

# Guide to help advisers navigate the ESG world with clients

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# About this guide

The Sustainability Assessment guide is designed to help you and your customers understand sustainable investing, sustainability preferences requirements and help you choose investments that match your customers' sustainability preferences.

It is now a requirement under the Insurance Distribution Directive (IDD) for Financial Advisers that provide investment advice to ask new and existing customers about their sustainability preferences.

## The process in detail

### Step 1

As usual, you should conduct your normal fact find, obtaining information about a customer to determine their suitability for a particular product. This includes the discussion around investment objectives, customer's financial and investment knowledge, their financial situation and assess their preference for risk taking and risk tolerance, among other things.

### Step 2

You will then need to explain to the customer what sustainability preferences are and the distinct categories available. See page 2 for terms that you, your colleagues and your current and potential customers should become familiar with.

There is one other point worth explaining to your client before you start the sustainability assessment.

There is currently a limited number of funds available that meet the narrow categories laid out by the IDD update. While there may be funds available that align with your customers' sustainability preferences, it is important that they also align with the suitability assessment carried out in the fact find e.g., risk and return profile, time horizon etc.

Currently most Article 8 and 9 funds tend to be equity funds with a risk rating of 5 or 6. These would not be suitable for a low-risk investor.

### Step 3

This step involves carrying out the sustainability assessment with your customer. Please refer to page 4 for a look at what is involved and how you might approach the assessment.

### Step 4

After carrying out the sustainability preferences assessment you can then recommend an investment that matches both your customer's sustainability preferences and other criteria that was found in the fact find such as risk appetite, time horizon to retirement etc. To help with the recommendations, see page 4 for a breakdown of our ESG fund solutions.

### Step 5

As usual, you must maintain records of the fact find and now the sustainability preferences assessment.

You should also document the reasoning if you cannot recommend a fund solution in line with your customer's preferences.

## What about existing customers?

Maintaining records also applies to existing customers and offers an opportunity to engage with these clients.

Where a Financial Adviser providing investment advice has informed the customer that it will carry out a periodic assessment of suitability, the periodic report shall contain an updated statement of how the investment product meets the customer's preferences, objectives and other characteristics of the customer, now including sustainability.

If an existing customer has not specified their sustainability preferences, you can follow steps 2 and 3 to assess their sustainability preferences.

If your existing customer has already specified their sustainability preferences, assess if these are being met by the current investment strategy.

If the investment you recommended no longer matches your customer's preferences: inform them and make new recommendations where required and document the reasoning.

Staff providing investment advice should also be provided with training on sustainability topics.

## Explanation of sustainability terms

### Q1 What do we mean by “sustainable preferences”?

Sustainability preferences describe the customer's decision as to whether and to what extent aspects of sustainability should be included in their investment decision. Sustainable investment preferences are divided into three categories under IDD:

- Environmentally Sustainable Investments
- Sustainable Investments
- Investments that consider the negative impacts of the investment strategy on ESG factors

### Q2 Environmentally sustainable investments

“Environmentally sustainable investments” are focused on significant positive contributions to one or more of the six ecological objectives set out in the EU Taxonomy while at the same time not doing any significant harm to any of the remaining objectives. These investments must also follow good corporate governance. The six environmental objectives are:

- Climate change mitigation
- Climate change adaptation
- Sustainable use and protection of water and marine resources
- The transition to a circular economy
- Pollution prevention and control
- Protection and restoration of biodiversity and ecosystems

### Q3 Sustainable investments

“Sustainable investments” are Article 9 investments according to the Sustainable Finance Disclosure Regulation.

- Article 9 investments are funds with a specific environmental or social objective
- They can therefore have a broader focus than “environmentally sustainable investments”
- Article 9 funds are also known as “dark green” funds

**Q4**

### **Investments that consider the negative impacts of the investment strategy on ESG factors**

- This may also be referred to as Principal Adverse Impacts (PAIs)
- PAIs refers to negative ESG indicators that are taken into consideration. Examples of what you might expect to see are greenhouse gas emissions, carbon footprint, hazardous waste, water emissions, negative impacts on areas of biodiversity
- Article 8 investments are funds promote social and/or environmental characteristics, invest in companies that follow good governance but do not have a sustainable investment objective
- Article 8 funds are also known as “light green” funds

## Your clients may also ask:

**Q1**

### **What do you mean by “sustainable Investing”?**

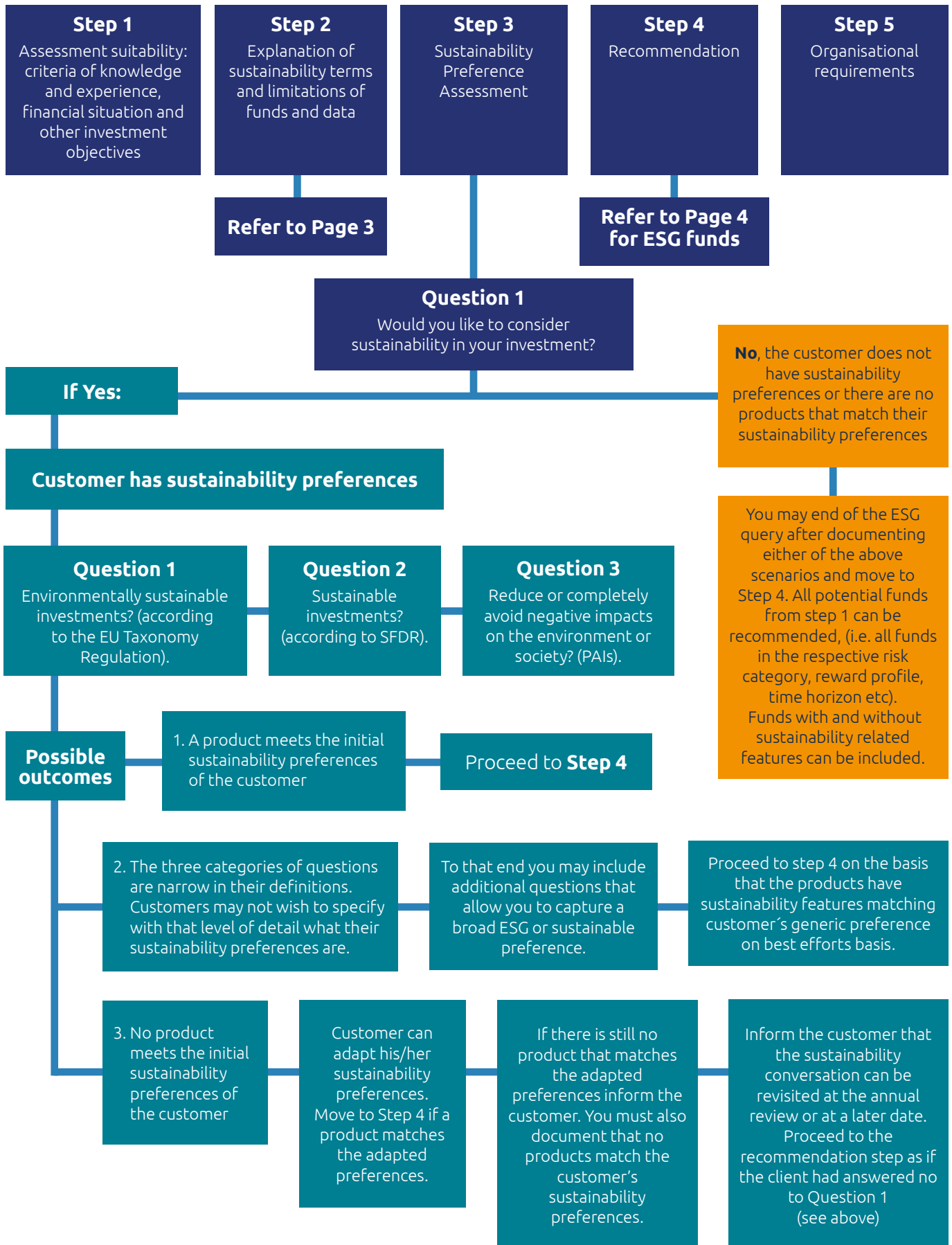
- Investments that are environmentally related are sustainable e.g. climate protection, water protection, forest protection, biodiversity) and/or address social criteria (e.g. fair pay, fair working conditions, fair supply chains) and follow good corporate governance (e.g. fair tax payments, no corruption)
- Sustainable Investing means investing in companies that contribute to an environmental or social objective while ensuring that the investment does not significantly harm any other environmental or societal objective under the EU Taxonomy. It also requires companies to follow good governance practices
- You may also come across the term “ESG”. It refers to the environmental, social, and governance factors used to evaluate companies and funds during the investment process
- ESG investing can be achieved by applying exclusions, limiting ESG risk, seeking ESG opportunities, practicing active ownership, targeting sustainability themes, or assessing impact

**Q2**

### **How does “sustainability” affect performance?**

- The performance of an investment depends on many factors
- Sustainability is at infancy stage in terms of performance. No statement can be made as to whether an ESG investment will deliver better, the same or worse results in the medium term than a comparable “non-ESG investment”. In addition, past performance is no guarantee of future performance
- Applying ESG and sustainability criteria in the investment process may result in the exclusion of securities in which a Fund might otherwise invest. Such securities could be part of the benchmark against which the Fund is managed, or be within the universe of potential investments. This may have a positive or negative impact on performance and may mean that the Fund’s performance profile differs to that of funds which are managed against the same benchmark or invest in a similar universe of potential investments but without applying ESG or sustainability criteria

# Sustainable Assessment Playbook



## What can Standard Life offer if your customer has “sustainable preferences”?

Standard Life currently offer a range of Article 8 Funds and one Article 9 Fund through their range of Synergy saving, investment and pension products.

## Sustainable investments

### Dark Green Funds (Article 9) – funds with a specific environmental or social objective

- Standard Life Global Equity Impact

## Environmentally sustainable investments

### EU Taxonomy aligned

- Standard Life currently do not offer EU Taxonomy aligned funds

## Principal Adverse Impacts (PAIs)

Principal Adverse Impact Indicators are metrics that measure the negative effects on environmental and social matters. abrdn consider PAIs within the investment process for their funds.

This may include considering whether to make an investment, or they may be used as an engagement tool for example where there is no policy in place and this would be beneficial, or where carbon emissions are considered to be high, abrdn may engage to seek the creation of a long-term target and reduction plan.

abrdn assess PAIs by using, amongst others, the PAI indicators referred to in the SFDR Delegated Regulation; however, depending on data availability, quality and relevance to the investments not all SFDR PAI indicators may be considered. Where Funds consider PAIs, information on that consideration will be made available in annual reports.

Funds that consider the Principal Adverse Impact on:

## Greenhouse gas emissions

- Standard Life European Smaller Companies - Article 8
- Standard Life Global Corporate SRI Bond - Article 8
- Standard Life Global Equity Impact -Article 9
- Standard Life Global Smaller Companies - Article 8
- Standard Life Multi-Asset ESG - Article 8

## Social and Employee Issues

- Standard Life Global Corporate SRI Bond - Article 8
- Standard Life Global Equity Impact -Article 9
- Standard Life Multi-Asset ESG - Article 8

## Water

- Currently no funds available

## Biodiversity

- Currently no funds available

## Waste

- Currently no funds available

## Other ESG funds

### Light Green Funds (Article 8) – funds that promote environmental and/or social characteristics

- Standard Life Corporate Bond
- Standard Life European Ethical Equity
- Standard Life European Smaller Companies
- Standard Life Global Corporate SRI Bond
- Standard Life Global REIT
- Standard Life Global Smaller Companies
- Standard Life Multi-Asset ESG
- Standard Life MyFolio Active range
- Standard Life Sustainable Index World Equity
- Standard Life Total Return Credit

## The Sustainability and ESG regulatory landscape

### The EU Action Plan

In 2018 the EU launched its strategy for financing sustainable growth. The 10-Point Plan aims to leverage financial markets to address sustainability challenges, especially those related to climate change.

The EU's Action Plan is part of the implementation of the wider Paris Agreement on Climate Change and the UN 2030 Agenda for Sustainable Development.

### The 10-Point Action Plan

The Action Plan proposes 10 reforms based on three sustainability objectives:

#### Reorienting capital flows towards a more sustainable economy

1. Establishing an EU classification system for sustainability activities (The EU Taxonomy)
2. Creating standards and labels for green financial products
3. Fostering investment in sustainable projects
4. Including sustainability when providing financial advice (IDD update)
5. Developing sustainability benchmarks

#### Mainstreaming sustainability into risk management

6. Better integrating sustainability in ratings and research.
7. ESG in investment management (PAIs)
8. Incorporating sustainability in prudential requirements

#### Fostering transparency and long termism

9. Strengthening sustainability disclosure (SFDR and PAIs)
10. Fostering sustainable corporate governance

With the alphabet soup of new regulations and standards that are being introduced, it can be difficult for advisers, clients, asset managers and product providers to effectively navigate this space.

Below we have provided a high level look at the IDD's Sustainability Preferences requirement, SFDR, the EU Taxonomy, and PAIs.

### Sustainability Preferences (IDD)

The IDD update that came in for effect on 2 August 2022 introduced the requirement for financial advisers providing investment advice relating to the sale of Insurance Based Investment Products (IBIPs) to integrate sustainability preferences assessment into their advisory process.

The IDD update set out three categories to determine and document customer sustainability preferences. You may include other sustainability related questions if you wish.

- IBIPs for which a minimum proportion shall be invested in environmentally sustainable activities which are taxonomy-aligned
- IBIPs for which a minimum proportion shall be invested in sustainable activities according to SFDR
- IBIPs that considers principal adverse impacts (PAIs) on sustainability factors

An explanation of these three categories is provided on page 3. Both you and your client should understand what each one means.

### Sustainable Finance Disclosure (SFDR)

SFDR Level 1 came into effect in March 2021, requiring managers to disclose how sustainability risks are considered in their investment process, what metrics they use to assess ESG factors, and how they consider investment decisions that might result in negative effects on sustainability factors (or Principal Adverse Impacts (PAIs)). Its aim is to support client understanding of sustainability risks by categorising investment funds as follows:

- **Article 6** are funds that do not consider sustainability risks in their investment decisions
- **Article 8 or Light Green** are funds that promote environmental or social characteristics, and invests in companies that follow good corporate governance.
- **Article 9 or Dark Green** are funds with specific environmental or social objectives and invests in companies that follow good corporate governance. These funds must invest only in Sustainable Investments excluding instruments used for liquidity purposes

From the 01 January 2023 (under SFDR Level 2), both Dark Green and Light Green funds will need to disclose the extent that they invest in sustainable investments and their EU Taxonomy alignment.

## What is a “sustainable investment” under SFDR?

A “sustainable investment” under SFDR must:

- Explain how they consider Principle Adverse impacts
- ‘Do No Significant Harm’ (DNSH). DNSH is linked to the EU Taxonomy Minimum Safeguards:
  1. OECD Guidelines for Multinational Enterprises UN Guiding Principles on Business and Human Rights
  2. Intl Labour Organisation on Fundamental Principles and Rights at Work
  3. International Bill of Human Rights

Funds investing in environmentally sustainable activities (EU Taxonomy) can state this and would not need to explain how they consider PAIs or DNSH.

## The EU Taxonomy

In its simplest terms, the Taxonomy Regulation is a classification tool to determine whether an economic activity is environmentally sustainable. It is intended helps investors, companies and policy makers make more informed decisions by identifying activities that are deemed to make substantial contributions to environmental objectives and thereby help to finance the transition to a more sustainable economy.

Six environmental objectives defined by the Taxonomy:

1. Climate change mitigation
2. Climate change adaptation
3. Sustainable use and protection of water and marine resources
4. The transition to a circular economy, waste prevention and recycling
5. Pollution prevention and ion control
6. Protection and restoration of biodiversity and ecosystems

For an activity to be classified as sustainable, it must:

- Substantially contribute to at least one of the six environmental objectives mentioned above
- Do no significant harm to any of the other environmental objectives (DNSH criteria)
- Comply with minimum safeguards created to avoid negatively impacting societal stakeholders

## Principal Adverse Impacts

“Principal Adverse Impacts” are the most significant negative impacts of investment decisions on sustainability factors relating to environmental, social and employee matters.

Examples can include, but not limited to:

- Greenhouse gas emissions
- Carbon footprint
- Activities negatively affecting biodiversity areas
- Violations of UNGC principles and OECD Guidelines
- Board gender diversity
- Exposure to controversial weapons



**The guide was designed with great care to the best of our knowledge. However, Standard Life does not warrant that use of this guidance is sufficient to ensure proper IDD advice.**

For more information on our funds, please visit [standardlife.ie/funds](https://standardlife.ie/funds)

## Find out more

Talk to your financial adviser. They'll give you the information you need. Also, you can call us or visit our website.

## Call us on (01) 639 7000

Mon-Fri, 9am to 5pm. Calls may be monitored and/or recorded to protect both you and us and help with our training. Call charges will vary.

[standardlife.ie](https://standardlife.ie)