ESG know how: Regulation

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AVIVA INVESTORS

The below table is intended to give you a high-level overview of some of the changing ESG regulation and the impact it could have on your firm

What is changing?	How is it changing?	What will it mean?	When does it change?

Sustainable Finance Disclosure Regulation (SFDR)	• Covers EU collective investment funds, segregated mandates, pensions, and unit-linked funds, also financial advisers.
	• Firm-level disclosure on integration of sustainability risk, consideration of principal adverse impacts of investments, and remuneration.
	• Product providers also to make product-level disclosures (e.g. in prospectus or key facts) reporting on integration of sustainability risk and potential impact on returns, and consideration of adverse impacts.
	• Additional requirements for products marketed as sustainable to make clear how the claims can be measured and assessed. Two new categories:
	  • "products promoting environmental or socialcharacteristics" (Article 8) and
	  • "products with a sustainable investment objective" (Article 9)
		• EU-based Advisers will need to set out how they approach sustainability risks and adverse impacts in their advice.
		• For EU-domiciled products, and for many UK products where providers apply the rules voluntarily.
		• Huge amount more information about firms and their products. Advisers will need a way to identify those that best meet clients' needs.
			• First obligations from 10 March 2021 for EU states. More detailed "Level 2" rules and disclosures will apply from 1 January 2022
			• UK government still expected to bring forward similar provisions post-Brexit and we await details from HM Treasury and the FCA

Suitability test (MiFID II)	• Asking about sustainability preferences of clients to become a mandatory requirement of the suitability process for EU advisers and portfolio managers. • Sustainability preferences" defined by reference to a minimum proportion of taxonomy-aligned investments, investments defined as sustainable under SFDR, or with limits on the principal adverse impacts of investments (again, as set out in SFDR)	• Evolve processes to include clients' sustainability preferences, match them with appropriate products, and reflect them in recommendations.	• Rules to apply from October 2022. • UK expected to bring forward equivalent rules
Changes to key EU Directives	• Rules in key directives (UCITS, AIFMD, MiFID, IDD, Solvency II) to add requirements on integration of sustainability risk into governance, organisation, investment processes and product governance.	• Will significantly raise regulatory requirements on sustainability for whole market. (ESG integration and risk management in effect mandatory)	• Rules to apply from October 2022.
EU Taxonomy	• Provides definitions of what counts as "environmentally sustainable economic activity". • Need to make a "substantial contribution to one of six environmental objectives: (1) climate change mitigation; (2) climate change adaptation; (3) sustainable use and protection of water and marine resources; (4) transition to a circular economy; (5) pollution prevention and control; and (6) protection and restoration of biodiversity and ecosystems. Also need to do no significant harm to any other objective. • Products caught under SFDR must report how they use the taxonomy and the % of investments aligned with it, or make a clear statement that it is not taken into account.	• Should help to clarify what is and is not sustainable and will inform product disclosures. • Also links to one element of the revised suitability test (see above).	• First disclosures (focussed on the two climate change objectives) from end 2021.
Sustainable benchmarks	• Two new categories of benchmark have a standardised methodology (Paris-aligned and low carbon). • All benchmarks will have to explain how ESG factors are reflected in the benchmark (or explain why they are not) plus a statement of how they align (or not) with the Paris Climate Agreement.	• Comparison of ESG performance against a product's benchmark will become clearer.	• New benchmark methodology in force. • Other BMs report from end 2021
Changes for UK pension schemes	• 2019 changes required schemes to set out how they take ESG factors, including climate change into account in their investment policy. Reporting on implementation began in October 2020 • Government will require mandatory TCFD (climate risk strategy and disclosure) for pensions from October 2021. • Pension Schemes Act 2021	• Clearer information for pension savers and advisers. • Increased pressure on pension providers to increase sustainability of offering.	• 2019 changes already in force. • TCFD disclosure from October 2021.
UK TCFD reporting roll out	• Government and FCA have committed to making TCFD climate risk disclosures mandatory across the UK financial system. Listing rules for UK listed companies have already been amended and consultations in 2021 will make disclosures about their products mandatory for asset managers and life insurers.	• More information from companies and product providers about their climate risks and strategy.	• Listing rules changes apply from 1 January 2021, product disclosures from 2022

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