



CLERKIN LYNCH LLP

Regulatory update: ESG Investing

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Agenda

- Introduction and definitions
- Market Developments
- International Developments
- European Union Legal Updates



Introduction and Definitions



Introduction

- Socially responsible investing: any investment strategy which seeks to consider both financial return and social/environmental impacts to achieve change regarded as positive by proponents.
- A multitude of investment approaches and strategies.
- Absence of a single legal definition.
- Differences in reporting, collection and evaluation of relevant data.
- Role of industry standards: consistency.
- ESG: three central factors identified in measuring the sustainability and societal impact of an investment.



Introduction: what is ESG?

“E”

Environmental Considerations

- Climate change mitigation and adaption (e.g. carbon footprint);
- Environmental issues more broadly (e.g. pollution, land use);
- Environmental related risks, including natural disasters.



Introduction: what is ESG ?

“S”

Social Considerations

- Inequality, inclusiveness;
- Labor relations;
- Investment in human capital and communities.



Introduction: what is ESG ?

“G”

Governance Considerations

- Public and private institutions;
- Management structures;
- Employee relations and executive remuneration;
- Fundamental means of ensuring inclusion of E and S factors into the decision making process.



Introduction

European Commission:

- ESG: integral parts of sustainable economic development
- Sustainable finance: finance to support economic growth while reducing pressure on the environment and taking into account social and governance aspects.
- Transparency of risks related to ESG factors
- Mitigation of those risks



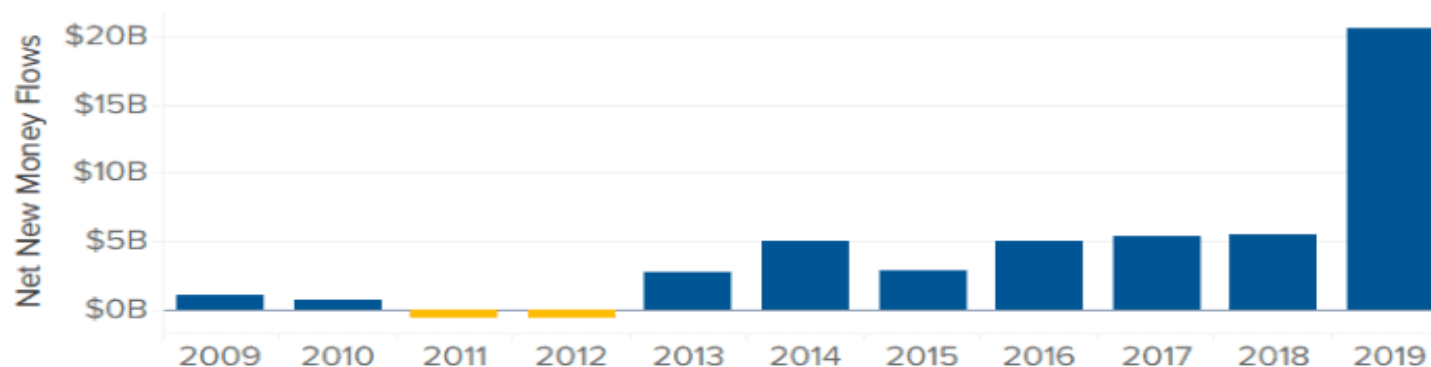
Market Developments



Growth of ESG Investing

ESG funds capture record flows in 2019

The investments raked in almost four times as much last year as the year prior



SOURCE: Morningstar





Growth of ESG Investing

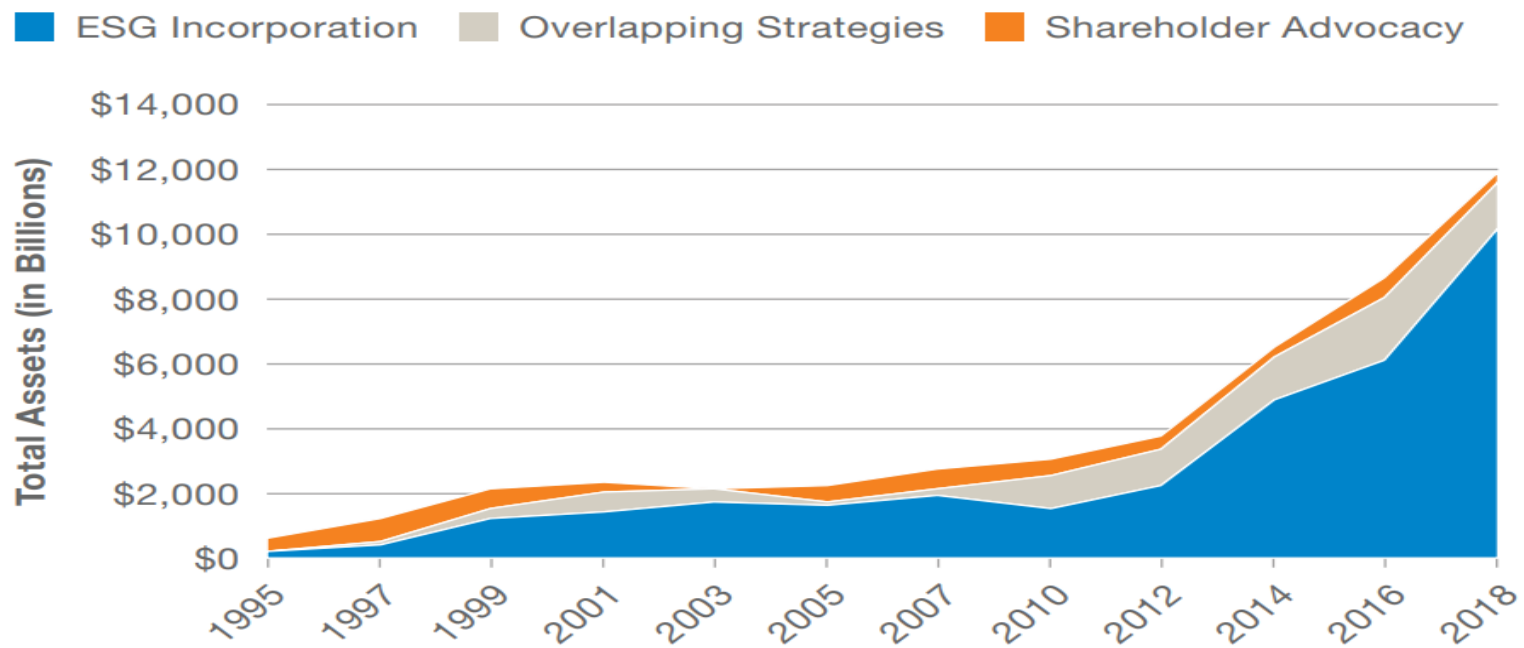
Assets in ESG funds surge

Total assets in environmental, social and governance and socially responsible ETFs (\$bn)



Source: EFR Global
© FT

Growth of ESG Investing in the U.S. (1995–2018)



SOURCE: US SIF Foundation.



Market Developments

- Exponential growth
- Differences between the US, Europe and the rest of the world
- Classification Issues
- Need for standardisation
- Regulatory imperatives
- Not merely an optional marketing strategy



International Developments



Global Initiatives

- Created by supra-governmental and non-governmental organizations and industry associations:
 - United Nations (UN) Principals of Responsible Investment (2006)
 - UN Conference on Sustainable Development – Rio+20 (2012)
 - Paris Agreement on Climate Change (2015)
 - UN 2030 Sustainable Development Agenda and Sustainable Development Goals (SDGs) (2015)
- Global Reporting Initiative (GRI)
- Sustainability Accounting Standards Board (SASB)



European Union Developments:

- LEGAL DEVELOPMENTS IN THE EU PERTAINING TO ESG



EU Action Plan

- European Commission appointed ‘High-Level Expert Group’: published its final report (January 2018)
- Action Plan on Sustainable Growth (March 2018)
- EC Green Deal (December 2019)
- Sustainable Finance Strategy (February 2020)



Implementing the EU Action Plan

Initiative	Full Title
Climate Benchmarks Regulation	Regulation (EU) 2019/2089 of the European Parliament and of the Council of 27 November 2019 amending Regulation (EU) 2016/1011 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks (the "Climate Benchmarks Regulation")
Sustainable Finance Disclosure Regulation	Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (the "Sustainable Finance Disclosure Regulation")
Taxonomy Regulation	Regulation of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment and amending Regulation (EU) 2019/2088 (the "Taxonomy Regulation")
MiFID and IDD	Commission Delegated Regulation amending Delegated Regulation (EU) 2017/565 as regards the integration of Environmental, Social and Governance (ESG) considerations and preferences into the investment advice and portfolio management Acts on integrating sustainability risks and factors in MiFID II
UCITS and AIFMD	Commission Delegated Acts on integrating sustainability risks and factors in the UCITS Directive and AIFMD



Climate Benchmarks Regulation

Requires benchmark “administrators” to make disclosures regarding the methodology used to measure and reconcile ESG factors and low-carbon factors in the composition of relevant benchmarks.

Two new types of “climate benchmark” to ensure benchmark integrity:

- EU Climate Transition Benchmark (“CTB”), and
- EU Paris-Aligned Benchmark (“PAB”)

Effective Date

- 30 April 2020 for ESG benchmark statement/methodology disclosure
- 31 December 2021 Paris alignment disclosures



Sustainable Finance Disclosure Regulation

Applies to “Financial market participants” (FMPs)

- Manager-level disclosure requirements
- Product-level disclosure requirements

New harmonized disclosure requirements for FMPs and financial products (FPs) covering:

- **All** FMPs/FPs (regardless of approach to sustainable investment)
- FPs which **promote** ESG aims (Light Green)
- FPs which have “sustainable investment” as their **objective** (Dark Green)

Effective date

- 10 March 2021 for most provisions
- 1 January 2022 for annual report disclosure



Sustainable Finance Disclosure Regulation

Types of disclosure

- Pre-contractual disclosure (Prospectus Updates)
- Website disclosure of policies
- Periodic reporting
- Marketing

Nature of disclosure

- Inclusion and Integration of sustainability risks
- principal adverse impacts on sustainability factors (comply or explain)
- Environmental or social characteristics/objects – how met and the methodologies to assess, measure and monitor impact (including benchmarks)
- Over-all sustainability-related impact



Taxonomy Regulation

EU-wide classification system or ‘framework’ for sustainable investment

Defines “environmentally sustainable” economic activities, as those that contribute to:

▪ Climate change mitigation	▪ Transition to a circular economy
▪ Climate change adaption	▪ Pollution prevention and control
▪ Sustainable use/protection of water/marine resources	▪ Protection/restoration of biodiversity/ecosystems

Requires relevant entities, including FMPs (e.g. UCITS mancos), to disclose alignment

Technical screening criteria to be developed to determine an investment’s degree of Taxonomy alignment

FPs promoting environmental/social characteristics or with a sustainable development objective must disclose percentage of alignment with Taxonomy

Effective Date: 31 December 2021 for first set of financial products disclosure requirements

Draft Amendments to MiFID II



Requirement to take into account:

- Internal ESG focussed resources where relevant to services
- Sustainability Risk of investments
- Risk management
- Conflicts of interest
- ESG preferences of clients
- ESG characteristics of investments



Draft amendments to UCITS and AIFMD

Revision of existing directives to ensure sustainability risks:

- Recognised and Integrated into management responsibilities
- Conflicts of Interest
- Due Diligence
- Risk Management Policy



Other EU ESG Initiatives

- Changes to the Non-financial Reporting Directive
- Green Bond Standard
- EU Ecolabel framework for certain financial products
- CRR/Solvency II

EU Sustainable Finance Regime: Overview



EU Sustainable Finance Regime: Overview

Initiative	Current status	Estimated Implementation Timeframe
Climate Benchmarks Regulation	Regulation (EU) 2019/2089 of the European Parliament and of the Council of 27 November 2019 amending Regulation (EU) 2016/1011 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks (the "Climate Benchmarks Regulation")	In force
Sustainable Finance Disclosure Regulation	Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (the "Sustainable Finance Disclosure Regulation"). Subsequent Delegated Acts issued: Delegated Regulation (EU) 2022/1288 and 2023/363.	In force
Taxonomy Regulation	Regulation of 2020/852 the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment and amending Regulation (EU) 2019/2088 (the "Taxonomy Regulation")	In force
MiFID and IDD	Commission Delegated Regulation (EU) 2021/1253 amending Delegated Regulation (EU) 2017/565 as regards the integration of Environmental, Social and Governance (ESG) considerations and preferences into the investment advice and portfolio management Acts on integrating sustainability risks and factors in MiFID II	In force
UCITS and AIFMD	Delegated Regulations in force. Delegated Regulation (EU) 2012/1255 for AIFMs Delegated Regulation (EU) 2012/1270 for UCITS	In force
Corporate non-financial disclosures	Update to the Non-Financial Reporting Directive. Directive (EU) 2022/2464 passed 14 December 2022 as regards corporate sustainability reporting. Effective 5/01/23	In force
Green bonds	Technical Expert Group (TEG) Reports have issued . European Parliament has approved text.	TBD
EU Ecolabel	Technical Reports from the Commission Joint Research Centre have issued. Q3 2021 expected adoption of Commission decision	TBD
Corporate governance	Discussions ongoing.	TBD
CRR / Solvency II	Updated draft regulation circulates 2021. Expected implementation 2025.	TBD

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Clerkin Lynch LLP



Mark is a Partner and Head of Asset Management and Funds in Clerkin Lynch LLP. He has in excess of 15 years experience as a solicitor advising on the establishment, launch and ongoing operations of investment funds.

His experience covers both funds authorised as UCITS and under the AIFMD. In addition to Dublin, he has worked in some of the other key international fund domiciles including the Cayman Islands and Luxembourg.

ESG is one of his particular areas of focus.