SPTF
Promoting standards & practices for responsible inclusive finance

SPTF Social Investor Working Group
February 17, 2021

Implementing the Sustainable Finance Disclosure Regulation (SFDR)

Overview of the SFDR

- *Goals of SFDR*
  - Integrate sustainability risks into investment decision-making process and investment advice. Sustainability risk is an environmental, social or governance event or condition that, if it occurs, could cause an actual or a potential material negative impact on the value of the investment.
  - Disclose consideration of principal adverse impacts on sustainability factors in investment decision-making process or investment advice. Principal adverse impacts are the impacts of investment decisions and advice that result in negative effects on sustainability factors (without looking at the value of an investment).

- *SFDR Background & Timeline*
  - SFDR is part of a package of reforms implementing the UN 2030 Agenda on SDGs and the Paris Agreement. It imposes ESG transparency requirements (i.e., website disclosures, pre-contractual disclosures, and investor reporting) on investment managers, advisers, and financial products.
  - **Feb 28, 2021**: Fast-track procedure pre-contractual disclosure deadline.
  - **Mar 10, 2021**: Sustainability risk and principal adverse impact website disclosures apply; sustainability risk pre-contractual disclosures apply.
  - **Jan 1, 2022:** Investor reporting on the sustainability-related impacts of the financial products applies; technical standards apply.
  - **Dec 30, 2022**: Principal adverse impact pre-contractual disclosures apply.

- *Practical Implications*
  - Applies to asset managers, financial advisers, and financial products
  - Uses technical standards as guidance
  - Disclosures in issue documents/prospectuses and the CSSF fast track procedure (plus confirmation letter)
  - The SFDR's application to non-EU AIFMs
  - **SIWG poll:** 32% of participants on the call said that their organization falls under the SFDR, 17% said their organizations did not, and 2% said their organizations partially fall under the regulation.

Panel on Implementing the SFDR

- *Panelists*
  - Mette Kjaer, responsAbility
  - Christophe Bochatay, Triple Jump
  - Amy Bergstraesser, Symbiotics

- *Where are you in the implementation of the regulation? What are your main challenges in preparation?*
  - Mette said responsAbility is in the final stage of implementation and is ready to publish on its website. It's working on final versions of policies on sustainability risks. They've had many challenges in understanding the requirements of the regulation, determining how to implement into policies, and identifying how to categorize funds. It used a sustainability test to ask if the majority of the fund meets the different criteria.
  - Christophe said Triple Jump spent the majority of its time looking at which funds and mandates are in the scope of the regulation. How do you communicate and disclose this information to investors? It conducted a gap analysis and action plan in December and focused on Level I. It revisited risk and ESG policies. Its challenge will be to abide to Level II, which are more specific and not suited for smaller investments in financial inclusion.
  - Amy Bergstraesser said Level I is the base document of SFDR and Level II is the technical standards. Level II is telling how to implement Level I. Symbiotics used Level II as a guide to implement Level I. If the fund fits within the Article distinction, then that is the Article that needs to be abided by.

- *As impact investors, do you feel that you already have most of the information required?*
  - Mette said responsAbility had most of the information already available, but generally this regulation is good when it comes to greenwashing issues. As impact investors this is already mostly in place.
  - Christophe said more work needs to be done with the technical guidance regarding the requirement on reporting on new indicators (greenhouse gas emissions, using non-renewable energy sources, etc.)

- *Do you have any advice for smaller organizations who are trying to prioritize where to start?*
  - Mette said to start as early as possible because it will take time to implement the criteria. Prioritize prospectus disclosure before doing the website disclosure. Include top management for strategic considerations.
  - Christophe said it's important to start with the right people who can explain exactly what is required. Policies need to be approved by the board and this time requirement should not be underestimated.
  - Amy noted that not everything needs to be perfect in the first version. CSSF will be relaxed at looking at prospectus changes and high level will be okay for now.

- *How can SPTF SIWG be useful in helping you implement the SFDR?*
  - This working group can start compiling practical examples. Justina Alders of Triodos noted that shared experiences are useful, especially on quantifying sustainability risk
  - How can we ensure that there is adequate alignment with certain standards as we have as a sector?
    - There might be some indicators that are relevant beyond the ones included that are specific to the sector
    - Will have to monitor how the UK addresses SFDR (working on something similar but more targeted towards UK firms)
  - Rita of Incofin noted that the Universal Standards are more robust than the guidelines mentioned in the regulation. How can we as a financial inclusion sector show the efforts that have already been done over the years without being forced into a framework that is general and will only weigh the ESG scores of the funds against the general framework that is not linked to the Universal Standards?
  - Participants noted that they want the SIWG to map the SPI4 indicators to the technical standards which were published on February 4th and will be ratified in the next few months. We should lobby to have the Universal Standards as accepted for this disclosure, given they are more rigorous than what is expected in the OECD framework.
  - **SIWG poll**: In a poll of participants during the meeting, 22% said they think the SIWG would be helpful in providing a platform for exchanging shared learnings in implementation, as well as preparation for compliance. 15% of participants said they think the SIWG should be lobbying for the Universal Standards at the EC level.

Update on responsible covenants during COVID-19

- Frank Streppel of Triodos noted that we are still facing questions about COVID-19's impact on clients and the portfolio quality of investees.
- He reminded the group that SIWG updated its responsible covenants document in September 2020 to account for these issues during COVID-19. The document, **available here**, can be used as a reference point and has definitions of common terms, approaches on how to handle breaches, responsible monitoring and data collection, forecasting, and stress testing.

Next steps for Client Interview Tool discussions

- Lisa Kuhn, an SPTF Consultant, walked through the lessons learned from SPTF's roundtables on customer insights gathered from the COVID-19 Client Interview Tool:
  - The shock was severe:
    - 85-95% of clients interviewed reported being in a worse or much worse financial situation than before the pandemic.
    - More than 50% of clients overall experiencing food insecurity—as much as 75-85% in some markets—with 30% reporting hunger
  - Financial service providers helped many:
    - The majority of clients turned to savings as a coping mechanism
    - The moratoria and restructuring/rescheduling helped

    - Those FSPs that continued to lend during the lockdown and early stages of re-opening were appreciated and even grew
  - The effects of the crisis are going to be long-lasting
    - 80-90% of clients were still highly vulnerable in November
    - The percentage who had used 3 or more coping mechanisms rose from 7% in July to 21% in October/November.
    - The mix and trends in coping strategies varied from context to context, but most markets saw an increase in borrowing—both informal and formal – or sale of assets in combination with savings withdrawals and stopping loan repayments.
    - Majority of clients' incomes have not returned to pre-COVID-19 levels.
  - Clients are emerging with weakened resilience to face future shocks: lower incomes, depleted savings, social networks tapped out
- Next steps for addressing client vulnerability and diversity of experience (*Financial Service Providers*)
  - Collect and monitor segmented data on what's happening with specific groups of clients
  - Segment and analyze operational and portfolio data regularly to detect stress in sub-segments
  - Offer flexible and customizable products
  - Support client business adaptation
  - Savings campaigns
  - Offer flexible repayments and debt relief as necessary
  - Talk openly with investors about how your clients are doing and how you are responding
  - Invest in or expand digital service offerings and/or expanded agent networks
- Next steps for addressing client vulnerability and diversity of experience (*Investors and Donors*)
  - Talk with investees about what is happening with clients and how they are responding
  - Fund data collection initiatives and share data with other actors
  - Fund initiatives by investees to support client recovery
  - Give FSPs flexibility to respond to changing client needs and support sustainable recovery—even if it impacts the bottom line in the short term.
- The SIWG is creating a sub-group focused on identifying strategies and measures that could be taken by the industry – either as individual actors or as a group – to mitigate client vulnerability and thereby increase the resilience and health of the sector. **If you're interested in joining the sub-group, email allyryder@sptfnetwork.org.**