SRI Services response to the Investment Association's consultation on Sustainability and Responsible Investment

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From: Julia Dreblow, Director SRI Services and founder of SRI fund database tool Fund EcoMarket.

Hello Jess,

I hope all is well with you?

Here are a few thoughts on your beautifully presented paper which I hope you will find helpful when taking this forward:

Q4. Definitions, here are some thoughts that also cross over with subsequent questions.

- I have concerns about the use of the term **'sustainable returns'** as many in our industry to not understand the similarities and differences between 'financial' and 'environmental' sustainability.
- **Stewardship / Active Ownership** is potentially misleading. Active and Passive mandates can and should both 'do Stewardship/Responsible Ownership'. A more common term would be Stewardship/Responsible Ownership.
- **ESG Integration** is about 'integrating ESG factors as part of standard financial analysis' – not 'alongside it'. I have moved away from using this as a label now on Fund EcoMarket as most fund managers now say that 'do ESG Integration' – but their strategies range from 'extensive and well thought through' to 'nothing/greenwash'.
- **Sustainability themed** funds do not necessarily have sustainability related 'objectives' as this has compliance implications. This should more usefully be referred to as 'aims/themes/policies or strategies'
- Be careful with the link between **Sustainability and Negative screening** – ethical funds typically blend a wide range of issues and often combine both positive and negative criteria. They may or may not be sustainability led (that depends on the fund strategy and policies). The examples you give within B1 are indeed 'ethical' issues.

- **Positively Managed** Investment Approaches also often also have negative criteria, often combined with 'best in sector' stock selection. Such strategies are not necessarily 'stand alone'.
- **Thematic funds** often have ethical exclusions. (You should note crossover between strategies).
- **Best in Class** – this is often used alongside other strategies. Your example of 'tobacco' does not work. Decent funds in this field would always avoid tobacco companies even if they have some positive attributes.
- **Impact** – yes, the dual objective references are right, but be aware impact measurement is regarded as imperfect so the IA should be careful. Suggested draft definition - 'Investing with the express intention of delivering specific positive, measurable environmental and, or social outcomes'.

Q5 I do not follow the logic regarding the need for two labels 'Sustainable Investment approaches' vs 'Sustainable funds and mandates'. Could these be combined?

Q6 See above. Also:
-The split between **'ESG Integration' and 'Responsible Ownership'** is right but presents problems. (I previously had this on my site and agree the these two approaches exist and are separate.)

- My concern is that ESG is in high demand (eg via RFPs) so most managers now says they 'do ESG integration' (although most probably do little). If this area is not 'policed' it will be problematic, so proceed with care. RO may be similar but I do not hear as many comments about that area.

-Separating into two strategies is problematic as they are often two sides to the**'negative' and 'positive'** same coin. The main difference between them is often marketing / positioning. This is why on Fund EcoMarket I user terminology such as 'Has policy on xyz' (for example: 'environmental pollution' – a fund may say they 'avoid companies with poor practices' or 'favour in companies with higher standards'. The outcome may be the same.
- Regarding **impact** – the IA should note that many funds aim to and do help deliver positive impacts though holding investments in 'better' (higher ESG standards) companies. Their benefits are not necessarily able to be sensibly measured however and some highly regarded 'positive' fund managers are reluctant to use this 'label'. Many 'quality' managers (and others) also have deep reservations about the quality of data in this area - and investee companies' ability to supply sensible data. These represent real risks for an otherwise hugely welcome sector. The expectation is that this is likely to improve over time. Notwithstanding related concerns, with regard to a specific label (see Q4), **'intentionality' and 'measurement'** are widely agreed core features of this area.

- Be careful about using these headers as labels as in practice strategies are often **multifaceted** (largely because companies are complex and client needs vary). As such, many of the best run funds would need multiple labels. If this were not possible this could lead to the dumbing down of the sector / gaming the system. (IA needs to talk to fund managers who are experienced in running these funds).

Q7 See above. The labels 'positive, thematic and best in class' are useful but need to be tidied up and caveated (as explained).

Q8 – additional comments

Areas of concern:	**Areas welcome**

- References to **'ethical investment'** are confusing in places.
  ○ Be aware many/most IFAs and media call this entire area 'ethical' (although I prefer SRI as do many others).
  ○ You need to be careful with references to 'ethical' in the pensions market material (ESG) and theoretically 'non-material' (ie ethical/values led issues) are treated separately in the new rules – because of a focus on materiality.
- References to **'sustainability'** are unclear in places. Be aware people often mix up 'financial sustainability' (that they are very used to talking about but which may ignore ESG) and 'environmental sustainability' – which is about recognising the need to use resources carefully, future generations etc. The two are of course interconnected, but similarities and differences should ideally be articulated.
	- The 'oversight regime' idea is a good one – but it would need to be independent in order to work.
	- The use of labels rather than reclassifying funds into a single sector is welcome:
	  ○ as SRI funds are too diverse to be brought together in a single sector
	  ○ 'conventional' funds are increasingly integrating ESG so where would the IA 'draw the line'?
	  ○ It may be best for the IA to develop a solid 'basic' label system (in collaboration with the BSI, EU, industry experts etc) and leave more granular, market specific work to others.
	  ○ Note the Financial Express label 'Ethical/Sustainable' could work for the IA also (or similar – if it is to be kept simple). This could be based on what the IA already does when it collates (ethical fund)

- I’d encourage caution in your references to **Impact Investment**. If ‘social/environmental impact’ is to be in stated fund **objective** this needs to be quantified and disclosed in literature (an FCA requirement) however again, although it is improving the data in this field is imperfect and so could lead to mis-selling risks/claims. This relates to the fact that the impact field is hugely positive, but immature and ‘increasingly mainstream’.	data for reporting in its current form. - I welcome your call for greater transparency/disclosure and the idea of agreeing definitions if possible - although this would benefit from additional work.

Q9. A label or labels could be useful, but it would depend on its purpose. The problem is that at present we have too many (not too few) often informal ‘labels’ and that they are used differently by different people. The IA may not be well place to sort this out because of their narrow membership base (ie not pensions, not IFAs).

The IA should work with both industry and the BSI and the EU on this. They should be careful that their work in this area does not risk hampering useful innovation or setting rigid rules that mean fund managers either hug a new pseudo benchmark or are reluctant to respond to client’s often diverse needs.

Q10 See above. In general terms, the IA is well placed to collect data and report on it but do not cover the entire investment chain. If this were to proceed (and it could be a useful reference for all markets) it should probably be kept broad and open / principles based and with sufficient independent oversight to ensure it is not ‘gamed’.

Q11 Yes, at first. It should be tested on a voluntary basis to ensure it fits with those with experience in this field. Noting that some may prefer the clarity of obligatory requirements (particularly if they do not understand why this area has emerged to be so dynamic and necessarily diverse).

Q12 (A decision for members)

Q13 See Q5. I do not follow the logic regarding the need for two labels 'SI approaches' vs 'Sustainable funds and mandates’. Could these be combined – with matching criteria?

Q14 (A decision for members)

Q15 The 'measures of success' (p12 - number of funds using this label, and fund inflows). In an ideal world yes - these would be right – and this may be the only option. But in practice there is a risk of clustering around minimum ‘entry standards’. There would also need to be rules around sub funds, different units etc.

Q16-32 (for members – although I’d be happy to share opinions.)

I hope you find this information of use.

With kind regards,

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