



# SFDR and other key ESG regimes

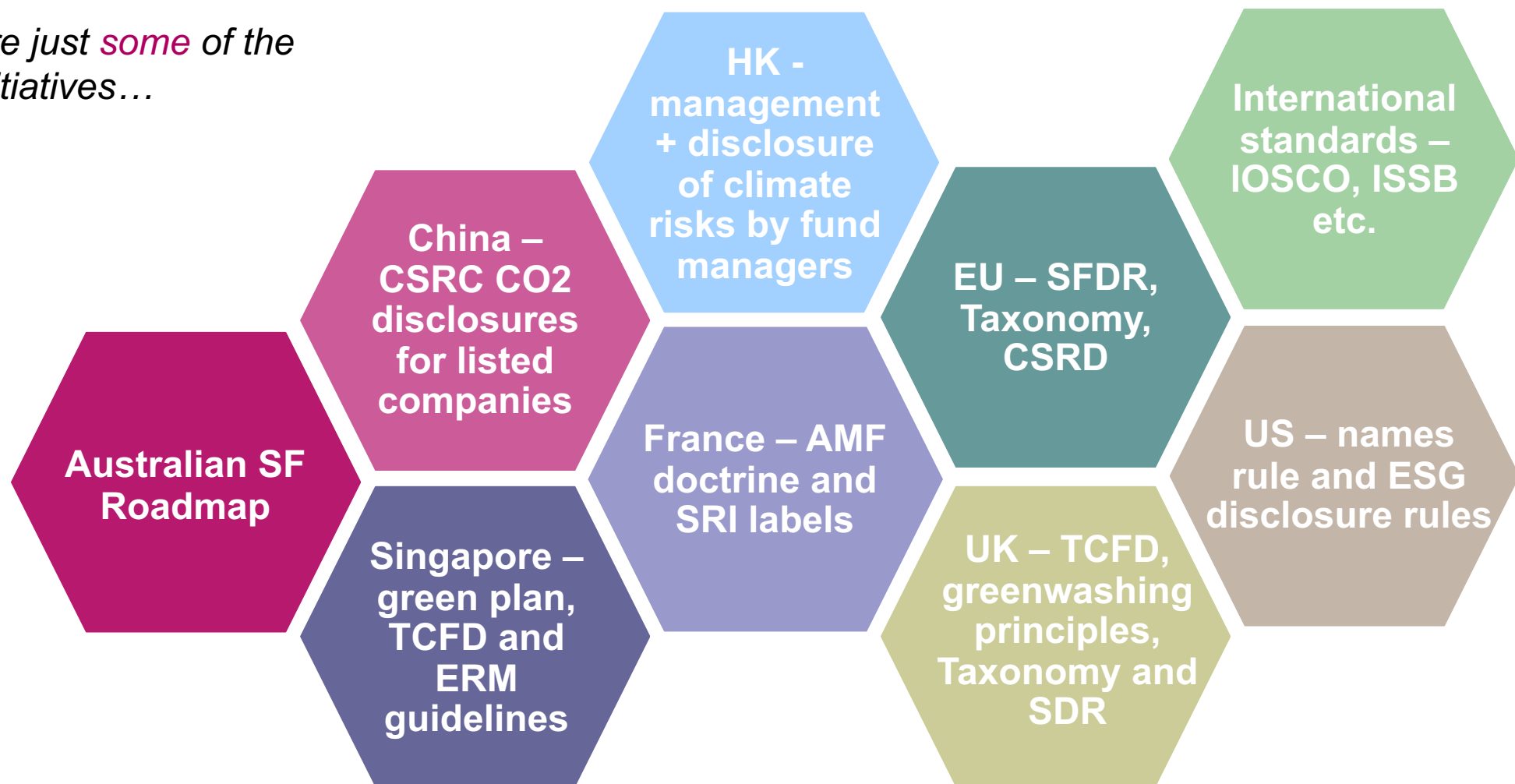
**Raza Naeem**, Partner -Linklaters LLP

**Mona Benisi**, Executive Director - Morgan Stanley Real Assets

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# Global ESG landscape

*These are just **some** of the global initiatives...*



# Three Common Themes

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**Identifying and  
managing ESG risks**



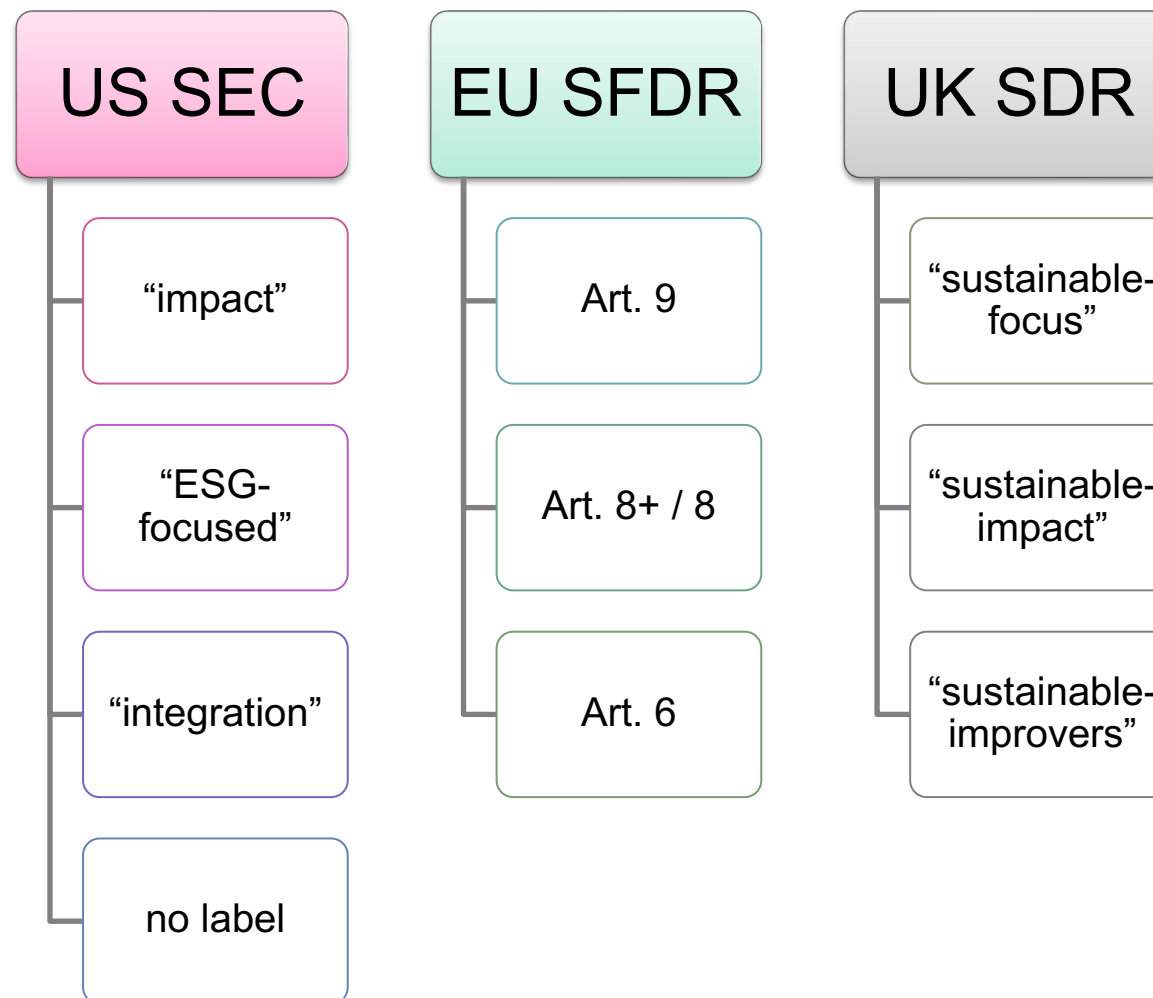
**Increased ESG disclosures  
to encourage firm  
accountability and direct  
investments towards  
greener products / firms**



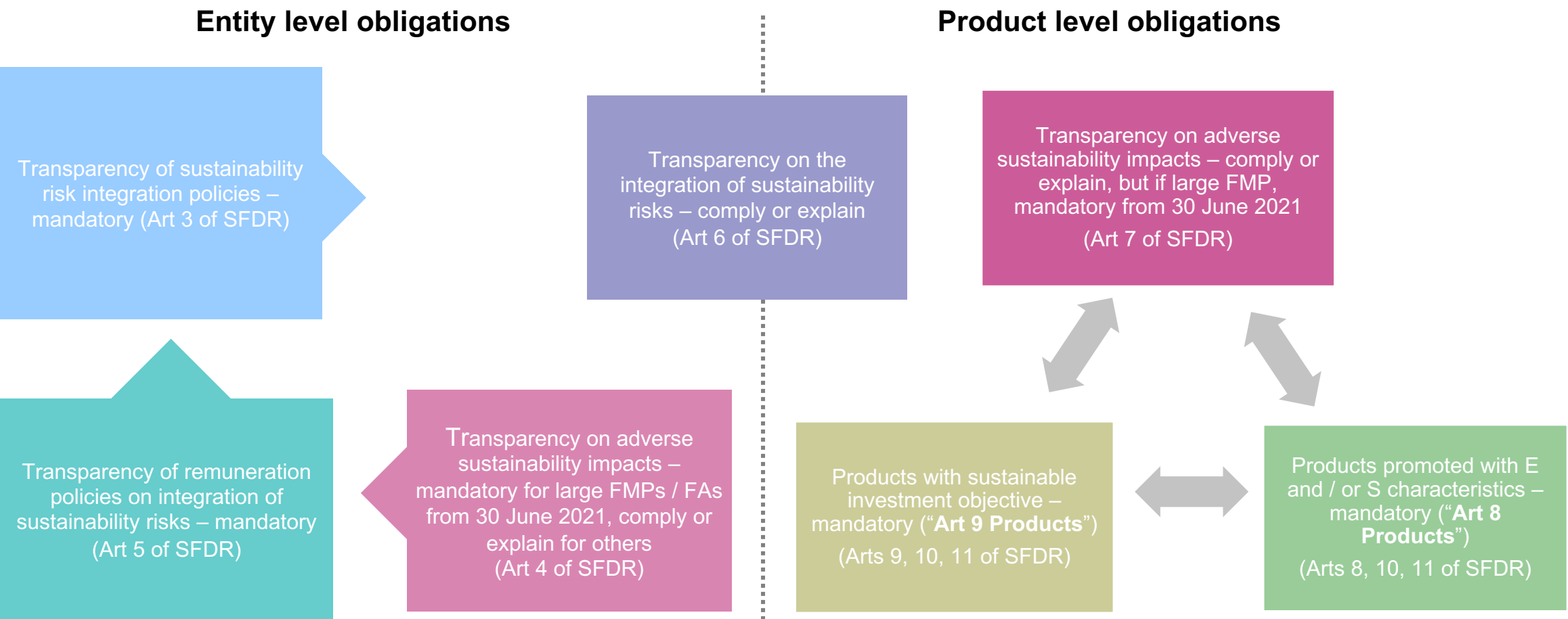
**Combatting  
Greenwashing**

# EU vs. UK vs. US Fund Classifications

- All rule sets offer a **choice** – with consequences - of extent to which disclosure obligations hit
- Double materiality?
- Scope?

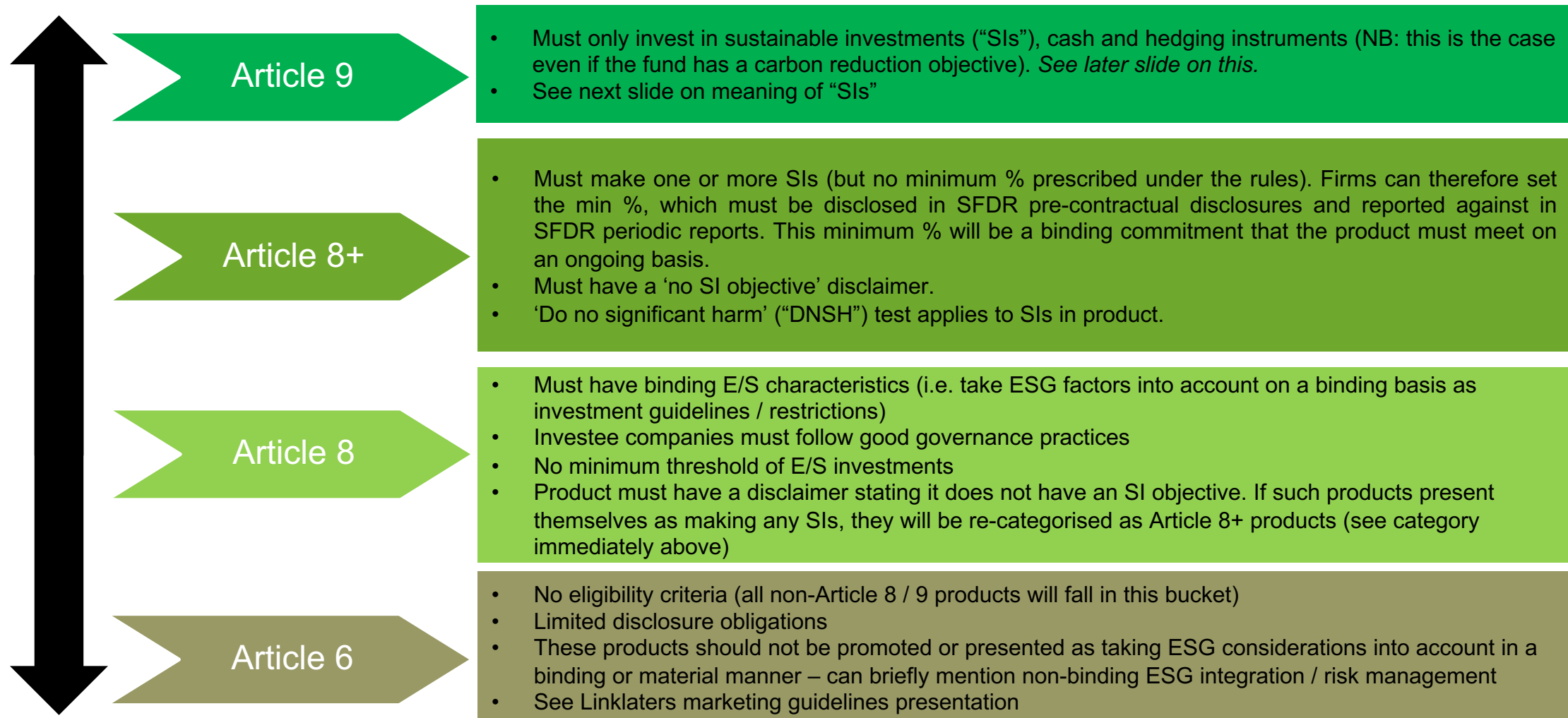


# EU SFDR – Overview



**Note:** SFDR applies to **Financial Market Participants** (mainly buy-side firms) and **Financial Advisers**

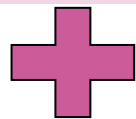
# EU SFDR: Categorisation of ‘Financial Products’



# SFDR: 3 building blocks for Sustainable Investments

## 1. Positive Measurable 'E' or 'S' contribution made by Investment

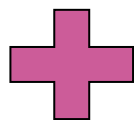
No definition or min proportion prescribed under rules and a variety of approaches could meet this limb - e.g. investee company is better than peers / benchmark on specific ESG metrics or has a 20% renewable business **BUT** we are expecting Q&A guidance now



## 2. Investment Does No Significant Harm (DNSH) to other E / S objectives

This must be assessed using:

- i. at least the mandatory PAI indicators in the SFDR RTS Annex (e.g. GHG emissions) by setting thresholds for significant harm that all investments must be screened against – these are effectively negative screens but with some potential to build in buffer for temporary blips;
- ii. minimum social safeguards i.e. OECD guidelines for multinationals and UN Guiding Principles on Business + Human Rights.

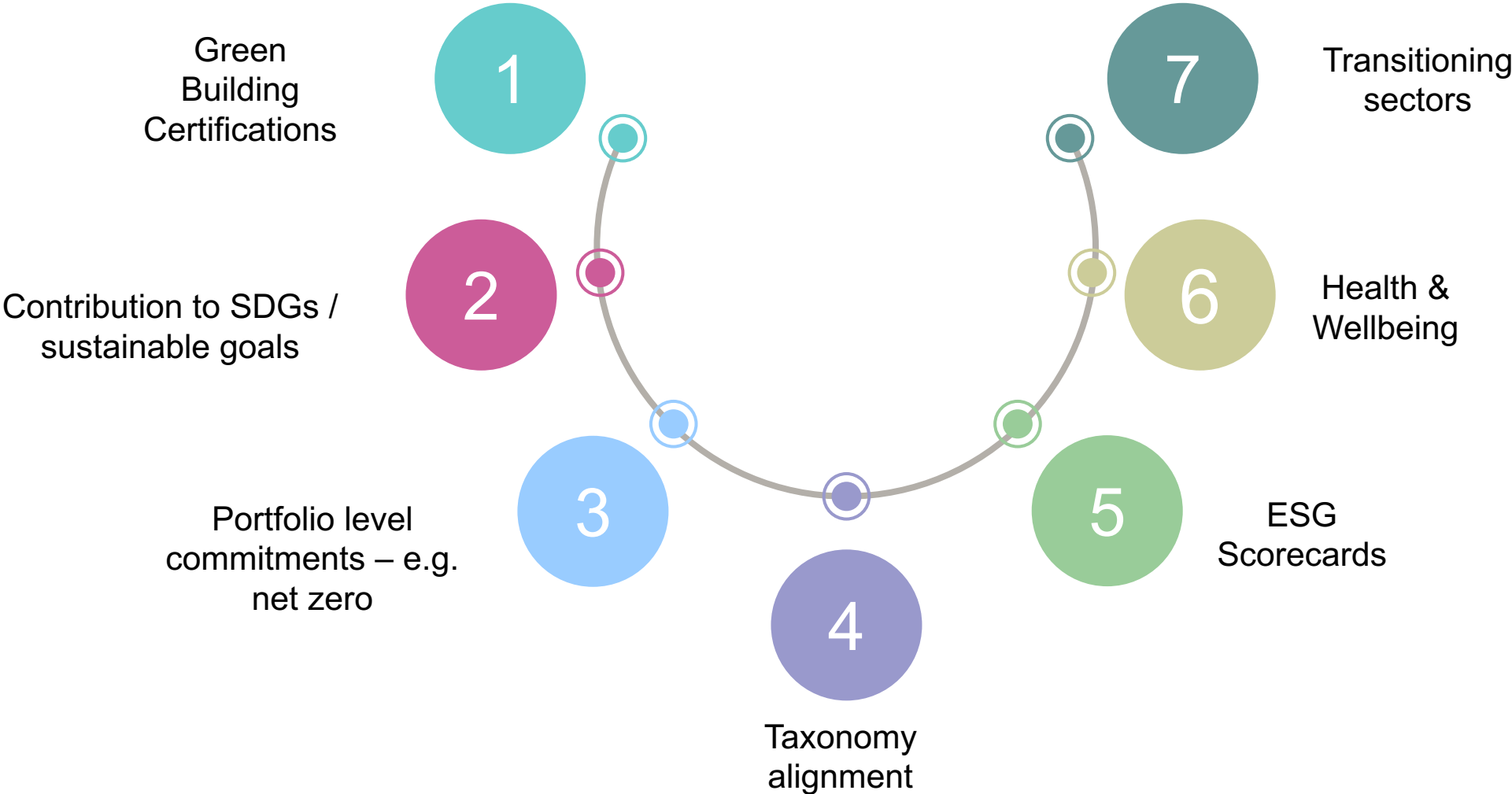


## 3. Good governance practices at investee company level

Qualitative assessment including consideration of sound management structures, employee relations, staff remuneration and tax compliance at least.

The latest Q&As from May 2022 confirmed that this requirement applies to all corporate investments within Article 9 products, and not to other types of investments (such as sovereign investments).

# EU SFDR – Examples of Article 8 characteristics





# EU Taxonomy Regulation – substantially contributing activities

To be environmentally sustainable, an **economic activity** must:

- > contribute substantially to **at least one of** six specified environmental objectives on the right (lifecycle approach);
- > comply with **qualitative and quantitative technical screening criteria**, for that activity developed in Level 2 rules

**AND**

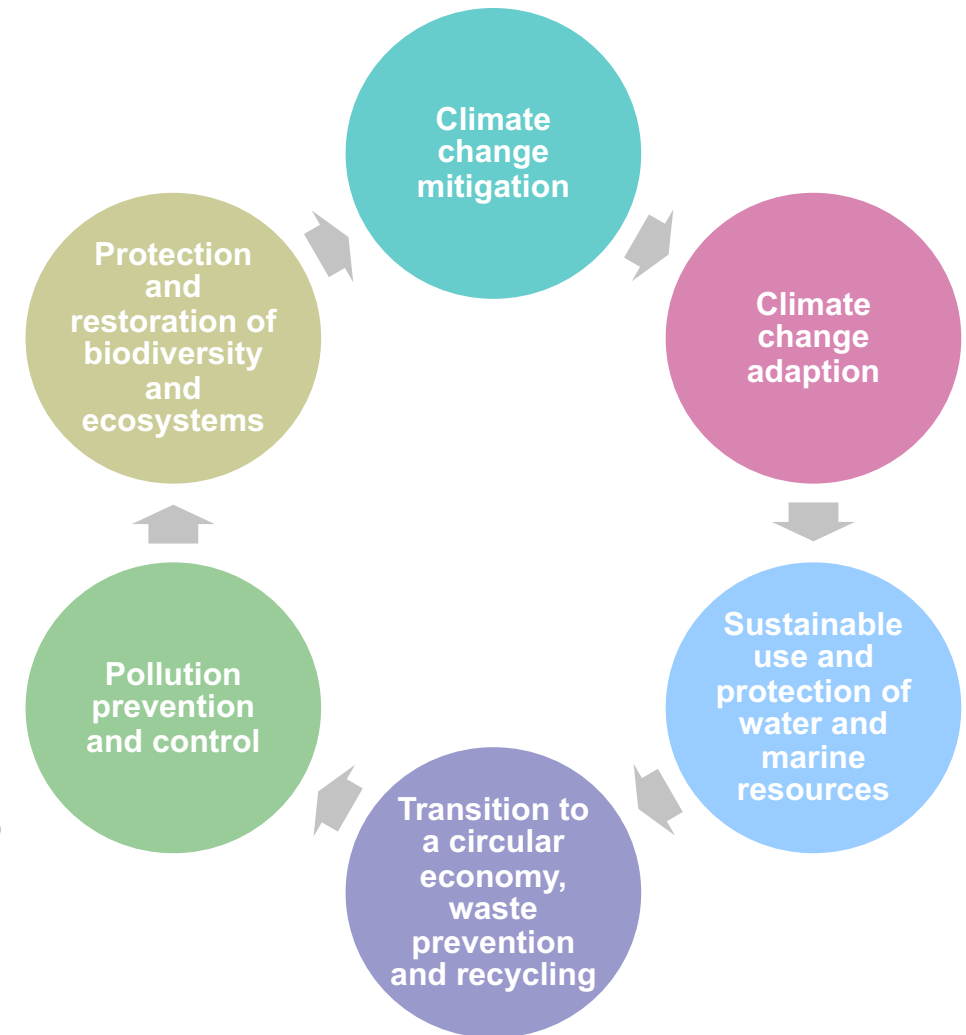
- > **not significantly harm any** of the (other) six environmental objectives;

**AND**

- > be carried out by the **economic** operator/investee company in compliance with certain **minimum social and governance safeguards**

**BUT** only TSCs for **climate change objectives** have been developed so far

**NOTE:** SFDR applies at an **investment level** (e.g. investee / portfolio company is assessed as a whole) but Taxonomy assessment looks through and considers the sustainability of specific **economic activities / business lines** of the company



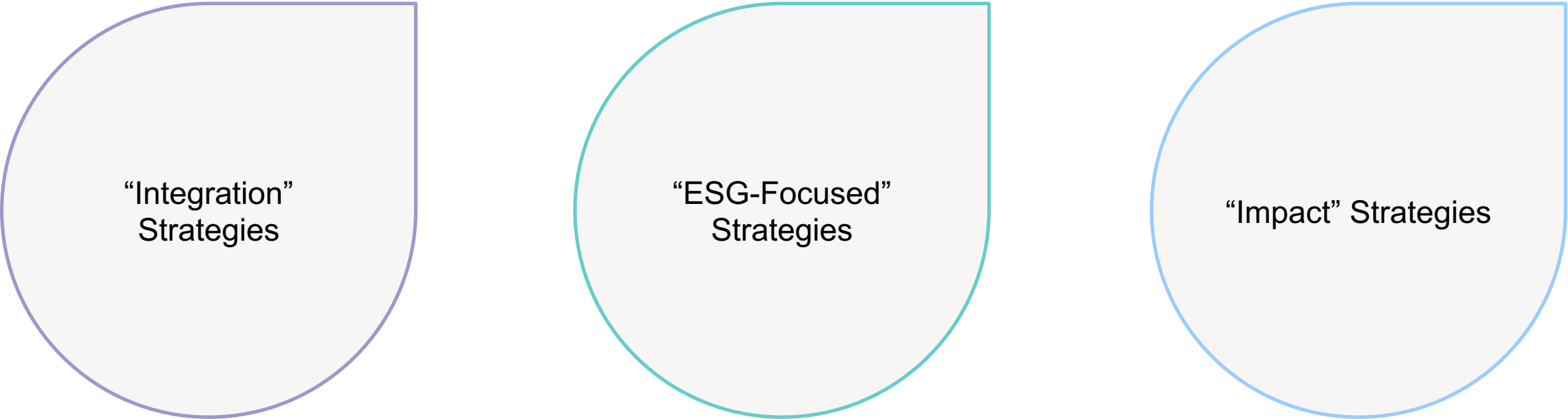
# UK SDR Regime: Proposed Categorisation

- > Labels only applicable for funds / portfolios sold to retail investors.
- > FCA are also proposing to restrict the use of sustainability-related terms in the naming and marketing of in-scope products that do not qualify for and use a sustainable investment label. For instance, such products will not be able to use sustainability-related terms including (but not limited to) ‘ESG’, ‘climate’, ‘impact’, sustainable’, ‘responsible’, ‘green’, ‘SDG’, ‘Paris-aligned’ or ‘net zero’.
- > Overseas funds not currently in scope – but UK distributors will need to impose disclosures and comply with general anti greenwashing rules.

FCA Product Label	Overview of Category	Proposed Eligibility Criteria
Sustainable – Impact	<p>Alongside financial risk / return objective, product must have an objective to achieve a pre-defined, positive and measurable environmental and/or social impact.</p> <p>The FCA expect this to be a narrow and highly selective category.</p>	<ul style="list-style-type: none"> <li>• No minimum proportion specified – but we expect firms will have to show predominant focus is on such assets (again approx. 70%).</li> <li>• Investments should be in projects and activities that offer solutions to environmental or social problems, often in underserved markets or to address observed market failures.</li> </ul>
Sustainable – focus	<p>Alongside financial risk / return objective, must have an objective to invest in assets that meet a credible standard of environmental and/or social sustainability, or that align with a specified environmental and/or social sustainability theme.</p> <p>The FCA expect this to be a narrow and highly selective category.</p>	<ul style="list-style-type: none"> <li>• At least 70% of the product must be invested in such assets to qualify.</li> <li>• A credible standard according to the FCA is one that is robust, independently assessed, evidence-based and transparent.</li> <li>• No longer linked to the UK Green Taxonomy – but the FCA have noted that the UK Taxonomy could be one way of demonstrating the credible standard of sustainability criteria.</li> </ul>
Sustainable – improvers	<p>Alongside financial risk / return objective, product must have an objective to deliver measurable improvements in the sustainability profile of its assets over time, including via investor stewardship.</p> <p>The FCA consider that this category will be more flexible compared to the other 2 categories, as it should accommodate a much broader range of investments, with stewardship playing a key role.</p>	<ul style="list-style-type: none"> <li>• No minimum proportion specified – but we expect firms will have to show predominant focus is on such assets (again approx. 70%).</li> <li>• The FCA expect stewardship will be the main channel to pursue sustainability aims / goals of the product – however the portfolio should be constructed with improvers in mind.</li> <li>• There should be clear KPIs, targets for improvements of the sustainability profile of products over time (this is key as this is what distinguishes the product from an ESG integration product) and disclosures on asset selection and stewardship activities, including when firms will escalate and potentially divest if stewardship is not attaining intended outcomes.</li> </ul>

# US SEC proposals: Fund Categories

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The diagram consists of three light gray rounded rectangular boxes arranged horizontally. Each box has a colored border: purple for the first, teal for the second, and blue for the third. Each box contains text describing a fund category.

“Integration”  
Strategies

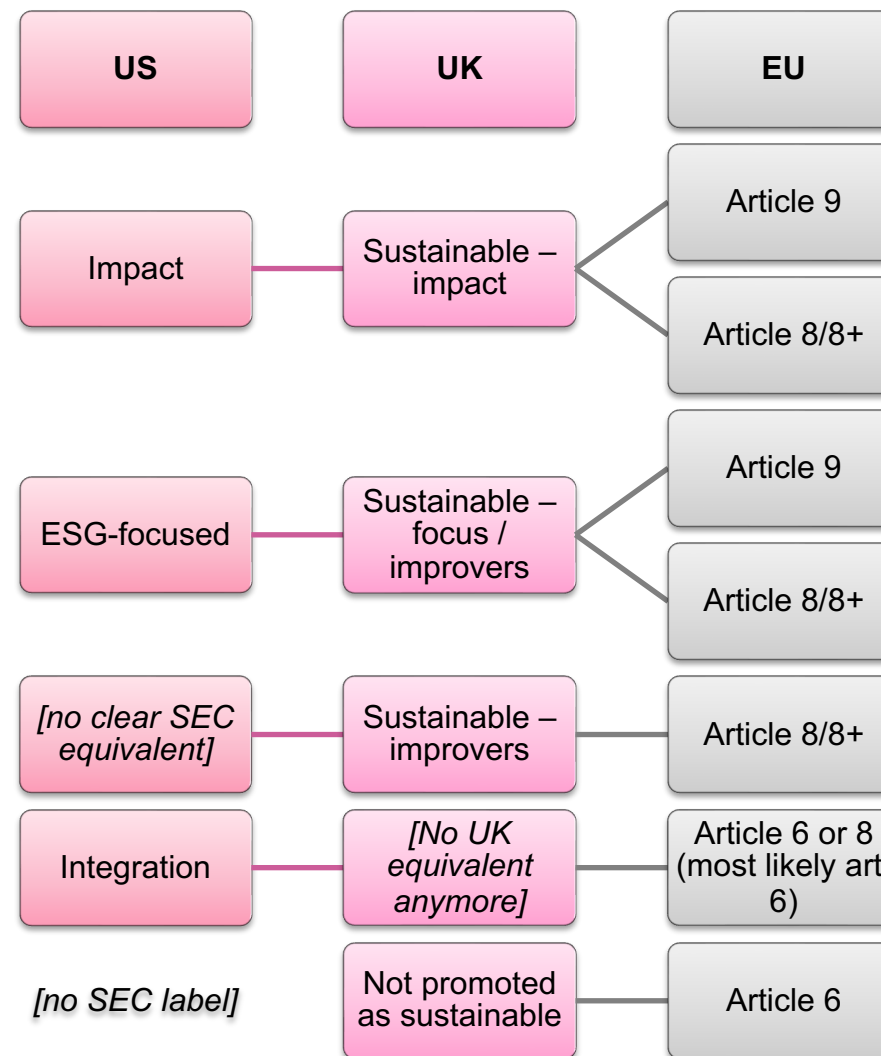
“ESG-Focused”  
Strategies

“Impact” Strategies

The ESG Strategy Proposal would impose varying disclosure requirements based on the type of ESG strategy pursued by the adviser or fund.

# US/UK/EU ESG Fund Classifications: How do they map?

- Unfortunately, there is no “easy”, unambiguous translation from one classification framework to another.
- The ultimate classification per rule-set will derive from the detail of the fund strategy.



Questions?

