require large listed non-financial and financial companies to disclose the proportion of their activities linked to

natural gas and nuclear energy. Its provisions applied from 1 January 2023.

- The EU Taxonomy Article 8 Delegated Regulation,²⁴ which specifies the content and presentation of information to be disclosed by non-financial undertakings, asset managers, credit institutions, investment firms, and insurance and reinsurance undertakings, as well as common rules relating to key performance indicators entered into force on 30 December 2021 and has applied since 1 January 2022, with a phased application. The Environmental Delegated Act also amends the EU Taxonomy Article 8 Delegated Regulation to ensure that the disclosure requirements under both pieces of legislation are consistent.
- Amendments to existing legislation (the Alternative Investment Fund Managers Directive (AIFMD),²⁵ the Undertakings for Collective Investment in Transferable Securities (UCITS) Directive²⁶ and the Markets in Financial Instruments Directive (MiFID)²⁷), which were implemented to:
 - ensure that sustainability factors and sustainability-related objectives are considered in the product oversight and governance process for products/instruments;
 - require the integration of sustainability factors, risks and preferences into certain organisational requirements and operating conditions for investment firms;
 - ensure sustainability risks and sustainability factors are taken into account by alternative investment fund managers and for UCITS; and
 - ensure a client's sustainability preferences are taken into account in managing their investments, providing investment advice or selling them an investment product.
- On 23 February 2022, the EU Commission adopted a proposal for a Directive on corporate sustainability due diligence (CSDDD),²⁸ to establish a legal framework which would require companies operating in the EU which meet certain prescribed thresholds or carrying out a certain amount of business in the EU to incorporate mandatory human rights and environmental due diligence into their core business activities. In-scope entities will also need to identify actual or potential adverse impacts arising from their own operations, those of any subsidiaries and from established business relationships in value chains. The CSDDD is currently making its way through the EU legislative process and final agreement on the rules is expected in Q4 2023/Q1 2024.
- In June 2023, the EU Commission adopted a legislative proposal²⁹ for a Regulation on the transparency and integrity of ESG rating activities which will introduce a regulatory framework governing the activities of ESG rating providers operating in the EU. The regulation proposes, amongst other things, that EU ESG rating providers must apply for authorisation from ESMA, meet certain organisational requirements (for example, general principles concerning their governance and their approach to rating methodologies and maintaining robust procedures regarding their oversight function) and would be expected to have robust conflicts of interest arrangements in place.

While the entities in scope of the various Regulations and Directives are essentially financial firms active in the EU or the EU entities in which they invest, the impact is being felt much more broadly, not only because financial firms are frequently global or operate across borders into the EU, but also because the EU has moved first to define regulatory parameters in a space that is of growing global importance and relates to issues such as global warming, which does not obey national boundaries.

UK

Although a great deal of existing EU legislation was “on-shored” into the UK statute book following the UK’s exit from the EU on 31 January 2020, this approach was not extended to any EU legislation taking effect after this time. In the context of ESG, this means the Taxonomy Regulation, the SFDR and the CSRD, as well as the amendments to existing legislation (i.e., the AIFMD, UCITS Directive and MiFID) are not part of UK law – regulating sustainable finance is an area where the UK and EU are following divergent paths.

Although it is not taking the same direction of travel as the EU, the UK government has repeatedly stated its commitment to fighting climate change. The UK Chancellor stated that the government’s economic policy objective “*remains to achieve strong, sustainable and balanced growth*”³⁰ and that the UK government aims to deliver a “*financial system which supports and enables a net zero economy by mobilising private finance towards sustainable and resilient growth and is resilient to the physical and transition risks that climate change presents*”.³¹

More specifically, the UK government endorsed the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD)³² in 2017 and made implementation of the TCFD proposals a central part of its 2019 Green Finance Strategy,³³ the principal objective of the strategy being to “*align private sector financial flows with clean, environmentally sustainable and resilient growth, supported by Government action*”. In promoting the TCFD’s recommendations, the UK Taskforce (described below) aims not only to improve the flow of information, but also to foster a step change in how organisations think about climate-related risks and opportunities.

On 30 March 2023, the UK government published an updated Green Finance Strategy³⁴ and a consultation on a future regulatory regime for ESG ratings providers,³⁵ with the aim of improving transparency and promoting good conduct in the ESG ratings market. The consultation closed to comment on 30 June 2023 and responses will inform the UK government’s next steps in this area.

In November 2020, a UK government and regulator-led taskforce – including the two principal financial regulators, the Financial Conduct Authority (FCA) and the Prudential Regulatory Authority (together, the **UK Taskforce**) – published an Interim Report³⁶ and Roadmap³⁷ setting out a strategy towards mandatory TCFD-aligned disclosures across the UK by 2025 and an indicative path for the introduction of regulatory rules and legislative requirements over the next five years, with most to be implemented in the first three years. The UK Taskforce recognises the global nature of the asset management industry and its interactions with related international initiatives, including those that derive from the EU’s Sustainable Finance Action Plan. Most encouragingly, the Interim Report stated that the proposed TCFD-aligned requirements would, as far as possible, be consistent with, and complementary to, these initiatives.

The FCA has developed its own ESG strategy³⁸ which sets out its target outcomes and the actions it expects to take in order to deliver these. The FCA states that “*ESG matters are high on the regulatory agenda*” and that its aim is to support the financial sector in driving positive change, including the transition to net zero. The FCA’s work is based on five core themes:

- Transparency – promoting transparency on climate change and wider sustainability along the value chain.
- Trust – building trust and integrity in ESG-labelled instruments, products and the supporting ecosystem.
- Tools – working with others to enhance industry capabilities and support firms’ management of climate-related and wider sustainability risks, opportunities and impacts.

- Transition – supporting the role of finance in delivering a market-led transition to a more sustainable economy.
- Team – developing strategies, organisational structures, resources and tools to support the integration of ESG into FCA activities.

The FCA has undertaken a programme of work to deliver the outcomes it has set out in its business plan for 2021/2022 and in its ESG strategy, some of which are discussed below.

New disclosure rules for companies with a UK premium listing were finalised in December 2020 and since 1 January 2022, the application of the TCFD-aligned Listing Rule for premium-listed commercial companies has been extended to include issuers of standard-listed equity shares.

The FCA has also introduced climate-related disclosure requirements, aligned with the TCFD's recommendations, for asset managers, life insurers, and FCA-regulated pension providers. The disclosures are: (i) "entity-level disclosures", meaning firms are required to publish annually an entity-level TCFD report on how they take climate-related risks and opportunities into account in managing or administering investments on behalf of clients and consumers, with these disclosures being made in a prominent place on the main website for the firm's business, and covering the entity-level approach to all assets managed by the UK firm; and (ii) "product or portfolio-level disclosures", meaning firms are required annually to produce a baseline set of consistent, comparable disclosures in respect of their products and portfolios, including a core set of metrics.

These new disclosure rules have applied to in scope UK asset managers with assets under management (AUM) of £50 billion or more since 1 January 2022 and from 1 January 2023 for firms with an AUM between £5 billion and £50 billion. Firms with an AUM less than £5 billion are exempt from the reporting regime. The publication deadline for the first entity and product-level disclosures was 30 June 2023 for firms with AUM above £50 billion and will be 30 June 2024 for smaller firms above the £5 billion exemption threshold. The reports issued on 30 June 2024 will cover data for the period 1 January to 31 December 2023. The FCA's rules and guidance are set out within the ESG Sourcebook of the FCA Handbook, which will be expanded to cover additional sustainability topics over time.

In November 2021, the FCA issued a discussion paper on sustainability disclosure requirements (SDR) and investment labels (DP 21/4) and, in October 2022, published a Consultation Paper on Sustainability Disclosure Requirements and investment labels (CP 22/20).³⁹ CP 22/20 sets out the FCA's proposed sustainability-related disclosure rules for UK-domiciled funds and portfolio mandates and the UK-based investment firms managing those products. The proposed regime does not apply to investment managers which are not FCA regulated, nor does it apply to non-UK funds, although the FCA has stated that it intends to follow up with a separate consultation on how the proposals in CP 22/20 may be applied in respect of non-UK funds.

The proposals in CP 22/20 cover: (i) sustainable labels for investment products; (ii) consumer facing disclosure requirements; (iii) detailed disclosures targeted at a wider audience (institutional investors and consumers seeking additional information); (iv) naming and marketing rules; (v) requirements for distributors (such as investment platforms); and (vi) a general anti-greenwashing rule. The FCA originally intended publishing final rules by the end of the first half of 2023, with the proposed labelling, naming and marketing and initial disclosure requirements coming into force in June 2024 (i.e. one year after publication of the final rules), but with the proposed anti-greenwashing rule coming into force with immediate effect on the date of the publication of the Policy Statement. However, on 29 March 2023, the FCA announced that, due to the significant number of responses it had received to CP 22/20, it intended to delay publishing the Policy Statement outlining the

final rules in Q3 2023 and push back the date of application.⁴⁰ In July 2023, the UK government announced in its Regulatory Initiatives Grid that publication of the Policy Statement would be further delayed to Q4 2023.⁴¹ To date, the UK has predominantly focused on climate change, rather than the broader ESG concerns that are the focus of the EU regulators and legislators, although the FCA has stated that it will "leverage the extensive work we have already done recently, and over the years, on governance, diversity, culture and purpose" and that it is "working actively with our international partners to develop robust and commonly agreed international standards on ESG that can serve global markets effectively".

In summary, both the EU and UK legislative and regulatory bodies continue to focus on ESG. However, their divergent approaches mean that it will become increasingly complex to navigate the overlapping but distinct legal and regulatory requirements as they evolve.

Hong Kong

Hong Kong's regulatory framework with regard to climate change and sustainable investment has gradually taken shape in recent years. Although the Climate Action Plan 2030+ published by the Hong Kong Environmental Bureau in January 2017 originally centred on green finance, the Hong Kong Securities and Futures Commission (SFC) and Hong Kong Exchanges and Clearing Limited (HKEX) have taken cues from international bodies and Mainland China to develop a regulatory agenda that goes beyond this initial focus.

There are three key drivers underlying Hong Kong's regulatory agenda with respect to sustainable investment: (i) Mainland China's status as a signatory to the Paris Agreement, the provisions of which apply to Hong Kong; (ii) the conviction of key regulators (including the SFC and HKEX) that climate change is a real threat and a source of financial risk to investors; and (iii) Hong Kong's position as an international financial centre, which necessitates proactive engagement with financial participants on climate risk-related issues.

In light of these drivers, the SFC's and HKEX's efforts have been directed at: (1) disclosure of listed companies' environmental information and climate-related risks; (2) integration by asset managers of climate change factors into their investment and risk management processes; and (3) ensuring accurate product disclosure of green investments, consistent with international standards, and avoiding greenwashing.

So far, similar to the regulations in the EU, the rules continue to develop and evolve. At the time of writing, the following are the key measures that have been taken:

- the Hong Kong Stock Exchange published guidelines on mandatory reporting on ESG,⁴² which came into effect on 1 July 2020 and replaced the voluntary ESG reporting regime that was first introduced in 2012. The guidelines largely emphasise climate-related disclosure, aligning with recommendations of the TCFD;
- the SFC released a circular to management companies of SFC-authorized unit trusts and mutual funds on "green" or "ESG" funds on 11 April 2019,⁴³ which was subsequently amended on 29 June 2021.⁴⁴ The circular sets out the SFC's expectations on the "product-level" disclosure obligations of SFC-authorized funds that incorporate ESG factors as their key investment focus with the goal of improving their comparability, transparency and visibility. To accompany the circular, the SFC also set up a dedicated website to list all SFC-authorized funds that categorised themselves as ESG funds; and
- on 20 August 2022, the Fund Manager Code of Conduct was revised to incorporate SFC requirements on Management and Disclosure of Climate-related Risks

by Fund Managers,⁴⁵ which sets out amendments to the existing SFC Fund Manager Code of Conduct. The document establishes high-level principles setting out the governance, investment management, risk management and disclosure obligations of fund managers with respect to climate risks. The requirements largely reference the recommendations of the TCFD – and notably allow for a two-tier approach (i.e., with baseline requirements for all fund managers and enhanced standards for fund managers with AUM exceeding a threshold of HK\$8 billion).

In late 2022, the SFC noted that it has largely achieved the objectives set out in the 2018 Strategic Framework, and moving forward will focus on: (i) enhancing corporate disclosure standards, potentially embedding those of ISSB; (ii) monitoring the implementation of and enhancing existing climate risk-related measures; and (iii) developing a regulatory framework for carbon markets.

Singapore

Singapore is actively harnessing finance as a force for good to transform economies, infrastructure and societies towards a greener, net-zero world. At the heart of this, Singapore's political leadership has emphasised Singapore's commitment to combatting climate change at an accelerated pace.⁴⁶ Looking beyond its own “net zero by 2050” plans, Singapore aims to play a broader role in the climate change agenda by establishing itself as the premier financial hub for green and sustainable finance in Asia, so as to catalyse Asia's net-zero transition and decarbonisation efforts.⁴⁷

Fundamental to fulfilling Singapore's vision is the “Finance for Net Zero Action Plan” (**FiNZ Action Plan**), launched by the Monetary Authority of Singapore (**MAS**) in April 2023. A summary of these strategic outcomes is set out below:⁴⁸

- **Climate Data & Disclosures:** The MAS has focussed its regulatory agenda on promoting consistent, comparable and reliable climate data and disclosures, so as to safeguard against greenwashing risks.
 - In January 2023, MAS' circular on the disclosure and reporting guidelines for retail funds came into effect. All retail ESG funds must now disclose their ESG investment objectives, approaches, criteria and metrics in their offering documents. Additionally, such funds must periodically disclose their ESG-related investments and how their ESG objectives have been met.
 - The Green Finance Industry Taskforce convened by the MAS is developing a Singapore-Asia Taxonomy (**Taxonomy**) for Singapore-based financial institutions, which will be among the first globally to adopt a “traffic light” system that classifies activities as either green or transitioning based on science-based criteria and thresholds.⁴⁹ The final Taxonomy is expected to be published by the end of 2023.⁵⁰
 - The MAS is working on a roadmap for key financial institutions and SGX-listed companies to align climate disclosures to standards that are being developed by the International Sustainability Standards Board.⁵¹
 - The MAS has piloted ESGenome, a sustainability reporting platform which went “live” in September 2022. This allows Singapore-listed companies to standardise their ESG reporting against a set of baseline metrics, and for their input to be automatically mapped to ESG standards and frameworks across major jurisdictions. The intent is to lower the cost of collecting and reporting climate data and improve access to such data across institutions and jurisdictions.

- As financial market participants are increasingly integrating ESG data into their investment strategies and risk management, the use of ESG ratings and data products has grown. The MAS has implemented a voluntary code of conduct to establish baseline industry standards on governance, transparency and management of conflicts of interest on the use of ESG ratings and data, so as to protect against greenwashing risks.⁵²

- **Climate Resilient Financial Sector:** In December 2020, the MAS published the Guidelines on Environmental Risk Management for Asset Managers (**Guidelines**).⁵³ The Guidelines are largely aligned with the recommendations of the TCFD and cover the areas of: (i) governance and strategy; (ii) research and portfolio construction; (iii) risk management; and (iv) stewardship and disclosure. The Guidelines have since been supplemented by information papers in May 2022 that highlight certain good and bad practices in asset management, as well as areas where further work is required, which serves as a reference point for asset managers when managing environmental risk.
- **Credible Transition Plans:** The MAS announced in June 2023 that it intends to set certain supervisory guidance to financial institutions with respect to their transition planning process, covering the financial institutions' governance frameworks and client engagement processes to manage climate-related financial risks and support transition in the real economy.⁵⁴
- **Green & Transition Solutions & Markets:** The MAS is also actively promoting green and transition financing solutions and markets. This includes certain government grants to enhance the Sustainable Bond Grant Scheme and Sustainable Loan Grant Scheme, so as to offset the expenses incurred for external review of sustainable debt instruments such as green, social, sustainability, sustainability-linked as well as transition loans and bonds. This has helped to spur significant growth in sustainable debt issuance out of Singapore.⁵⁵

In summary, Singapore has made significant strides in the ESG space so as to position itself as a hub for green finance and ESG investing in Asia. Singapore continues to monitor the latest ESG trends and initiatives globally to strengthen its own sustainable investment regulatory framework, and has actively fostered international cooperation in the ESG space to drive cross-border green and transition financing flows.⁵⁶

US

At the federal level, the US has lagged behind many other jurisdictions, including the EU and UK, in adopting legislation or regulations relating to ESG and sustainable finance. The US Securities and Exchange Commission (**SEC**), under Chair Gary Gensler, has proposed a set of rules that would establish uniform climate risk disclosure standards for public reporting companies and impose ESG disclosure requirements on certain investment funds and certain US investment managers. As of the date of this publication, however, these rules have not yet been adopted. These proposals, if adopted, could significantly expand both the nature and comparability of ESG and climate risk disclosure available to financial market participants and investors. The SEC has, however, recently adopted rule amendments which standardise fund-naming conventions and require funds that include terms in their names indicating that their investment decisions incorporate one or more ESG factors (such as “socially responsible investing” or “green”) to invest a minimum percentage of their assets in companies with the particular characteristics suggested by their names. Funds will generally be required to comply with these new requirements in late-2025.

There has been far more activity at the state level within the US. Some state governments are attempting to prohibit the investment of state funds (including state pension funds) with managers or funds that boycott certain industries, such as fossil fuels and firearms, while other states will choose to only invest in managers that limit their exposure to, for example, fossil fuels. Moreover, as discussed above, “red state” attorneys general and other US government officials have been increasingly critically scrutinising ESG-related investment activities. These state officials have questioned the use of ESG factors on several fronts, including whether ESG practices represent a conflict of interest and a breach of fiduciary duties. State officials have also questioned whether there are antitrust concerns arising from commitments to, for example, develop investment practices addressing climate change and the de-carbonisation goals of the Paris Agreement.

Climate change reporting proposal

On 21 March 2022, the SEC proposed rules for the enhancement and standardisation of climate-related disclosures for public reporting companies (**Climate Change Proposal**).⁵⁷ The Climate Change Proposal would require new climate-related disclosures in a registrant’s registration statements and annual reports, in a separately captioned “Climate-Related Disclosure” section, and in the notes to financial statements. The proposed rules would mandate the disclosures summarised below:

- *Board and management oversight* – The proposed rules would require a registrant to disclose, as applicable, certain information regarding the board’s oversight of climate-related risks, and management’s role in assessing and managing those risks.
- *Climate-related risks* – The proposed rules would require disclosure of climate-related risks that have had or are likely to have a material impact on a registrant’s business and consolidated financial statements, which may manifest over the short, medium or long term.
- *Climate-related impacts on the business* – Having disclosed the material climate-related risks to the business, a registrant would be required to describe the actual and potential impact of those risks on its strategy, business model and outlook.
- *Risk management* – Registrants would be required to disclose their internal processes for managing climate-related risks, including how the registrant:
 - assesses the significance of climate-related risks in comparison to other risks or regulatory requirements, such as greenhouse gas (GHG) emissions limits;
 - considers changes in customer or counterparty preferences, technological changes, or changes in market prices in assessing transition risks;
 - decides whether to accept, mitigate, or adapt to a certain risk; and
 - prioritises climate-related risks and mitigates high-priority climate-related risks.
- *Transition plans* – If the registrant has adopted a transition plan in the context of its climate-related risk management, it must describe the plan along with the relevant metrics and targets used to identify physical and transition risks (e.g., reduction of GHG emissions, mitigation of risk related to extreme weather events, adaptation to the imposition of a carbon price, or adaptation to changing demands or preferences of consumers, investors, employees and business counterparties).
- *Carbon offsets or renewable energy credits (RECs)* – If, as part of its net emissions reduction strategy, a registrant uses

carbon offsets or RECs, the proposed rules would require it to disclose the role that carbon offsets or RECs play in the registrant’s climate-related business strategy.

- *Maintained internal carbon price* – Under the SEC’s proposed definition, an internal carbon price is an estimated cost of carbon emissions used internally within an organisation. If a registrant uses an internal carbon price, the proposed rules would require it to make various pricing disclosures, including the rationale for selecting the applied internal carbon price and how it uses its internal carbon price to evaluate and manage climate-related risks.
- *Scenario analysis* – A registrant must describe the resilience of its business strategy in light of potential future changes in climate-related risks.
- *GHG emissions* – A registrant must describe the resilience of its business strategy in light of potential future changes in climate-related risks.

If adopted in its current form, the Climate Change Proposal can be expected to impose significant disclosure burdens and related expenses on issuers, particularly those that do not yet have processes in place to gather the information necessary to provide the required disclosures. The Climate Change Proposal, which faces strong opposition from part of the industry, will likely face legal challenges if it is adopted.⁵⁸

SEC proposal to enhance ESG disclosures by certain investment advisers and investment companies

On 25 May 2022, the SEC proposed a framework requiring US-registered investment companies and business development companies and certain US-registered investment advisers to disclose their ESG investment practices (the **Proposal**).⁵⁹ The Proposal comes in the wake of substantial scrutiny of disclosure practices involving ESG investment practices by the SEC and its staff. The Proposal is intended to promote “consistent, comparable, and reliable” information to investors and to facilitate informed decision-making related to ESG investment products and strategy offerings.

In particular, the Proposal would seek to change existing disclosure practices by (among other provisions): expressly requiring ESG-related disclosures in fund prospectuses and annual reports and investment adviser regulatory filings (where funds and strategies use ESG investment techniques); implementing a standardised approach for certain types of ESG funds to disclose their ESG investing processes; and, for the first time, requiring the disclosure of GHG emissions data in certain circumstances.⁶⁰

The Proposal would require funds that consider ESG factors in their investment process to disclose additional information regarding their investment strategies in registration statements and in the “management discussion of fund performance” section of annual reports. The disclosure requirements would vary depending upon whether a fund is categorised as an “integration fund”, “ESG-focused fund” or “impact fund”.

Integration Funds

An integration fund would be defined as a fund that considers one or more ESG factors alongside other, non-ESG factors in its investment decisions, but those ESG factors are generally no more significant than other factors in the investment selection process, such that ESG factors may not be determinative in deciding to include or exclude any particular investment in the fund’s portfolio. If ESG factors are part of the integration fund’s principal investment strategy, the fund would be required to include disclosure in the summary prospectus as to how the fund incorporates ESG factors into the investment selection process, including what factors are considered.

All integration funds would be required to describe how the fund incorporates ESG factors into the investment selection process, including: the ESG factors considered and whether the fund considers the GHG emissions of its portfolio investments; and how the fund considers such information (including the methodology the fund uses) in the fund's statutory prospectus.

ESG-Focused Fund and Impact Funds

An ESG-focused fund would be defined as a fund that focuses on one or more ESG factors by using them as a significant or main consideration in selecting investments or in its engagement strategy with the companies in which it invests. This includes any fund whose name includes terms indicating that the fund's investment decisions incorporate one or more ESG factors, and any fund whose sales literature or advertisements indicate that the fund's investment decisions incorporate one or more ESG factors by using them as a significant or main consideration in selecting investments. The ESG Release indicates that it would also capture funds that track an ESG-focused index and funds that apply inclusionary or exclusionary screen based on ESG factors.

Impact funds would be a sub-set of ESG-focused funds and would be defined as ESG-focused funds that seek to achieve specific ESG impact(s). ESG-focused funds and impact funds would be required to disclose information in the summary prospectus in tabular format related to three broad categories: Overview of the Fund's Strategy; How the Fund Incorporates ESG Factors in its Investment Decisions (specific requirements apply with respect to impact funds); and How the Fund Votes Proxies and/or Engages with Companies about ESG Issues.

ESG-focused funds and impact funds would also need to describe in the statutory prospectus how the fund incorporates ESG factors into its investment process, including information related to: the index methodology for any index tracked; internal methodologies used and how they incorporate ESG factors; scoring or ratings systems of any third-party data provider used; factors applied in any inclusionary or exclusionary screen; description of any third-party frameworks followed and how they are used; and, with respect to engagement, a description of any specific engagement objectives and associated key performance indicators.

ESG-focused funds would need to disclose in their annual reports, to the extent applicable based on certain responses to Form N-CEN (primarily whether proxy voting or engagement is a "significant means" of implementing its ESG strategy), information related to: the percentage of ESG proxy voting matters where the fund voted in favour of the initiative; the fund's progress on engagement strategies; and/or GHG emissions data for portfolio investments (carbon footprint and weighted average carbon intensity).

Both methodologies would require Scope 1 and Scope 2 emissions to be included in the emissions calculation but would not require Scope 3 emissions. The GHG emissions requirements would potentially leverage information available under the Climate Change Proposal, to the extent that proposal is adopted.

The SEC also proposed to amend Form ADV Part 2A to require registered investment advisers that consider ESG factors as part of their advisory business to disclose information similar to that required in fund registration statements and annual reports. Specifically, the Proposal would require registered advisers to provide: a description of the ESG factors considered in providing advisory services and how they are incorporated and – if ESG factors are considered when selecting, reviewing or recommending portfolio managers – a description of the factors considered and how they are incorporated.

The Proposal also contains guidance related to fund and adviser compliance policies, as well as marketing materials, in the ESG context.

SEC rule amendments to prevent misleading or deceptive fund names related to ESG

Section 35(d) of the Investment Company Act of 1940 prohibits a US-registered investment company or business development company from adopting as part of its name or title any word or words that the SEC finds materially deceptive or misleading. The SEC adopted Rule 35d-1 (**Names Rule**) under Section 35(d) in 2001 to meet this objective. The Names Rule deems certain types of fund names to be materially deceptive or misleading for the purposes of Section 35(d) unless certain conditions are satisfied, such as the adoption of a policy to invest at least 80% of a fund's assets in the particular type of investment, industry, country or geographic region suggested by its name (**80% Investment Policy**).

On 20 September 2023, the SEC adopted amendments to the Names Rule (**Names Rule Amendments**). Among other things, the Names Rule Amendments expanded the scope of funds subject to the Names Rule by requiring a fund to adopt an 80% Investment Policy if its name suggests a focus "in investments that have, or whose issuers have, particular characteristics". The Names Rule Amendments identify terms indicating that a fund's investment decisions incorporate one or more ESG factor(s) as examples of names indicating a focus on investments or issuers having particular characteristics. For these purposes, the term "ESG" would include terms such as "socially responsible investing", "sustainable", "green", "ethical", "impact" or "good governance" to the extent they describe environmental, social and/or governance factors that may be considered when making an investment decision. Under the current rule, such names are generally considered by many fund managers to be investment strategies not subject to the 80% Investment Policy requirement. In expanding the scope of the Names Rule to capture funds that include terms in their names indicating that their investment decisions incorporate one or more ESG factors, the SEC was seeking to address potential investor confusion and "greenwashing" concerns.

Under the Names Rule Amendments, funds will retain some flexibility in defining the contours of their required 80% Investment Policies, ascribing definitions to the terms used in those policies, and determining (in many instances) what investments are appropriate to include in the 80% Investment Policy "basket". However, any investment focus-related terms used in a fund's name will be required to be defined "consistent with those terms' plain English meaning or established industry use".

The SEC also codified that compliance with a fund's 80% Investment Policy is not a safe harbour to the prohibitions on adopting a fund name that is materially deceptive or misleading under Section 35(d). For example, substantial investments made outside a fund's 80% Investment Policy that are "materially different" to the fund's investment focus could be deemed to be materially deceptive or misleading for purposes of Section 35(d), irrespective of whether the fund complies with its 80% Investment Policy.

The Names Rule Amendments become effective on 11 December 2023. However, the SEC adopted a fairly lengthy compliance period. For example, fund groups with net assets of \$1 billion or more will have 24 months to comply with the amendments (i.e., on or before 10 December 2025).

State-level anti-boycott legislation

Investment managers looking to market products that consider ESG factors across different state and national jurisdictions need to be cognisant of state laws in the US that prohibit or require the incorporation of ESG factors into the investment process.

A number of states have adopted legislation prohibiting forms of ESG investing. These “anti-ESG” rules generally fall into two categories: boycott bills and legislation prohibiting forms of ESG investing. The rapid adoption of these rules by Republican-dominated legislatures reflect an underlying concern that consideration of ESG factors unnecessarily favour political and social causes at the expense of shareholder return. Boycott bills aim to prevent state assets from being used to invest in, or do business with, financial institutions that boycott an ESG-targeted industry such as firearms, fossil fuels, and certain mining, agricultural, and timber practices. Rules prohibiting forms of ESG investing seek to prevent public entities such as agencies or state pension funds from considering ESG criteria when investing state assets. In contrast, states such as Illinois and Maryland have incorporated ESG and other non-pecuniary criteria in making investment decisions with regards to state funds. Additionally, states such as Connecticut and Maine have even taken the further step of divesting public dollars from being invested in the firearms or fossil fuel industries, respectively. Managers should be aware that EU-mandated disclosure requirements bring ESG investment activities to light that may run afoul of conflicting state laws in the US.

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Disclaimer

All of the above answers are up to date as at 27 November 2023.

Endnotes

1. Action Plan: Financing Sustainable Growth is available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0097&from=EN>
2. In summary, the 10 action points are: (1) establishing an EU classification system for sustainable activities; (2) creating standards and labels for green financial products (including an EU Green Bond Standard); (3) fostering investment in sustainable projects; (4) incorporating sustainability considerations when providing financial advice; (5) developing sustainable/low-carbon benchmarks; (6) better integrating sustainability in credit ratings and market research; (7) clarifying institutional investors’ and asset managers’ duties regarding sustainability; (8) incorporating sustainability in prudential requirements; (9) strengthening sustainability disclosure and accounting rulemaking; and (10) fostering sustainable corporate governance and reducing short-termism in capital markets.
3. The Strategy for Financing the Transition to a Sustainable Economy is available here: https://eur-lex.europa.eu/resource.html?uri=cellar:9f5e7e95-df06-11eb-895a-01aa75ed71a1.0001.02/DOC_1&format=PDF
4. “What is the Green Deal?” is available here: https://ec.europa.eu/commission/presscorner/detail/en/fs_19_6714 and a factsheet describing the architecture of the Green Deal is available here: https://ec.europa.eu/commission/presscorner/detail/en/fs_21_3671
5. The European Climate Law is available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32021R1119&from=EN>
6. ESMA’s sustainable finance roadmap for 2022–24 is available here: https://www.esma.europa.eu/sites/default/files/library/esma30-379-1051_sustainable_finance_roadmap.pdf
7. Regulation (EU) 2020/852, available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R0852&from=EN>
8. Regulation (EU) 2019/2088. The consolidated version, as amended by the Taxonomy Regulation, is available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:02019R2088-20200712&from=EN>
9. “[S]ustainable investment’ means an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance.”
10. The Factsheet to the April 2021 EU Sustainable Finance package is available here https://finance.ec.europa.eu/system/files/2021-04/sustainable-finance-communication-factsheet_en.pdf
11. Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022 supplementing Regulation (EU) 2019/2088 of the European Parliament and of the Council with regard to regulatory technical standards specifying the details of the content and presentation of the information in relation to the principle of “do no significant harm”, specifying the content, methodologies and presentation of information in relation to sustainability indicators and adverse sustainability impacts, and the content and presentation of the information in relation to the promotion of environmental or social characteristics and sustainable investment objectives in pre-contractual documents, on websites and in periodic reports, is available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32022R1288&from=EN>
12. <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32023R0363>
13. The collective term for ESMA, the European Insurance and Occupational Pensions Authority (EIOPA) and the European Central Bank (EBA).
14. https://www.esma.europa.eu/sites/default/files/2023-04/JC_2023_09_Joint_consultation_paper_on_review_of_SFDR_Delegated_Regulation.pdf
15. https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13961-Report-on-the-Sustainable-Finance-Disclosure-Regulation/public-consultation_en
16. https://finance.ec.europa.eu/regulation-and-supervision/consultations/finance-2023-sfdr-implementation_en
17. Directive 2014/95 EU.
18. Regulation (EU) 2019/2089, available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R2089&from=EN>
19. ESMA’s response to the EU Commission’s consultation on the BMR review included its views on climate benchmarks, and the response is available here: https://www.esma.europa.eu/sites/default/files/library/esma81-393-502_esma_response_to_the_ec_consultation_on_the_bmr_review_2022.pdf

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23. Commission Delegated Regulation (EU) 2022/1214 is available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32022R1214&from=EN>
24. Commission Delegated Regulation (EU) 2021/2178 is available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32021R2178&from=EN>
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26. Directive 2009/65/EC.
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29. <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52023PC0314>
30. Letter from the Chancellor to the FCA “Recommendations for the Financial Conduct Authority”, dated 23 March 2021, is available here: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/972445/CX_Letter_-_FCA_Remit_230321.pdf
31. *Ibid.*
32. The TCFD has over 1,000 supporters, which are headquartered in 55 countries, span the public and private sectors and include organisations such as corporations, national governments (Belgium, Canada, Chile, France, Japan, Sweden and the UK), government ministries, central banks, regulators, stock exchanges and credit rating agencies.
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34. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1149690/mobilising-green-investment-2023-green-finance-strategy.pdf
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37. The Roadmap is available here: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/933783/FINAL_TCFD_ROADMAP.pdf
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39. <https://www.fca.org.uk/publication/consultation/cp22-20.pdf>
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42. The ESG Reporting Guide is available here: <https://en-rules.hkex.com.hk/rulebook/environmental-social-and-governance-reporting-guide-0>
43. The SFC circular dated 11 April 2019 is available here: <https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=19EC18>
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45. https://www.sfc.hk/-/media/EN/assets/components/codes/files-current/web/codes/fund-manager-code-of-conduct/Fund-Manager-Code-of-Conduct_Eng_20082022.pdf?rev=9aac7a8541054823b7f4626749e56cf8
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53. <https://www.mas.gov.sg/regulation/guidelines/guidelines-on-environmental-risk-management-for-asset-managers>
54. <https://www.mas.gov.sg/news/media-releases/2023/mas-to-set-expectations-on-credible-transition-planning-by-financial-institutions>
55. It is estimated that Singapore accounts for more than half of the cumulative issuances of sustainable debt in Southeast Asia: <https://www.mas.gov.sg/news/speeches/2023/official-launch-of-sgfin#:~:text=Based%20on%20estimates%2C%20Singapore%20accounts,of%20sustainable%20debt%20was%20issued>
56. <https://www.mas.gov.sg/news/speeches/2023/official-launch-of-sgfin>
57. See The Enhancement and Standardization of Climate-Related Disclosures for Investors, Rel. Nos. 33-11042 & 34-94479 (21 March 2022).
58. See generally Biden’s Push to Disclose Climate Risks Hits Wall of Industry Resistance, Washington Post (May 2, 2023).
59. See Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices, Rel. Nos. IA-6034 & IC-34594 (25 May 2022).
60. In addition, the amendments would require the tagging of certain ESG disclosures using the Inline Extensible Business Reporting Language (Inline XBRL) structured data language. This would apply to funds that file registration statements on Forms N-1A, N-2 or S-6, annual shareholder reports on Form N-CSR and annual reports on Form 10-K.



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