Sustainable Disclosure Regulation

Webinar

14 May 2020

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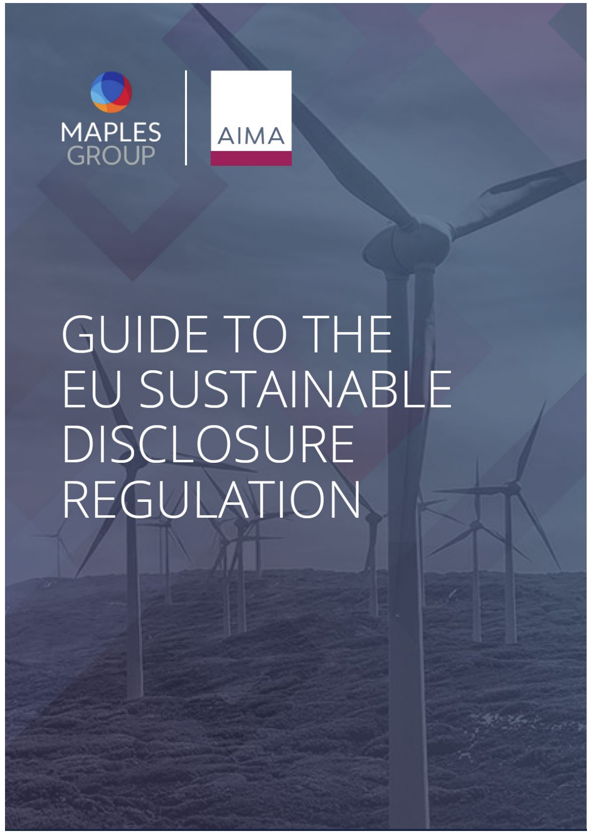
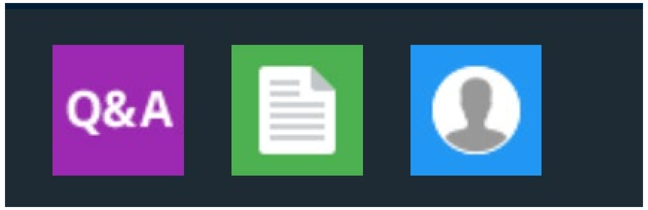
Resources

- Relevant ESG materials are available to download from **esg.maples.com**
- If viewing from a mobile device, the resource centre along with speaker bios and question portal, can be found by clicking on your screen and then clicking the relevant icons below
- For questions, please email webcasts@maples.com





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AIMA's Role

- Advocacy for Members at the Political and Supervisory Level
- Overview of the Guide to the Disclosure Regulation
- The aim of the Guide is to provide:
  - A practical summary of the key rules regarding sustainable finance disclosures and their relevance to Investment Managers and their "financial products"
  - Detailed compliance checklists for Investment Managers to assist with the implementation of the Disclosure Regulation

Background to the Disclosure Regulations

- The EU is strongly supporting the transition to a low-carbon, more resource-efficient and sustainable economy and has been at the forefront of efforts to build a financial system that supports sustainable growth

- "Sustainable finance" generally refers to the process of taking due account of **environmental**, **social** and **governance** ("**ESG**") considerations when making investment decisions, leading to increased investment in longer-term and sustainable activities

Environmental	**S**ocial	**G**overnance
Environmental considerations refer to climate change mitigation and adaptation, as well as the environment more broadly and the related risks (e.g. natural disasters)	Social considerations may refer to issues of inequality, inclusiveness, labour relations, investment in human capital and communities	The governance of public and private institutions, including management structures, employee relations and executive remuneration, plays a fundamental role in ensuring the inclusion of social and environmental considerations in the decision-making process

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*Based on the European Commission's definition of 'sustainable finance'

EU Sustainable Action Plan

- A key objective of the European Commission ("EC") is to **channel private investment as a complement to public money** into projects which will transition the EU to a climate-neutral economy
- To achieve the EU's 2030 targets agreed in Paris, including a 40% cut in greenhouse gas emissions, Member States will have to fill an investment gap that **was** estimated at 180 billion EUR per year
- The number is growing all the time…
- To incentivise and, where necessary, compel Investment Managers to make private capital available, the EC adopted a series of legislative measures in an action plan on sustainable finance (the "**Sustainable Action Plan**")

Objectives of the Sustainable Action Plan

- The objectives of the Sustainable Action Plan include:
  - Establishing a clear and detailed EU classification system – or taxonomy – for sustainable activities
  - Establishing mandatory disclosures and EU labels for green financial products
  - Introducing measures to clarify Investment Managers' and institutional investors' duties regarding sustainability
  - Strengthening the transparency of financial market participants and companies on their ESG policies
  - Incorporating climate risks into banks' risk management policies and supporting financial institutions that contribute to fund sustainable projects

EU Sustainable Finance Framework

- The Sustainable Action Plan also included a number of legislative proposals, one of which resulted in the adoption of the Disclosure Regulation
- There are many other legislative proposals in various stages of the EU's legislative process which will start to become effective from 2020 onwards

Disclosures Regulation	Consistent Disclosure Requirements in Relation to Sustainability
Taxonomy Regulation	A unified classification system for sustainable activities
Benchmarks Regulation	Standardised sustainability benchmarks for green products
MiFID and IDD	Including sustainability considerations in financial advice
UCITS AND AIFMD	Integrating sustainability risks and factors into UCITS and AIFMD
Corporate Non-Financial Disclosure	Strengthening ESG data reporting and accounting rule-making
Green Bonds	A common green bond standard to increase comparability and transparency
EU Ecolabel	Common EU Ecolabel for sustainable products, including financial products
Corporate Governance	Fostering sustainable corporate governance and collecting evidence of undue short-term pressure from capital markets
CRR / Solvency II	Incorporating sustainability into prudential requirements
Credit Ratings	Integrating sustainability in ratings and market research

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Renewed Sustainable Finance Strategy

- In addition, these ESG specific laws will have a knock-on impact and, in many cases, result in amendments to existing requirements for Investment Managers, e.g. **amendments are proposed to the UCITS, AIFM and MiFID Directives**

- The European Green Deal and the recovery from the economic consequences of the COVID-19 crisis will significantly increase the investment efforts needed across all sectors

- A Renewed Sustainable Finance Strategy was **launched** in April 2020 to:

  - Contribute to the objectives of the European Green Deal Investment Plan, in particular to create an enabling framework for private investors and the public sector to facilitate sustainable investments; and
  - Build on previous initiatives and reports, such as the Sustainable Action Plan and the reports of the Technical Expert Group ("**TEG**") on Sustainable Finance

- The EU has launched a consultation which will close on 15 July 2020

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Disclosures Regulation

- New harmonised disclosure requirements relating to three key areas which will be applicable to:

Financial Market Participants	Financial Advisors	Financial Products
• Alternative Investment Fund Managers • UCITS Management Companies • MiFID Investment Firms	• Alternative Investment Fund Managers • UCITS Management Companies • MiFID Investment Firms	• Alternative Investment Funds • UCITS Funds • ESG Products • Segregated Accounts

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Disclosure Regulation at Firm Level

Requirements	Scope	Channel of the Disclosure
Sustainability risks at the level of the financial market participant (Article 3)	All financial market participants – no opt out	Website (public)
Sustainability Risks at the level of the financial adviser (Article 3)	All financial advisers – no opt out	Website (public)
Principal adverse sustainability impacts (PASI) at the level of the financial market participant (Article 4)	All financial market participants on a "comply or explain" basis. Financial market participants with more than 500 employees or qualifying parent undertakings are obliged to comply from 30 June 2021 Those that choose to explain why they don't consider PASI are referred to as "PASI" opt-out firms in this table	Website (public)
Principal adverse sustainability impacts (PASI) at the level of the financial advisers (Article 4)	All financial advisers on a "comply or explain" basis. Those that choose to explain why they don't consider PASI are referred to as "PASI" opt-out firms in this table	Website (public)
Remuneration (Article 5) at the level of financial market participants and financial advisers (Article 4)	Financial market participants and financial advisers subject to UCITS, AIFMD, MiFID, CRD / CRR, IORPs frameworks No opt out	Website (public)
Absence of reference to EU Green Taxonomy	Products that are not being marketed with a sustainable investment objective nor promoting sustainable characteristics	Investors: Pre-contractual disclosures and periodic reports

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Disclosure at Product Level

Requirements	Scope	Channel of the Disclosure
Sustainability risks by financial market participants (Article 6)	Description of manner which sustainability risk is integrated into investment decision and assessment of likely impact on the returns of the product OR explanation why sustainability risks are not relevant. "Comply or explain" clause.	Investors: Pre-contractual disclosure
Sustainability risks by financial advisers (Article 6)	Description of manner which sustainability risks are integrated into their investment or insurance advice and assessment of likely impact on the returns of the product they advise on OR explanation why sustainability risks are not relevant. "Comply or explain".	Investors: Pre-contractual disclosure
Principal adverse sustainability impact by financial market participants (not applicable to financial advisers) (Article 7)	Where a financial market participant has a sustainability due diligence policy (under Article 4), a description of whether and how a financial product considers PASI. Where a financial market participant does not have a sustainability due diligence policy (under Article 4), a statement that the financial market participant does not consider the adverse impacts of investment decisions on sustainability factors and why. "Comply or explain".	Investors: Pre-contractual disclosure and periodic reports

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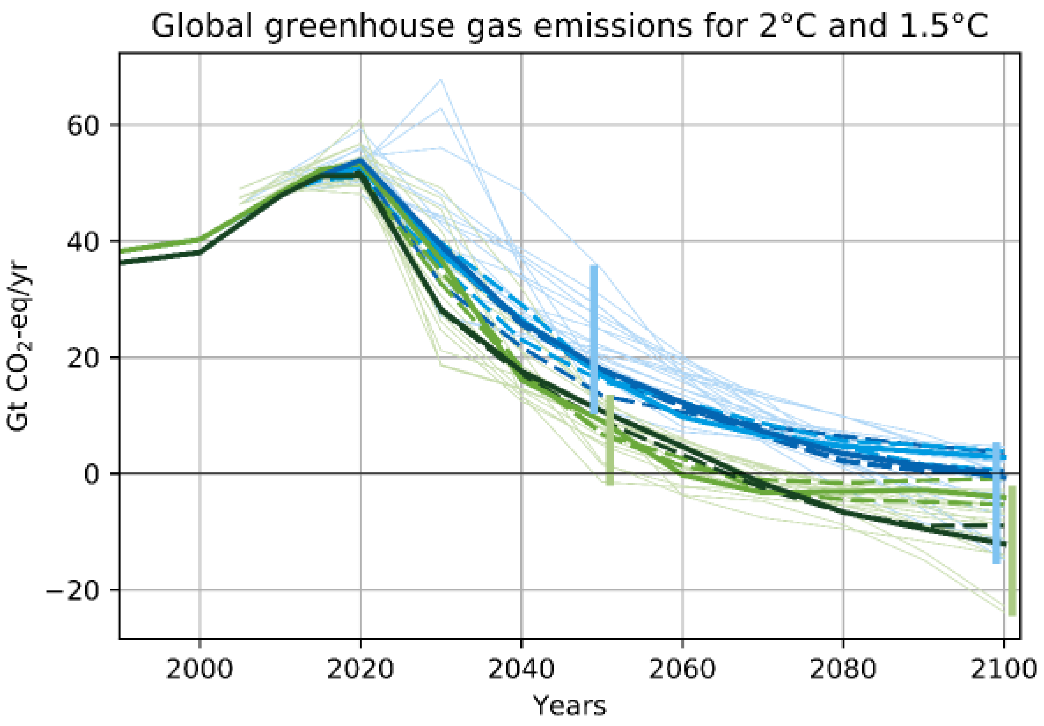
EU Sustainable Finance Strategy and Technical Expert Group

- TEG established in June 2018
- 35 members from finance, academia, business, civil society, EU and international bodies
- The Taxonomy subgroup developed recommendations towards carbon neutrality – net zero carbon emissions by 2050
- TEG recommendations inform legislation, strategy and guidance



2°C (blue bar) and 1.5°C (green bar) runs from POLES-JRC and IMAGE models

Why Act? Why Sustainable Finance?

Environmental risks occupy the top right quadrant of the Global Risks Landscape of 2020

Top Global risks in terms of likelihood and impact include:

- Climate Action Failure
- Biodiversity Loss
- Extreme Weather
- Water Crisis
- Natural Disaster
- Cyber-Attacks
- Human-Made Environmental Disasters (pollution)
- Global Governance Failure
- Interstate Conflict
- Involuntary Migration

Taxonomy Regulation

- Harmonised classification system for economic activities that qualify as environmentally sustainable for investment purposes
- Applies to all financial products regardless of whether they are marketed as "green" or not
- In order to be considered an "environmentally sustainable investment" a fund must:
    - Invest in economic activities that contribute substantially to one or more of six environmental objectives
    - Do no significant harm to any of the six environmental objectives
    - Comply with minimum human rights / social safeguards
    - Comply with minimum technical screening criteria (to be established)
- Disclosure on level of compliance – requirements based on whether the fund is "green" or has ESG characteristics

Environmental Objectives

1. CLIMATE CHANGE MITIGATION
2. CLIMATE CHANGE ADAPTATION
3. SUSTAINABLE USE OF WATER AND MARINE RESOURCES
4. CIRCULAR ECONOMY
5. POLLUTION PREVENTION
6. HEALTHY ECOSYSTEM

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Who will use the Taxonomy?

- The Taxonomy Regulation applies to:
  - Financial market participants ("**FMPs**")
  - EU Member States or the EU when adopting measures or setting requirements on market actors in respect to financial products or corporate bonds that are marketed as environmentally sustainable
  - Undertakings subject to the Non-Financial Reporting Directive (2013/34/EU)
- The Taxonomy can be used on a voluntary basis

FMPs are defined in Article 2(1) Disclosure Regulation

Uses and Users of the Taxonomy		
	Disclosure Obligations	**Optional Additional Uses**

Asset Management	• UCITS Funds:
	  • Equity funds
	  • Exchange-traded funds ("**ETFs**")
	  • Bond funds
	• Alternative Investment Funds ("**AIFs**"):
	  • Fund of funds
	  • Real estate funds
	  • Private equity or SME loan funds
	  • Venture capital funds
	  • Infrastructure funds
	• Portfolio management	

Insurance	• Insurance-based investment products ("**IBIP**") • Institution for occupational retirement provision ("**IORP**")	• Insurance (selected non-life LOBs)
Corporate & Investment Banking	• Securitisation funds* • Venture capital and private equity funds • Portfolio Management • Indices funds	• Securitisation • Venture capital and private equity • Indices • Project finance and corporate financing
Retail Banking		• Mortgages • Commercial building loans • Car loans, Home equity loans

* Securitisations, indices, venture capital or private equity conducted by investment banks do not fall under the scope of the regulation. They would not have to report on how they relate to the Taxonomy. However, the funds that replicate the indices, aggregate or package the green securitisations or private equity investments which are sold as AIFs, UCITS, EUVECA funds or EU SEF would have to disclose the extent to which they use the taxonomy.

Disclosures for Taxonomy Aligned Sustainable Investments

- For each relevant product, the FMP will be required to state:
  - **How and to what extent** they have used the Taxonomy in determining the sustainability of the underlying investments;
  - **To what environmental objective(s)** the investments contribute; and
  - **The proportion of underlying investments** that are Taxonomy-aligned, expressed as a percentage of the investment, fund or portfolio – this disclosure should include details on the respective proportions of **enabling and transition** activities, as defined under the Regulation
- The disclosures must be made as part of existing **pre-contractual and periodic reporting** requirements – these products also carry sustainability disclosure obligations under the Disclosure Regulation

Sample Client Checklists

Investment Managers managing or distributing financial products in the EU

Policies	• Draft or update your internal policy describing how sustainability risks are considered in the investment process • Amend the internal UCITS, AIFMD or other remuneration policy to ensure consistency with the consideration of sustainability risks
Products	• Identify specific products being marketed by your organisation according to key criteria
Website	• Draft and publish a paragraph describing the main features of the sustainability risks policy; alternatively, firms might elect to publish the policy in full • Publish the information in the remuneration policy that shows the consistency of the policy with the integration of sustainability risks
Prospectus or Offering Document	• Check for which products sustainability risks are relevant and describe the manner in which these risks are integrated in investment decisions • For products for which sustainability risks are not relevant, give a clear and concise explanation of the reasons why such risks are not relevant
Other Issues	• Check whether the consideration of principal adverse impacts is mandatory for your firm (500 employees threshold), or consider whether to opt out

Other Sample Checklists

- Investment Managers with 500+ employees
- PASI Opt-out Firms
- Mainstream Financial Products
- Products with E or S Characteristics
- Products with Sustainable Investment Objectives

Q&A

- Some Investment Managers are concerned that the Disclosure Regulation and Taxonomy impose too great a burden on them and may make the EU less competitive. What would you say to address such concerns and do you also see the positives in the new laws?

- What about timelines? When should managers start actively working on ESG updates. How is the Maples Group working on this with clients?

- How can AIMA further assist members who are focusing on Sustainable Finance?

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Questions

- Further questions can be sent to webcasts@maples.com

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May 2020