SRI Services response to 'Financial Conduct Authority - Sustainability Disclosure Requirements (SDR) and investment labels' questions (DP21/4), published November 2021

https://www.fca.org.uk/publications/discussion-papers/dp21-4-sustainability-disclosure-requirements-investment-labels

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Introduction

There is much excellent material in this paper and I am delighted to offer comments in the spirit of aiding 'discussion', highlighting issues and offering suggestions to aid rapid progress. My suggestions will no doubt need to be finessed – but will hopefully aid your journey.

The scope of this project could, in my view, vary significantly. For its next stage I would like to see the possible parameters (scope) that you have in mind. For example, might we be talking about every aspect of every fund – or focusing on funds that put themselves forward as 'sustainable' (or similar) only?

Either way, I support (endorse and would encourage) the premise that transparency is largely the key to success in sustainable investment and driving change in this area – and that 'guardrails' rather than extensive prescription are the way forward.

About SRI Services

I am the founder of SRI Services, a specialist business that focuses on helping intermediaries match client aims to retail sustainable investment fund options. I have focused on retail sustainable investment since 1991, and worked full time in the area since the late 1990s. SRI Services has been running for 12 years. Our main 'product' is the Fund EcoMarket a 'whole of (regulated, retail) market' fund database – a free to use, open database tool that classifies/labels all relevant funds. Information is supplied directly by fund managers. The tool is 'supported' by 21 fund management groups. Our mission is to change the way people invest by making it easier to bring environmental and social issues into investment decision making.

There is more about SRI Services in the Appendix, but in brief our information is mainly for financial advisers (to use with their clients) – but is also used by other intermediaries. It allows users to research and explore fund strategies – and generate client reports. There are filters which cover the issues funds consider, the approaches and methodologies they use, their responsible ownership attributes – as well as generic filters such as product, geography and asset type. We use 'real world words' and avoid jargon as much as possible to help our users (all filter options are explained with 'hover over' text).

Fund EcoMarket user data

Google Analytics tells us that our database has had over 53,000 'unique users' over the last 5 years (19,000 in 2021). We know from the search data that by far the majority of enquiries are generic financial planning filter options (eg OEIC), or relate to specific 'issues' or company/industry types (eg represented by both our SRI Styles (eg Sustainability Themed) and 'Policies, issues and themes' filter options (eg Sustainability policy, Avoids coal, oil and gas majors etc).

Although our system does not map directly to Figure 3 we can see that only a small number of our users look at 'methodology' type filter options. In fact for 2021 the first 'methodology' type options are ranked 86 and 87 – 'Negative selection bias' and 'ESG integration strategy' – both used under 200 times. Our 'Top 100 searches' from 2021 are in the Appendix. This relates to over 42,000 'events' (clicks).

This experience has shaped the input below.

Summary of key points

1. For most of the questions below I have put '**consumers who care'** centre stage as I believe it is their needs we must focus on serving. This means we should focus on how relevant clients think, not how the investment industry sees things. I recommend the FCA seeks to further explore their thought processes, interests, fears and what they believe constitutes 'greenwash'. You will find that their views vary. Many will favour exclusions, most will be interested in 'real issues' and few will understand stewardship or be industry constructed methodologies (although many will probably agree with the aims and purpose of both).
2. We need to cater for the full range of relevant funds and the environmental and social issues they cover – making it clear **what** issues a fund considers and **how** they approach each issues.
    I. We need to reflect and encourage (not shut down) diverse, dynamic, new and old strategies – in order to solve the problems and reflect different client opinions.
    II. To do this we need a wide range of methodologies, which will also help reach a greater number of listed entities and guard against bubbles. Focusing on 'transition' (and its subset 'alignment') is not appropriate. These speak to 'how' a fund works (which elements of the investment community focus on) rather than 'what' is being considered, what is held in the fund - or what is its 'purpose' (which individual clients are more focused on.)
3. I disagree with the view that this is about 'end investor training' – it is the investment community that needs to upskill. Trying to upskill clients is looking down the **wrong end of the telescope.** Two reasons:
    I. We have proven largely unsuccessful raising basic financial awareness in the UK – so focusing on upskilling the public on this would be a major headache.
    II. We need to take responsibility and recognise it is **our job to create products that can be understood,** not the other way round. The investment community has **failed to take account of 'real world'** issues for too long. Clients are often ahead of us here. We need to listen and learn from others – recognising that our **methodologies are only a means to an end.** Real world issues need to be our starting (and end) point. This would also help improve trust.
4. **Why figure 3 structure won't work**. Figure 3 highlights many of the useful fund approaches that are high profile today, particularly in the climate investment arena. It is not however flexible enough to cope with the full range of sustainability issues, it is also not client friendly and does not cater for other strategies – such as funds that specialise in only environmental issues or only social issues (many of which have a valuable role to play). You also need to be mindful of the responsibilities of investors with strategies that use to earlier/other methodologies – and the fact methodologies will continue to change over time. There are also potentially serious implications with a regulator to labelling some providers as 'responsible' – and by implication others being 'not responsible'. There are better ways of encouraging higher standards. Questions 2 and 4 and Appendix 1 'A possible pathway' should help.
5. The work you did on the 'principles' - **Dear Chair** letter - was excellent. Future work should reflect this ethos. (If there has been a lack of specific criticism that should probably be read as 'a success').

6. If we can get the language right – focusing on 'real life issues' we should be able to help shift the mindset of all investment professionals – which is ultimately what needs to happen. Almost everyone will need a knowledge of sustainability issues in order and identify the part they and their companies can most usefully play ('purpose') in helping to address meet their clients' needs ever better.
7. Sustainability information should be **as high profile as possible** if we are to play our full part in driving the necessary shifts. This means it should be embedded in **all existing client facing literature**. Levels of detail will necessarily vary, but no document (required by law) should be allowed to ignore sustainability entirely. Some will simply tell readers where to look for sustainability information, others will include a list of criteria / key aims – and there will also be a need for detailed policy/strategy explanation document also. We need to **ensure all clients are aware** of the relevance of sustainability issues and be able teo see how a fund deals with them. This will both help **raise standards** and where necessary **redirect capital**.
8. You should not put too much emphasis on recently designed metrics, methodologies or collaborative initiatives yet - no matter how useful they appear to be. Further evolution is inevitable for '**early stage'** work. The focus should be the 'real issues/challenges' (eg reducing emissions, ending deforestation, improving equality). Initiatives should be highlighted as example/preferred means of achieving these goals. (Maybe something like 'Preferred Methodology Given Current Capabilities'? PMGCC?)
9. There must be **no chinks in the chain**. This information must get through to end investors and must be seen as 'business as usual' from manufacturer to client. (We can discuss further – see notes on intermediaries in appendix).
10. The FCA should **focus on what only a regulator can do**, which I'd suggest would include requiring transparency and agreeing some core disclosure structures and definitions. Aim to keep the 'rules' as simple and flexible as possible is important as is reflecting or using other initiatives where possible. Reducing duplication and contradictions will help keep costs down and benefit all – providing core aims can be achieved (eg addressing climate change).
11. **To replace Figure 3**, I am suggesting a structure that mostly highlights key issues a fund focuses on . This would be explained in a corresponding disclosure grid or report. Top level classifications could be '**Basic, Hybrid or Sustainability themed'** with a supporting 'image' along the lines of the following:

Sustainability	Environmental	Social	Responsibility	Exclusions
Meets the criteria of the highest sustainability, environmental and responsible ownership fund standards as described by the FCA here.				Armaments Tobacco
We assess companies in line with xyz methodology (expand) eg alignment, transition, thematic… You can find out more about how this fund works here.				

List of Appendices:

1. **A possible pathway**
2. **SRI Services graphics illustrating ways of describing this fund market**
3. **About financial advisers**
4. **About clients**
5. **'SRI Styles' Directory web page text**
6. **Explaining the sector to newcomers**
7. **A 20 year old media release**
8. **Further comments on content**
9. **About fund diversity**
10. **Top 100 searches on Fund EcoMarket 2021**

Ps please note I am 'timed out' on this.

The presentation of the responses below would benefit from extra time in places (and may include some duplication). Please contact me if you would like to discuss or clarify any aspects.

1. **What are your views on the tiered approach set out in Figure 2? We welcome views on any concerns and/or practical challenges.**

This is good. A structure of this kind should not be controversial in my view.

Comments are:

- The way in which **'Disclosure level 1'** is presented should be high level and not overly prescriptive as fund strategies are highly diverse. (The FCA should set requirements such as comprehensiveness, brevity, use of plain English). A list of high level criteria should suffice.

- **'Disclosure layer 2'** Transparency is a crucial element of this work so no strategy information should be hidden from end clients ('why would you?'). This may be a long document, which would be entirely appropriate if required.

About Availability

I agree level 1 would be more client facing and level 2 would be more for the investment industry but both documents should be readily available to all parties.

This is because there are many investors with a deep understanding of sustainability issues who will want information that could not sensibly be covered in a brief summary. (See appendix 3 About Financial Advisers)

About the content:

- The regulatory emphasis should focus on funds being 'open and transparent' – ie saying 'what they do' . If metrics or methodologies are used (and presented to clients) they must be fully explained, with reference to their purpose and the issues they seek to address.
- Disclosures must require both the 'issues' a fund deals with and the 'approach(es)' they apply to those issues to be explained to clients (ie drivers of stock selection and stewardship).
  - Strategies rightly vary, but clients must be able to understand them from the information the manager publishes – to guard against incorrect assumptions being made.
  - Even for the first tier there will need to be significant variations in the length of text as some funds cover more issues than others.
  - This needs to be flexible in terms of content because different strategies suit different clients. **Only a client can decide what suits them** – and they can only do this if they know '**what**' a fund strategy considers and '**how**' it deals with issues.
  - The focus should be on describing where a fund will and won't invest. Stewardship flows from this.
  - This should be tested against your targeted audience which is 'clients who care'. The opinions of those who do not care are not directly relevant here.

- These should indeed build on key initiatives such as TCFD but also 'leave the door open' to the likelihood that further initiatives will appear and may usurp existing initiatives. (Nothing in this area is time proof.) ie - 5 years ago we would not have used TCFD as a reference point as it did not exist. ISSB and TNFD are not settled yet but will probably be very useful. Keep in mind that eg the SDGs replaced the MDGs – and that funds can not switch reference points easily if they are part of their core offering (as a product will have been sold on a particular basis).
- AFMs should be allowed to use different terminology in levels 1 & 2 as level 2 will necessarily be more specific and potentially technical. (Eg Level 1 might say 'we avoid major polluters' whereas Level 2 should define what they mean by 'major' and 'polluters' and how they deal with these issues.

- The FCA should encourage industry bodies / marketeers etc to design explanatory and promotional materials and templates that aid their members – whilst being mindful no single body speaks for all investment professionals. These should encourage (not belittle / disincentivise) well thought through and often complex strategies as the issues we face are complex.

2. Which firms and products should be in scope of requirements for labels and disclosures? We particularly welcome views on whether labels would be more appropriate for certain types of product than for others, please provide examples.

Also see q10 and appendix 1

If the focus of this paper is 'end (retail) clients', it follows that **all firms that serve 'end clients'** – directly or indirectly should be in scope.

Increased sustainability **disclosure** should be 'across the board' (products and firms) in order to facilitate rapid system wide changes.

Where?

This information should be embedded or linked through to all core existing literature – in order for it to become 'business as usual'. Additional materials are also like to be required.

What products?

Labelling should probably focus on funds that make claims about their sustainability credentials although there would be a strong argument for flagging 'low or no' sustainability credentials for other products.

Labels appear to be very well suited to **retail funds** and similar regulated products intended for clients who are less likely to have baseline knowledge about investments but may be very interested in environmental and social (sustainability) issues.

- I would suggest the starting point should be mass market retail funds. (More complex products, portfolio services etc might sensibly be considered in a second phase.)
- Output should draw on the experience of well established funds (from when 'greenwash' was not widely regarded as 'an issue' – and rough edges have been smoothed through exchanges with clients.)

Labelling for **'firms'** – we need to be careful.

- A regulator 'labelling' a fund management company as 'responsible' or by implication for others 'not responsible' could have significant **unintended consequences** – some good, some bad. (As desirable as this sounds I am not sure how it would work).
- We need to be careful with language. Labelling a firm as 'responsible' is very different from identifying their 'responsible ownership' attributes.

My inclination is that the FCA should highlight (and encourage uptake of) good practices and desirable behaviours – such as being an FRC Stewardship Code signatory. For the benefit of clients these must be explained ('which means that…').

Aspects of the 'responsible ownership' ethos should become part of the formal (standard) regulatory regime and 'licence to operate' where deemed necessary. (I believe this is underway to some extent with requirements such as transition plans and TCFD reporting).

What would make a good label?

- Client friendly words, not industry jargon.
- Make it clear that funds focus on different real world lissues
- Have the right tone. Not judgemental, divisive or able to be disagreed with.

At present the focus should remain on **disclosure.** The ethos of the SRI principles / Dear Chair letter should be retained.

Over time you/we should probably look to flag concerns about companies with poor sustainability related practices that may represent greater risk to the system – ie go beyond labelling and disclosure to better address systemic risks.

Why focus on 'mass market' retail first? In part because that is the sector which represents most people. But also because that market is most likely to be adversely affected by Greenwash - or 'cry Greenwash' - when they are surprised by where a fund invests.

- Personal levels of wealth should not be confused with knowledge of - or interest in - sustainability issues, such as climate change. I doubt they correlate – or it may be that they are inversely correlated for significant minority. ('People who care' are presumably less likely to have focused solely on the accumulation of wealth).

Providers of more 'sophisticated' products are more likely to say this is impossible than others. Their motivations should be explored as it is more likely that they do not know how to – or need help. There should be a general assumption that 'disclosing something' on a well-informed / best efforts basis is preferable to 'doing nothing'. (MPS etc should either receive a lower label / disclose less and expect to be seen as doing less - if they can not articulate sustainability characteristics, or say what they can about a proportion of assets they could describe on a 'look through' basis. This should not however be allowed to become a mammoth task. Managers either are or are not committed to addressing sustainability challenges).

Disclosure should be across the board.

Example text:

Disclosure level 1:

Funds (and similar) to say 'what they do' in this area. If the answer is 'not a lot' that is acceptable (for now) – but they must disclose this in order for all clients to be able to make informed decisions (and reduce risk of markets being distorted by false assumptions / clients being misled). The focus should be on enabling clients to identify options that meet their expectations.

Providers. Firms should also say what they do. The key messages to outline 'what they do with regard to sustainability' (not expressing alignment to a label). They should describe the core issues that they consider and indicate how they deal with them. The framework would need to be flexible and focused on encouraging higher standards (whilst ending false or poorly informed statements).

Additional issues to consider for more complex products:

- tax related issues (which can be divisive).
- Variations between asset types such as equities, bonds, property etc

Disclosure level 2:

A suggested (basic) structure

A client friendly disclosure matrix along the lines of the following could work (although this could work equally well in report form).

This would direct fund managers to articulate specific environmental, social and sustainability (which combine E&S) issues they consider – split between avoidance / positive selection (impact) / engagement (stewardship) . ('Labels' could vary but must not be leading or too complicated).

There should be no obligation to complete all boxes, but there should always be the obligation to be 'true, fair, not misleading'.

	Environmental	Social	Sustainable
Avoid (Exclusions)			
Support (Positive / impact aims)			
Engage (Stewardship)			

3. **Which aspects of these initiatives, or any others, would be particularly useful to consider (for example in defining terms such as responsible, sustainable and impact) and how best should we engage with them?**

I am broadly supportive of most of the initiatives that have been launched recently – however none should be confused with what a regulator can or should do.

Terminology has tended to evolve over time and I am concerned about the FCA potentially using terms fixed in a point in time (now) - which will soon become history.

I have learned over time to favour very open definitions such as: 'sustainable investment funds pay significant attention to both environmental and social issues' – although almost uniquely – the concept of sustainability generally needs further explaining.

I have written / helped write many glossaries etc over the years – the following (slightly dated) pages are current on our websites. These are intentionally brief (I'd be happy to discuss further):

- https://www.sriservices.co.uk/about-sri/jargon-buster
- https://www.fundecomarket.co.uk/help/getting-started-in-sri-and-esg/jargon

Some comments about glossaries:

- They vary depending on the author's experience and intended audience
- They have to run a fine line between explaining financial and ESG (type) words -and how the two work together. In brief – clients normally need help with financial industry terms whereas our industry needs help with sustainability concepts. Problems can occur when documents are collated or approved by people with little practical experience in sustainable investment. (They tend to overstate their positions – reflecting how far they feel they have come.)

- Meaning can vary in different countries / may become dated / common usage shifts

4. **Do you agree with the labelling and classification system set out in Figure 3, including the design principles we have considered and mapping to SFDR? We welcome views on further considerations and/or challenges.**

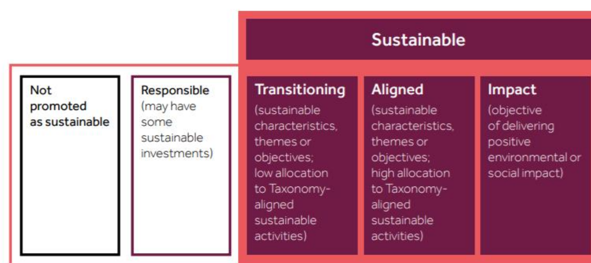


Figure 3: Potential approach to a sustainable product classification and labelling system

Note: The five blocks in this Figure represent potential categories of product in the classification and labelling system. Each would be supported by clear definitions and criteria

Opinion on Figure 3.

Why figure 3 structure won't work. Figure 3 highlights many of the useful fund approaches that are high profile today, particularly in the climate arena. It is not however flexible enough to cope with the full range of sustainability issues, it is also not client friendly and does not allow for funds that focus specifically on only environmental issues or only social issues to be represented (many of which have a valuable role to play). There are also issues with what it might mean for a regulator to label a provider as 'responsible' - the implication for those outside of that circle could be severe. There are better ways of doing this.

Appendix 1 – also see 'A possible pathway'.

A structure like will not be able to adequately reflect funds that hold larger companies that display elements of leadership (impact) as well as areas of controversy / poor practices elsewhere (where hopefully investors will be encouraging them to 'transition').

The use of industry terminology risks greenwash allegations and undermining trust.

> Issues such as this put intermediaries in a difficult position and deter sales because most advisers could not explain either the concept of why specific (often surprising) holdings are deemed allowable.
>
> Pension members are less likely to raise concerns as fewer are actively engaged in fund selection at present (this may change).

Some of the misunderstandings I have observed in our recent meetings include:

- The chart is seen as a '**bad to good'** continuum (along the lines of the 'spectrum of capital' which implies its ultimate 'best' use is philanthropy – which I disagree with. The purpose of investment is to make money for investors - as that is how we attract money / make money and effectively incentivise individuals to help solve problems).
- There was a view that '**transitioning'** is temporary – and that companies will exit that group. For some this will be true, for others it is more likely that their standards will not rise as fast as the necessary shifts require so they may be 'in transition' for a long while.
- There appears to be little understanding of what funds that are currently marketed as '**aligned**' do. Many hold companies that clients view as deeply controversial/undesirable. (Not retail friendly). The concept is good – the awareness (and therefore risk of funds being called greenwash) is less good and unlikely to change for individual investors.
- In essence 'aligned' and 'transitioning' describe the same process (companies that are heading towards becoming sustainable).

- This suggested structure is seen by some as a reasonable representation of what we have today however there were questions about how a manager would run a fund to a defined remit such as some of these. (Most funds mix company types for investment reasons and no fund would want to be forced to sell a company because it had become too aligned or impacful.)
- Additional questions included: should this be hard baked into regulation? Is this what we want/need? Do clients understand it or will they see some of this as greenwash?
  - I'd suggest that although highlighting and defining attributes such as these has value they do not work as fund labels because of what funds actually do/ or the nature of investing in a basket of often complex companies.
- Different people seemed to have different concerns about this - which implies it would not be able to be quickly fixed
- The implication that this is a 'bad to good' spectrum underplays the importance of transitioning – which is crucial as it is where most companies and funds currently sit.
- The term 'sustainable' implies the activities carried out by the funds are (literally) sustainable (ie able to continue ad infinitum) which is untrue & therefore open to greenwash allegations – even if the intentions of the fund manager are good.
  - This is perhaps why using less emotive terms like 'Article 8 or 9' works as it creates a straw man that can not be directly criticised because it is the regulators own construct.
- There is no explicit mention of 'harm' (DNSH) which is often what a lot of clients and intermediaries are most interested in.
- Attempting to map Articles 6, 8 & 9 would be broadly welcomed however use of Art 8 is so wide/diverse that it risks undermining the system / confusing clients.

Additional feedback:

- The labels do not separate out 'environmental' and 'social' aspects. Companies and funds may be strong on one but not the other. We should not imply such companies have no place in this field or risk misleading investors so that they expect companies and funds to be good at both (or neither).
- The term **'impact'** needs to be handled with care. At present we mostly need transition activity.
- '**Responsible ownership**' should by now be integral to all fund strategies (comply or explain), not separate, not optional. Responsible investment attributes should be flagged / promoted / encouraged – not binary and not as an alternative to these other descriptors.
- Be careful with the term **'sustainable'** as it implies something is genuinely sustainable (ie risks being hostage to fortune / greenwash allegations). Referring to sustainability attributes, methodologies, aims etc is less of a blunt instrument. 'Sustainability themed or focused is better.

  Note – it should be recognised that if you go live with these (or any label) they will develop a life of their own and a corresponding set of expectations.

Some suggested do's and don'ts

- Use Plain English – words 'interested individuals' will understand and are able to be matched to their opinions. (Do not focus (too much) on disinterested people – they won't be buying these funds or worrying about them being 'greenwash').
- Use true representation of what funds actually do / can do (the reality of holding 'real' and mostly imperfect companies).
- Do not risk clients being misled by funds lead with metrics and methodologies. They need to be clearer about their purpose. Metrics, norms etc help design mas market, IT friendly products but are open to greenwash allegations (which have exploded recently) if not properly explained (with caveats).

- Allow labels to overlap – as that is the reality of fund strategies (perhaps like Venn diagrams).
- Try not to use terminology that a reasonably well informed, interested client could sensibly contradict. (ie 'This fund is sustainable' is a fail. 'This fund focuses on sustainability issues' works. As does 'this fund aims to influence companies to do better' (rather than 'this fund is responsible').
- Avoid (explicit or implicit) labels that date stamp a category eg Paris – they will date
- Use existing methodologies and labels where you can but do not be afraid to do something different. If what we have now worked perfectly we would not have attracted the heavy (and often legitimate) criticism we have seen. Article 8 & 9 (in principle) work as labels as they are 'bespoke'.

Learning from other industries

What can we learn from food labelling / clothing labelling (as mentioned in meetings)?

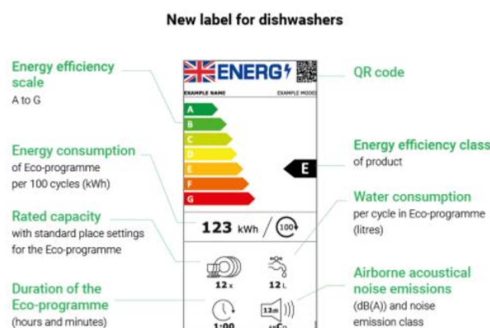
Energy labels

Energy labels have historically been discussed pretty regularly over the years as a way to help clients understand this area. This has mostly been decided against in part as it would be hard to reflect the multiple dimensions of fund strategies and sustainability issues.

Note - CISL were working on using energy labels as their baseline a few years ago – you might like to ask them about their experience.

Note the new energy labelling system below is more likely to be useful than pre 2021 version. ns at base).

https://energylabel.org.uk/for-consumers/essential-new-features/

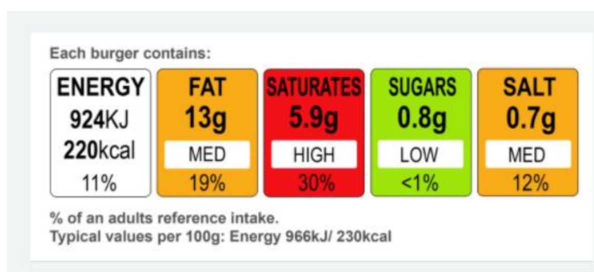


Food labels

Food labels have been mentioned more recently and may have potential.

https://www.food.gov.uk/business-guidance/packaging-and-labelling - the multifaceted nature of food labelling and requirements could be a useful model for this area.

https://www.nhs.uk/live-well/eat-well/how-to-read-food-labels/



Strengths	Weaknesses
Multi dimensional (boxes could represent different issues/approaches, with different elements of response shown in colours and numbers) Simple / intuitive / retail friendly (key feature is RAG) Scope for change over time eg data could be included / upgraded over time over time, RAG boundaries could evolve Could be supplemented with tick box list of exclusions – in this chart or separately (see Allergens) Potential complexity reduces greenwash risk	Won't work well for companies / funds on the boundaries Specific percentages are hard to measure (may need to use bands) – this layout may confuse if seen as too complex for safe use in investments now Does this work for colour blind people? Scope for misinterpretation / what if mixed message Unintended consequences eg if everyone goes for 'green' (reduced pressure on laggards, bubbles?) Too much information? (Or too little?)

Front-of-pack labels usually give a quick guide to:

- energy
- fat content
- saturated fat content
- sugars content
- salt content

Clothing labels

Clothing labelling may also offer useful input – but images typically need explanation and can open up much debate.

https://www.coats.com/en/Information-Hub/Care-Labels

Labelling System (ASTM Symbols)

The **clothing labelling** system(s) could also allow us to separate issues and approaches, gradating responses– although as shown icons such as these would probably need text also to avoid confusion (particularly as most people do not chose investments often) .

This appears to be able to represent the multidimensional nature of (actual) sustainability funds / funds that consider sustainability – if we can find images that do not cause confusion.

SRI Services labelling

Also see 'About SRI Services' in introduction and Appendix 2

We've been working to design and fine tune retail sustainable investment labels for over 12 years.

We offer a system of SRI Styles. The 'styles' describe retail fund options to financial advisers in ways that their clients can understand.

> Google Analytics tells us there have been 53,000 unique users on Fund EcoMarket over the last 5 years – to 4/1/22. Previous sampling indicates around 2/3 of those will be 'advisers/industry professionals').
>
> Our SRI Styles (labels/classifications) are amongst our most used filter options alongside searches for specific issues and generic financial planning searches (product, region etc). They have been periodically updated to reflect market shifts - and will continue to change as the area evolves.
>
> In the interest of having a manageable number of categories the groups are imperfect (and always will be). Fund strategies vary within 'styles'- and there is crossover between the styles (eg most funds consider climate change).
>
> These are important realities of classifications/labels in this area. Because of this our labels are supplemented with 188 drop down 'issues and approaches' related sub filters to help users understand strategies - plus detailed fund manager supplied text and links. (This number of filters could easily be doubled).

Our SRI Styles focus on a combination of issues (eg sustainability, environmental, social, ethical, faith related) as well as 'approaches' – particularly where there are lot of funds so splitting up the group is useful from an advice perspective.

> Some years ago we split 'sustainability' into three: 'Sustainability themed' (where there is a more clearly positive / investing in solutions / unlikely to hold highly contentious companies strategy), 'Sustainability tilt' (where funds focus on being overweight in sustainability leaders, but are likely to hold laggards also – typically alongside stewardship activity/encouraging progress), 'ESG Plus' – funds where the literature emphasises the aim to reduce risk by understanding (and managing) ESG issues better. To be relevant for our platform we expect these funds to have exclusions &/or very significant stewardship activity also – as these indicate that the fund is intended for and likely to be suited to some clients in an interest in this area.

Our classifications uniquely aim to capture what is '**actually available'** in today's fund market (across the entire market – we classify all funds we can find sufficient information on) – helping intermediaries match client aims to fund options.

You can see more here: https://www.fundecomarket.co.uk/help/sri-styles-directory

This experience informs the views below.

Suggestion for the sustainable investment market

Also see **'A possible pathway'** section - appendix 1

High level labels: '**Basic / Hybrid/ Sustainability theme'** (or focus)

Label for the key elements of each relevant fund (each subject to criteria) – perhaps along the lines of the following:

Sustainability*	**Environmental***	**Social***	**Responsible^ ownership – voting**	**Exclusions (FM to list)**
Colours: Red – little or no consideration given Amber – favour transition leaders/engage with laggards Green – invest mostly in leaders & solutions cos	Red – little or no consideration given Amber – favour transition leaders /engage with laggards Green – invest mostly in leaders & solutions cos	Red – little or no consideration given Amber – favour transition leaders /engage with laggards Green –invests mostly in leaders & solutions cos	Red – little or no activity / rarely vote against management Amber – extensive engagement and voting with most companies Green – engage when necessary / where leadership is not demonstrated	(Use of RAG could be optional) Coal extraction Armaments cos Tobacco cos Companies involved in animal testing for non medical purpose / not required by law
Insert text on metrics, ratings, caveats etc				

***FCA to set metrics –** mapping to taxonomy as far as possible

^ **Map to FRC stew code?** (signatory, near miss, far miss?)

(This could potentially be compounded to entity level also):

Example in label / image form:

Sustainability	Environmental	Social	Responsibility	Exclusions
Meets the criteria of the highest sustainability, environmental and responsible ownership fund standards as described by the FCA here. We assess companies in line with xyz methodology (expand) eg alignment, transition, thematic… You can find out more about how this fund works here.				Armaments Tobacco

See Appendix 1 'A Possible Pathway' for further explanation, which has example text and reasoning.

This would need further work, listing specific issues and measures. I'd be happy to discuss this conceptually before considering details.

5. **What are your views on 'entry-level' criteria, set at the relevant entity level, before products can be considered 'Responsible' or 'Sustainable'? We welcome views on what the potential criteria could be and whether a higher entity-level standard should be applied for 'Sustainable' products. We also welcome feedback on potential challenges with this approach.**

Mixed views.

This is a balancing act between client protection (not allowing poor funds/companies to use a label that will be undermined by parent company activity) and effecting change (which means we want to encourage everyone to come on board – even if they are at a low starting point).

We should look to consider other new (FCA) disclosure requirements that may serve this purpose eg TCFD reporting, transition statements – as well as related indicators of sound practices such as the FRC Stewardship Code. (Licence to operate?)

The following explores where an 'entity' has to meet certain requirements for a fund to be classed as 'sustainable' (irrespective of strategy).

Pros	**Cons**
This could make things simpler – shifting the emphasis from 'our starting point is what a fund manager says they do' to 'our starting point is what we know the fund house does'. This may help push fund houses to adopt whatever higher across the board standards are set as the entry point (stewardship code, GFANZ membership etc) If this were a collection of criteria (eg Stewardship Code signatories, without major compliance issues (fines?), who's CEO has committed the organisation to address climate risk and are member of/adhere to/have audited statements proving they adhere to x, y and/or z this could be a hugely effective for encouraging a swift transition. (Fund managers would have to be given due warning / a grace period to avoid backlash / expensive disruption). This could help avoid greenwash as criteria could be set that require certain company wide behaviours. The ESG market could become an effective agent of across-the-board progress. This might naturally evolve anyway – so codifying it in regulation could help to accelerate progress. In some fund houses the lines between fund and fund management company wide strategies are already blurred. Information is sometimes missing from sustainable fund literature because clients are expected to know that certain standards are applied across the board (eg ESG risk mitigation, avoidance of certain sectors). Initiatives such as the Stewardship Code (although available) are rarely considered in retail markets	If this leans heavily on Stewardship (which is likely to be desirable) this would be a tough message for retail clients. (I've been discussing & promoting the value of 'engagement' for 20 years and whilst we seem to have made good progress with intermediaries (who were initially entirely opposed) the concept has not landed well with others – particularly those who distrust the investment community – particularly when holdings do not meet expectations). This may slow progress in companies if they are not exposed to the benefits of having a trail blazing fund in their suite of options (who may be working to influence others). Bigger fund management organisations will be better placed to meet requirements – this could hamper innovation and be challenging for smaller companies and start ups. (This could be dealt with by having certain exemptions). Choosing an entry point will be difficult. It should not be commercial or able to be influenced by any particular cohort. (The profit motive should probably be removed). The level at which they set the bar will need to evolve/move up over time also. It is incredibly hard to check (or audit) how genuine statements of purpose, engagement and similar are. We can not know the seriousness of engagement strategies. Evidence (lack of progress in the 'real world') would suggest investor activity has, to date, mostly lacked teeth. (Or maybe investors think companies care more about their views than they actually do?)

6. **What do you consider to be the appropriate balance between principles and prescription in defining the criteria for sustainable product classification? We welcome examples of quantifiable, measurable thresholds and criteria**.

As this market is diverse and dynamic and will continue to evolve apace regulators should favour 'principles' wherever possible.

I agree advances will not happen without greater 'definition' however, particularly around what are desirable outcomes (and how we get to them – collectively), so with regard to the suggested grid above I would have specific requirements (eg being able to prove a fund is overweight or underweight in a given area).

Work here should link through to other initiatives and collaboration projects which will provide useful metrics.

The ethos of the Sustainable Investment Principles (see Dear Chair letter) should be built on.

Examples of why we should not be too prescriptive:

- **Codes can replace one another**– eg the Paris Agreement may/will be usurped or updated (we no longer mention Kyoto) – there may be a 'Sharm El Sheik Agreement' (although exiting users of Paris may find it hard to switch benchmarks). MDG's were replaced by SDGs, the new FRC Stewardship Code is different from the previous one (and very different from Cadbury etc)
- **Issues evolve** – deforestation is one of the earliest criteria in this field but is now mostly considered as being part of the biodiversity / nature agenda. Exclusion of companies supporting the Apartheid regime is no longer relevant.
- **Approaches go in and out of fashion** – although this area was in fact built on the three aims of 'avoidance of damaging activities, 'supporting good companies' and 'helping to drive change' (all were around in c1984,) the latter two were widely ignored externally for many years.) We have however now seen, at various times, big swings between divestment, positive/impact and stewardship. As such all should be catered for.
- We need to be careful **not to unintentionally nudge** people into a particular group as that could have unintended consequences (capital flows, reputations etc)

Examples requirements that should be able to stand the test of time (to some extent):

- Requiring fund managers to make it clear what sustainability issues the fund considers and how they deal with these issues. (How, what?)
- Requiring funds/fund managers to have a publicly available written policy that sets out where a fund will and/or will not (as applicable) invest – from an ESG perspective (this could be level 2 – or additional). This should include an explanation of how companies with both negative and positive attributes will be dealt with.
- Requiring managers to flag controversial activities to potentially interested clients/advisers.
- Requiring managers to supply both short form 'lists of criteria' (strategy summaries) and 'detailed explanations'.
- A requirement to explain (not simply name) any index, benchmark or similar that the fund is significantly reliant on
- Requiring managers to make it clear what it means to invest sustainably in different types of assets
- Requiring the explanation of deminimus / tolerance levels where applicable
- Publish voting (and potentially holdings - tbd) information

7. **Do you agree with these high-level features of impact investing? If not, why not? Please explain, with reference to the following characteristics:**

   a. **Intentionality,**
   b. **return expectations**
   c. **impact measurement**
   d. **additionality**
   e. **other characteristics that an impact product should have**

Broadly yes. They focus minds on key issues, however some are challenging if they are used out of context or inappropriately and do not always work for 'mass market' investors.

Impact has largely been the domain of the GIIN – however the concepts they highlight go to the beginning of the ethical fund movement if not well before.

The GIINs definitions, whilst useful, have somewhat split opinions as there are excellent fund managers who predate the GIIN who have concerns about how these terms are used – particularly in retail equity markets.

Some dislike the term 'impact' being used extensively in (secondary) equity markets as although impacts are real - and the relevance of being concerned about impacts is beyond question - there are questions about how much credit equity investors can rightly claim and some of the data. (These are the perennial issues relating to the benefits of simplicity and using proxies and the risks of misleading.)

That said, the contribution of the 'impact' community has been valuable. Many such funds can be seen as 'the icing on the cake' although the cake itself remains crucial;. It is therefore the context and way in which terms such as these are used that is the concern, not the fact they are used. Regulators need to ensure this is carefully managed and with appropriate caveats.

- **Intentionality,** ('the explicit 'intention' to deliver beneficial real world environmental and or social outcomes') yes, essential – but realistically we want most funds in this area to aim to deliver real world benefits, so be careful not to push this concept into a niche which implies it is not relevant to other investments – or into a corner widely regarded (by IFAs) as largely uninvestable for most retail investors.
- **Return expectations** (financial gains/losses) yes, returns are relevant to impact investment (both financial and real world). Be careful what you say however. Current common methodologies (for risk management and forming opinions around likely future performance) fail to reflect the realities of risks such as climate change, biodiversity loss and equality – any of which could hit markets at any time. We need to change the narrative so that funds that aim to help deliver improved societal outcomes are regarded as inherently lower risk as their activity can help protect the investment system. We are currently scaring investors away from funds with higher standards with risk ratings indicating 'sustainable funds are higher risk' . We are therefore directing clients into funds that hold major polluters indicating this will reduce their risk. This is a very dated view – and slowing progress. This also risks complaints arising as/when such companies – particularly those that are slow to transition – become stranded assets - and lose money for clients.
- **Impact measurement** (quantifying beneficial outcomes) . Seeking to measure impact (positive and negative) is hugely important, highly desirable and incredibly difficult to present in such a way that retail clients who are interested in equity markets will understand. It is particularly risky in equity/secondary markets as fund managers are not directly responsible for any benefits/problems. We need managers to be honest and explain often complex dynamics and tradeoffs (most retail clients would not want to make direct investments). Regulators need to encourage the focus on measurement – but not at the expense of honesty. Pros and cons should be explained to clients so that investors do not feel short changed when they have thought this through further. We also need to be collectively more honest about negative impacts (otherwise we are cherry picking).
- **Additionality** (using financial markets to enable useful things to happen that would not happen otherwise). Again, highly desirable, but potentially misleading in secondary markets. It is beyond question that helping to raise a company's share value (by buying their shares) can bring benefits (eg access to capital) – but these are rarely explained.
- **Other characteristics that an impact product should have**. Expertise (at point of buy / sell) and a genuine desire by the managers to 'do good' in a financially appropriate, properly explained way.

8. **What are your views on our treatment of transitioning assets for:**

   a. **the inclusion of a sub-category of 'Transitioning' funds under the 'Sustainable' label?**
   b. **possible minimum criteria, including minimum allocation thresholds, for 'Sustainable' funds in either sub-category?**

Withing the context that I do not agree with Figure 3 – I would entirely support the view that explaining 'Transition' (and ideally a Just Transition) is crucial.

Transition starts to get to the heart of the realities of investing in real companies. Change does not happen overnight and will take planning, but is still crucial. Parts of the sustainable investment market have often been lazy – describing companies as entirely good or bad, which few are.

Keeping in mind that our focus is interested clients (and not advisers or trustees who may not be interested) there are probably two main aspects to consider/ explain:

(a) What transitioning means (ie what reducing emissions by 7% pa means and does not mean) and
(b) What a fund does in order to align to a given metric (what is in/out)

Some additional thoughts:

Transitioning means (or must mean) that investee company operations are moving towards being literally, entirely and unequivocally 'sustainable'.

1. In other words – they no longer use finite resources (they use only renewable / recyclable resources), they generate zero (unusable) waste (including carbon/GHG emissions) and treat employees and those in their supply chain with respect so that inequality issues become a thing of the past. Understanding the benefit of this they will probably also be collaborating with others to ensure this becomes 'normal' - probably through engagement with policy makers, collaboration with competitors etc. They should also have grasped the need to correct historic mistakes – for the benefit of current and future generations – working towards becoming 'net positive'. (See Paul Polman book of the same name).

2. With regard to what funds do – as we are so far away from almost any company being able to claim a total transition (although case studies such as Orsted show what can be done) worrying about what a fund should do 'when companies have transitioned' should not be seen as a problem. And although highly desirable – the likelihood of funds 'jumping up a group' is similarly minimal (at present).

3. The reality is that the majority of funds in this sector invest in companies that are on a journey – transitioning – to a greater or lesser extent. The description given above is likely to be viewed as nonsense by many – however the reality is that at some point this will have to happen and as with other risks getting a head start on managing it is liable to be advantageous. Indeed this is why investing in 'transition leaders' is popular. In practice most funds (often for financial reasons) will tend to hold some of these companies – plus others that some classify as 'solution providers / enablers' (positive impact companies) as well as laggards they believe they can influence.

4. The label you give funds that focus on companies that can demonstrate they are on this journey (if they only invest in companies of that kind) is open to debate. I am not convinced

'aligned' or 'transition' will be understood by clients although they are important concepts that aid the explanation of funds strategies that will have exposure to assets that tick one or the other (or both) boxes.

5. As such 'transitioning' is firmly part of the 'sustainability' stable but perhaps not an ideal fund label.

6. The term '**alignment'** has emerged more recently. It can be a useful way of looking at companies, tracking and encouraging progress and explaining 'real life' company issues (the process of gradually transitioning) to clients – but again, the concept may or may not last. The alignment metric may end or be usurped, and it is not going to be easy to explain to clients – so yes, this is a valid (and useful) strategy, but not necessarily a useful label or classification.

7. With regard to '**minimum criteria'** from a retail investor's perspective – and in particular one that might be looking for greenwash because they do not trust the finance community – my view is that companies that are inherently unsustainable should not be allowed into sustainable funds. As such if a blunt label such as binary is used coal, oil and gas companies should be excluded. (I fully support the view that oil and gas companies must be encouraged to transition – but do not believe this sits comfortably in the retail universe under the simple label 'sustainable'. We make ourselves hostages – these funds need further clarification such as the word 'tilt'. (By contrast it is entirely 'responsible' to encourage such companies to change – so that label works better for such companies, although clarification is still beneficial.)

9. What are your views on potential criteria for 'Responsible' investment products?

Responsible ownership (by which I mean active stewardship, voting and engagement) is essential, but I would not want to see it as a fund classification. (It is a key element of fund or fund management company strategy, not a product label.)

From a regulatory perspective, resources may be better employed encouraging or requiring adherence to codes such as the Stewardship Code, giving examples of other desirable activities and integrating this into the wider rule book. Reference **points (such** as the Stewardship Code) should be periodically reviewed and provisions may need to be made for ineligible organisations.

AS mentioned elsewhere the FCA should also be mindful of their labelling some companies as responsible and my implication – others being 'not responsible'.

10. Do you agree that there are types of products for which sustainability factors, objectives and characteristics may not be relevant or considered? If not, why not? How would you describe or label such products?

Also see q2

There is almost certainly no investment that ESG factors will not be relevant to (the possible exception would be a very short term investment). However there may be asset managers who disagree – most probably because they do not know enough about sustainability risks. There are however undoubtedly products that are harder to describe as meeting certain sustainability criteria - where it then becomes a debate between 'simplifying the product' and having 'a better grasp of the ESG attributes or assets'.

On Fund EcoMarket we often classify such funds as 'Unclassified' (where there is insufficient information to warrant a classification) or 'Pending' where we are asking for additional information. We also have 'Limited

Exclusions' for funds with more basic strategies that may either decide to exclude a sector or indicate that they exclude some companies.

With regard to your response. I would suggest the following:

A failure to consider ESG risk should also be seen as a management failing (picked up by enforcement teams). It is hard to imagine that ignoring ESG factors could now ever be in any client's best interest – although those who dislike the area may disagree.

Allowing some investors to ignore ESG risks distorting markets – hence my suggestion (only semi in gest) that 'dangerous' is a suitable label for investments that ignore this area.

I'd therefore suggest all funds are obligated to consider this area. Strategies should however be able to vary – providing disclosure is complete. All should be able to answer client questions. (This shift is presumably starting to happen given TCFD and transition plans).

For those that de-emphasise ESG issues:

If it remains allowable for funds to entirely or mostly **ignore ESG** a label such as **'Basic'** (ie do not make use of words such as ESG or Sustainability) with the subtext -'**Designed and managed without considering sustainability issues like climate change, nature loss and human rights'** to aid end clients understanding. (Although 'Basic' may be overly kind – an 'Unclassified' or 'Failed' option may be better for the lowest level.)

For funds that pay **very limited attention to ESG / sustainability risks** – and do not let these factors influence stock selection (ie integration) or stewardship this may be harder to articulate to clients (not least as they would probably make a strong case explaining why their strategy was best). A **'Basic'** label would also probably work - with a subtext such as **'Investment strategy does not reflect environmental or social factors'**. (ie effectively a 'sustainability risk warning')

I would encourage the development of a label or other mechanism for funds that do **'ESG integration'** to get onto this ladder. Exclusions (ie 'ESG Plus') would indicate a seriousness about the area as such fund managers have recognised the benefits of going beyond integration to appeal to clients with specific concerns (eg tobacco, arms, coal) – perhaps encouraging all funds to complete a template such as the following would be a useful entry point (ie 'Basic Plus'):

See q 2 and appendix - for a suggested layout.

The fact these funds risk hampering efforts to address climate change and may put investments at risk should be spelt out. I'd suggest few people consider 'Article 6' as meaning this – but in terms of addressing climate change (etc) it would be useful if they did.

All funds / products should be required to go through the classification process in order to encourage its use and raise the profile of this area.

11. **How do you consider products tracking Climate Transition and Paris-aligned benchmarks should be classified?**

They are very welcome developments but it is too early and narrow to 'set in stone' as labels.

They are useful and should be encouraged as strategies – but not as labels. They are liable to be superseded by evolving issues, metrics or innovations within the next few years. Examples of crucial (at the time) issues and potential metrics that we rarely hear about to day include: Kyoto Protocol (climate), Montreal Protocol (CFCs /ozone depletion), Acid rain, ending Apartheid etc

There is also the consideration that some issues split opinions amongst those with deep knowledge of certain areas. eg nuclear. (Investors should be allowed to take opposing positions on issues of this kind – so it is necessary to supply additional information.)

Whilst writing this response - the issue of how the EU (taxonomy) appears to intend to classify some nuclear and gas activity as 'transitional' is causing concern. There are good arguments for and against their classification as such. The 'middle ground' the EU is looking to secure should be broadly agreeable to many – whilst others will see it as a fudge – potentially satisfying neither camp.

There will always be contentious and debatable issues such as these.

We do not know what innovation lies ahead, or where press attention will turn, so it is a risk for a financial regulator to say what is 'right or wrong'. As such investment institutions should be allowed to use any metric they believe makes sense and would be useful to clients.

As such I'd encourage a focus raising awareness (to nudge markets) and disclosure that allows clients to make for informed decisions, based on the knowledge that opinions vary and some issues (such as gas and nuclear) will continue to be contested.

Ultimately the only person who can decide whether or not they are comfortable with companies being included or excluded is the end client.

12. What do you consider the role of derivatives, shortselling and securities lending to be in sustainable investing? Please explain your views.

Funds with the highest (sustainability/transparency/ethical) standards often oppose such practices.

My view is that they undermine the long term, open characteristics we should be able to expect from sustainability funds. As such they risk undermining progress and damaging trust largely because of their opacity.

I would however be comfortable with their use if/when it could be proven a client knew what they were and if given the choice would opt for such tools themselves - perhaps for performance or price reasons (client aims vary).

Other practices that do not adhere to the spirit of long term, sustainable investment should also be viewed with caution. My view is that the more complex, short term and/or opaque a practice is the less likely it is to enhance the reputation of the area we are trying to grow. (And given the role of transparency here - our clients should not be expected to have taken investment exams in order to understand where their money is held).

13. What are your views on streamlining disclosure requirements under TCFD and SDR, and are there any jurisdictional or other limitations we should consider?

It feels too early to pass judgements on early-stage initiatives as TDFD and SDR as these will probably take some years to settle down. In principle however they should be included / in scope and regarded as potentially valuable.

I am not an expert on different jurisdictions but would encourage regulators to consider the cost implications of significant deviations - in part as we do not want these funds to be at a cost disadvantage.

This question points to the benefits of making us of 'principles' as they can allow greater flexibility as can integrate further initiatives as they emerge.

14. What are your views on consumer-facing disclosures, including the content and any considerations on location, format (eg an 'ESG factsheet') and scope?

Consumer facing disclosures must be **increased significantly** both within existing documentation and additional materials.

Transparency is a key attribute responsible investors demand of investee companies. Responsible investors should be ‘**walking the talk’** – and seen, by all, to be doing so.

Content would vary from document to document. For example, a standard fact sheet might simply make reference to a label and where to look for further information, whereas a KIID or prospectus should be expected to give extensive information if sustainability is genuinely integral to the fund strategy. Both should be supported by a full explanatory (policy/strategy) document

Requiring specific ESG fact sheets from fund managers, with a particular layout, it's not something I would encourage a regulator to do.

This is because fund strategies are **too diverse** - and over time managers may prefer to redesign their main fact sheets to include more information on ESG (some do already).

This is of course separate from the fact that for many fund managers, in particular those who are new to the area, offering an optional template may be helpful. However there is a big difference between a regulatory requirements and what an industry association or body might usefully create for their members.

Where are we now?

Disclosure and communication vary significantly as there is no obligation to publish extensive materials in this area (although the ‘Dear Chair’ principles should help address this.).

- Some fund managers make only the fund name and a few non specific words available to clients. Others publish extensive policy information and follow world events, commenting publicly on how the investment community could and should respond to address sustainability challenges.
- Some user boiler plate disclosures – which vary in quality.
- Some have strategies based on a combination of fund criteria and company wide activity that is almost impossible to bring together. This makes it very difficult for people to know where a fund will and will not invest and is also a disincentive for intermediaries.

Not everyone will want extensive ‘detail’ but all clients should have access to it if they wish.

It is important to factor in the reality that many **clients are often far more genuinely interested** in sustainability issues (and therefore fund characteristics) than many investment professionals.

It would also be **a problem for financial advisers** if full details were not available for use with clients.

Many advisers are willing to offer sustainable fund options now but few are expert at every aspect of sustainability. Not being able to provide a detailed response to a client query undermines the client/adviser relationship and is likely to discourage advisers from offering such funds in future.

15. What are your views on product-level disclosures, including structure, content, alignment with SFDR and degree of prescription?

Both product level and entity level disclosures are important.

All investments should make the extent to which they consider sustainability factors clear.

Additional information should be required of funds where sustainability is a key element of the proposition.

In most cases the focus should be on what funds do and do not do – or invest in - (relating to ‘real world’ issues) - with alignment used as evidence or supporting information in most cases.

A typical - well established - fund in this area can be expected to have a list of ‘criteria’ (or similar wording) – probably 5-20 brief bullet points used in client literature and presentations. Additional materials – or an appendix to a presentation - might have a paragraph or two explaining these criteria – and there would also

probably be a detailed 'policy' document that may or may not be made available externally (I'd suggest a version of it should be available to all.)

> It is notable that much of the information described above often does not appear on company websites (or is very hard to find). However when a presentation is requested slide packs (that have been compliance approved) – which run to 50-100 slides – are normally available. It would be interesting to work out why this is the case.

Duplication should be avoided wherever possible, reusing existing obligatory disclosure documents (such as reporting requirements) is also important in the interest of efficiency.

Content:

Funds should be clear about the basics and allow clients/interested parties to see the detail as they wish – particularly relating to where funds will and won't invest (offering the same information as that which is presented to institutional investors).

Publishing data and metrics to retail investors has pros and cons. It can be helpful (if it stands up to scrutiny) but can leave them feeling they may be being tricked if it is too vague or too detailed. 'Plain English' accompanying by information on underlying data/research is liable to work best (will / will not – do/don't … we know this because…). Where something can not be guaranteed terms such as 'aim to / aim not to') are necessary.

For feedback on draft content it would be useful to gather the views of 'interested client groups'. (You should be testing any hypothesis on 'clients who care' as they are more representative of the target market. Clients can be segmented by level of interest fyi.)

SFDR

There are issues around companies' (in all sectors) cherry picking the sustainability information they publish for commercial benefit. This is of course not a true reflection of reality. As such we should probably seek to ensure 'brown' attributes are disclosed also – to a greater or lesser extent.

16. **What are your views on building on TCFD entity-level disclosures, including any practical challenges you may face in broadening to sustainability-related disclosures?**

Making use of TCFD at entity level and building out to other issues makes sense conceptually however it would be likely to be difficult and it may be best to iron out any issues with TCFD first.

To answer this question fully I would also want to understand how ambitious the FCA is prepared to be (scope).

- Mapping every (good and bad) sustainability aspect of every product or service offered by every investee company (and therefore product and entity) could be incredibly useful – or almost impossible and hugely expensive. However it is notable that TNFD is underway, so there may be a sensible middle ground.
- In terms of what a client would want, I am confident that most people are not 'single issue' minded (we/FP research this many years ago). Most do not only care about the environment or eg climate change. And if someone cares about environmental issues they are also likely to care about people issues also. (This also concurs with the success of broad-based sustainability funds - and more 'narrowly focused' funds having additional criteria that do not directly relate to their core remit.)

This would need further thought.

17. **How can we best ensure alignment with requirements in the EU and other jurisdictions, as well as with the forthcoming ISSB standard? Please explain any practical or other considerations.**

It would be useful if the FCA had an area on their website where all relevant information of this kind (existing and proposed) could be found by all interested parties – ideally with tags.

I'd also urge caution if you are trying to align to a system that is new or has not yet been launched, or fully explained – eg ISSB – although it sounds potentially very valuable. This is in part why my suggestion of a revised disclosure structure would work as the ISSB could be readily 'slotted in' where used by managers.

18. **What are your views on the roles of other market participants in communicating sustainability - related information along the investment chain?**

This depends on your definition of participants.

However in general there is insufficient recognition on the significance of the issues we face across the investment chain ('existential threat' does not seem to have been understood). Retail investors are particularly poorly served.

If retail clients are to be properly served – and greenwash and trust issues are dealt with - there must be no chinks in the chain.

We also need to deal with misperceptions around risk (explained earlier). Current methods work against sustainability. We need to convey the message that 'unsustainable' implies an end date - and therefore increased risk whereas 'sustainable' implies a far brighter future.

Ideally we would all move in unison, however that will be difficult. More importantly perhaps is that we all need to be heading in the same general direction.

Ultimately if there are major chinks in the investment chain this will fail/struggle to have much effect. (This is largely where we are coming from with our Dialshifter® work (started c3 years ago)… although 'resource constrained').

19. **Do you consider that there is a role for third-party verification of the proposed approach to disclosures, product classification and labelling and organisational arrangements of product providers? Do you consider that the role may be clearer for certain types of products than others?**

Mixed views. Verification works (eg auditing companies is a good thing), however I am not convinced about the expertise, motivations or 'cross market / cross issues' expertise that would be available – although interest would no doubt be high and this would grow and this could move fast (see 'Big 4' sustainability recruitment drives).

There is also the reality that different clients want different things and that there are many (real world and financial) challenges to solve. The dynamic between fund holdings and stewardship also makes auditing difficult.

The key issues here are really 'matching the right product (fund etc) to the right client' and 'ensuring the fund does what it says it does'.

These both fall squarely within existing regulatory frameworks – and if sustainability is to be taken seriously it would make sense to bring these together.

Strategy could be steered or commented on by an expert panel. (Made up of people with proven personal interests /experience in sustainability & sustainable investment).

20. What approaches would you consider to be most effective in measuring the impact of our measures, including both regulatory and market-led approaches, and should disclosures be provided in a machine-readable format to better enable data collection and analysis?

Regarding **success** – some thoughts on measures, example questions:

- Are overall carbon emissions (from investee companies) falling?
- Are we moving towards a circular economy? (ie and not outsourcing problems overseas)
- Is the (investment) market favouring companies with higher sustainability standards? ('All other factors being equal').
- Is what the UK creates copied elsewhere - internationally?
- Are investee companies changing behaviours (shifting R&D budgets etc) in order to attract capital (or are they creating green silos to keep their options open?)
- Has the media (and others) started to focus on the useful ness of different sustainability approaches (whilst calling out true greenwash)?
- Can we evidence improved consumer trust?
- Also sales, complaints monitoring, market penetration of relevant products, surveying clients etc

On **machine readability** – this is not my area – but I'd suggest that those who wish to use 'machines' to read information should be designing machines that are capable of fulfilling this task – not the other way round. However I suspect a major fact may be that more information should be available to all – which in most cases means putting information online - which presumably helps machine readability (?).

Appendix

Appendix 1 - A possible pathway:

Labels – keep it simple: untechnical, unable to be disputed and unemotional, eg:

1. **Basic -** funds that do not significantly integrate ESG/sustainability. (Maps to Art 6)
2. **Hybrid** - funds that significantly integrate ESG/sustainability factors, but its impact on stock selection will vary. Likely to focus on transitioning companies and as such should be expected to hold some controversial stocks and be active stewards of capital. Where articulated, the goal of driving change / positive outcomes may be largely stewardship driven. (Loosely Art 8).
3. **Sustainability theme or focus** - this group focuses very significantly on ESG and Sustainability issues. Their holdings will be largely made up of companies that people with an understanding of sustainability would consider to be sustainability leaders & solutions providers. Having a positive impact (although not necessarily using the GIIN 'impact' description) would be at central to the strategy. Will not hold controversial, polluting or companies (eg oil). (Loosely to Art 9).

- FCA to set out rules relating to 'design, deliver and disclosure' for each so that clients know what to expect – and compliance can be confirmed. (Expert committee could steer.)
- Funds should be expected to be very clear about their methodologies (eg alignment to Paris goals as a means of driving transition … / focusing on transition / tracking a specific benchmark / bespoke positive and negative exclusion criteria etc
- There could be a level below 'Basic' – ie 'Not considered' but it is unlikely many investment organisations will admit to doing 'nothing' in this area.

*****(note to FCA – retail clients are not normally interested in governance – except when things go wrong. Institutional investors are generally not interested in ethics – until an issue becomes 'material').

I have therefore not created columns for either, but if these areas are core features of a fund strategy they should be included in the final column.)

Disclosure - template with example text for illustration purposes only) – **Level 1**

	Environmental	Social	Sustainable	Additional areas considered*
Describe any areas of **avoidance/ exclusion**	Eg Issue: **Deforestation** The fund will not invest in companies involved in illegal destruction of forests… See here for further information. Issue: **Waste.** We will avoid companies that have been fined within the last 3 years / are significant contributors to plastic	Eg Issue: **Human Rights** The fund will not invest in companies with poor employment and human rights records which we identify as those that breach ILO or UNGC standards. See here for further information.	Eg Issue: **Climate change** The fund will not invest in companies that we define as major contributors to climate change. We avoid coal, oil and gas companies. See here for further information.	Eg Issue: **Tobacco** This fund will not invest in tobacco companies Issue: **Armaments** We do not invest in companies that make cluster munitions in any of our funds.

	waste …			
Describe any areas of **positive selection** and where you aim to deliver positive impacts	Issue: **Energy efficiency.** We aim to invest in companies that are helping others to use energy more efficiently such producers of insulation and energy saving devices. See here for further information. Issue: **Waste management.** We invest in companies we believe are helping waste to be managed more responsibly by for example increasing rates of recycling amongst… See here for further information.	Issue: **Equality.** We aim to invest in companies that offer equal opportunities to their employees. One of the sources of information we use for this is gender pay gap data. Issue: **Ageing population.** We invest in companies that are helping to serve the needs of an aging population such as those in relevant medical and care sectors.	Issue: **Net Zero.** We aim to invest in companies with net zero commitments. We also look for clear statements of purpose where companies are aiming to transition to a **circular economy**.	-
Describe any areas where you aim to **encourage higher standards through engagement or voting at AGMs** (stating if this is for this fund only or across all assets) (ie Responsible Ownership)	Issue: **Nature loss.** We are currently engaging with companies to encourage them to pay greater attention to **nature loss** throughout their supply chains. See here for further information.	Issue: **Supply chains.** We are currently engaging with the apparel industry to ensure workers in their supply chains are appropriately remunerated and working in safe conditions with particular reference to covid related concerns.	Issue: **Net Zero.** We are actively encouraging all of the companies we invest in to write net zero action plans. We will vote against the reappointment of directors we believe are opposed to this proposal.	-

Second level disclosure framework

This would probably be better in a report form, but would need to replicate the structure above (which could be horizontal or vertical) so that where users are directed to 'more info' they can go straight to relevant pages of the report).

From a retail intermediary perspective this more detailed document should answer 'interested retail client questions' such as: 'what do they mean by that?', 'how does that change where they will and won't invest?', 'how do I know that's what they actually do / can they prove it?'.

From an institutional investor perspective there should be references to relevant metrics, methodologies, data sources etc as well as explanations of how this works differently for different assets (if being used for multiple asset types).

I would combine these on a single document as many institution professionals need to upskill on both 'the issues' and how these funds work (rather than relying just on data that may mean nothing to them) . Likewise many better informed (more interested) retail clients will like to see additional detail in order to allay greenwash fears (although it may be important to indicate that this is a technical document and that they are not the only intended audience). AFMs should be encouraged to use this information to create more 'bespoke' materials for their own use. I'd also suggest this should be supplied to (DC) pensions professionals and that their needs should be taken into account also so that this can be as joined up as possible (members need better information, trustees need help/training.)

Example text (combined levels 1 and 2):

Avoid / Environmental:

Level 1: Excludes companies in coal, oil, gas and mining sectors, companies causing environmental damage and companies that MSCI indicate do not meet the standards of the UN Global Compact.

Level 2: (to be available to all interested parties): We define 'coal, oil and gas companies' as companies that generate in excess of 10% of their revenue from the extraction of these fossil fuels. We also exclude companies with any direct exposure to fraking and tar sands. Companies where >25% of revenue originates from the distribution or sale of these products are also excluded. Other sectors we avoid are … [illegal deforestation, companies that have been fined over the last 3 years] etc etc.

We work out which companies can be in the fund with reference to MSCI/Moody's/Morningstar (etc) which does the following on your behalf …. You can learn more about their data here [link]…

Positive / Environmental:

Level 1: We aim to invest in companies with high environmental standards.

Level 2: We define high environmental standards as companies that have net zero plans, that have not been fined, that are regarded as sector leaders [on xyz metric], involved in the provision of enviornmental solutions (such as clean energy)… We assess them with the following tools [xyz], review them [annually?] – read more here…

Engage/Environmental:

Level 1: We aim to encourage the companies we invest in to have higher environmetal standards. We do this through a combination of direct contact with company management and voting at their AGMs.

Level 2: We vote all of our shares at AGMs and EGMs. We support / vote agains management when [insert reasons]. Over the last x years we have engaged with y companies. Our current engagement programmes are xyz because …. You can read our engagement report here [link]. We collaborate in xyz collaborative engagement programs and are members of abc.

Labelling system (draft)

What a labelling system might this look like: BASIC / HYBRID / SUSTAINABILITY THEMED (mapped to above)

Sustainability*	Environmental*	Social*	Responsible^ ownership – voting	Exclusions (FM to list)
Colours: Red – little or no consideration	Red – little or no consideration	Red – little or no consideration	Red – little or no activity / rarely vote	(Use of RAG could be optional) Coal extraction

given Amber – favour transition leaders/engage with laggards Green – invest mostly in leaders & solutions cos	given Amber – favour transition leaders /engage with laggards Green – invest mostly in leaders & solutions cos	given Amber – favour transition leaders /engage with laggards Green –invests mostly in leaders & solutions cos	against management Amber – extensive engagement and voting with most companies Green – engage when necessary / where leadership is not demonstrated	Armaments cos Tobacco cos Companies involved in animal testing for non medical purpose / not required by law
Insert text on metrics, ratings, caveats etc				

***FCA to set metrics –** mapping to taxonomy as far as possible

^ **Map to FRC stew code?** (signatory, near miss, far miss?)

What this might look like:

Sustainability	Environmental	Social	Responsibility	Exclusions
Meets the criteria of the highest sustainability, environmental and responsible ownership fund standards as described by the FCA here.				Armaments Tobacco
We assess companies in line with xyz methodology (expand) eg alignment, transition, thematic… You can find out more about how this fund works here.				

This could be used with a **'Basic / Hybrid/ Sustainability theme'** (or focus) **label**.

The criteria required to achieve 'red', 'amber' or 'green' should be published and revised regularly – for each column. (These should be kept client friendly, focus on holdings and outcomes).

Appendix 2.

SRI Services materials designed for financial advisers

Below are some (SRI Services) tables that show how we deal with this area.

1. **'The Big 3'**. This aims to help people to understand that client motivations – and therefore appropriate fund options – vary. The table cross references three common client positions against the clusters of funds we have identified (SRI Styles – first presented to FCA some years ago.)
2. **Example client pen portraits** – based on conversations over the years and highlighting some of the sticking points advisers find difficult.
3. **Example clients mapped to SRI Styles** (with different core personal 'aim') – showing which types of options are 'very likely / some what likely / very unlikely' to meet their aims.

The Big 3

Mapping core client motivations to fund options

	Sustainability themes			Values led		Tilted		Limited
SRI Style name	**Sustainability Theme**	**Environmental Theme**	**Social Theme**	**Ethical**	**Faith Based**	**Sustainability Tilt**	**ESG Plus**	**Limited Exclusions**
Mapping client motivation to fund purpose	Focus on sustainability themes, trends and opportunities, often with ethical exclusions. May hold 'transition' and/or 'solutions' companies. Stewardship/ engagement likely.	Focus on environmental themes, issues and opportunities. May have exclusions. Stewardship activity may apply.	Focus on social themes, issues and opportunities. Many have exclusions. Stewardship activity may apply.	Focus on ethical values - with environmental, social and governance criteria. May combine exclusions, positive selection and/or stewardship activity.	Screening strategy intended for investors of a specific faith.	Integrates sustainability into research. Favour companies with higher standards. May invest in all sectors. May have exclusions and stewardship policies.	ESG (environmental, social and governance) risk focus - with additional exclusions and/or stewardship strategies.	Has named area(s) of exclusions - typically avoid only a small fraction of universe.
Managing sustainability challenges well makes **good business sense**	✓	✓	✓	✓	?	✓	✓	?
I want to use my investments to deliver **positive real world impacts and outcomes**	✓	✓	✓	?	X	?	?	X
My main focus is **ethical issues** – but environmental, social and governance issues are important also	?	?	?	✓	?	?	?	X

Example clients

Which SRI Styles suit which client needs?

These client examples illustrate that different strategies and funds meet different client needs.

Example filter options that reflect likely client aims are listed below. These relate to the 'Policies, Issues and Themes', 'Approaches and Application' and 'Responsible Ownership' filters on Fund EcoMarket.

See chart to match fund SRI Styles to client examples.

Client 1
'General interest in sustainability'

Policies: Sustainability policy, Sustainability theme, ESG Integration strategy, Favours cleaner greener companies, Social policy.

Approaches: Balances company 'pros and cons'/best in sector, Combines ESG strategy with other SRI criteria.

Responsible Ownership: Responsible Ownership policy, Encourage GHG/Carbon reduction, UK Stewardship Code Signatory

Note: Most funds in this area recognise this - methods vary. Use additional filters if the client has stronger views

Client 2
'Looking for sustainability solutions & positive impacts'

Policies: Sustainability theme (and listed sub themes), Favours cleaner greener companies, Responsible supply chain policy

Approaches: Aims to generate positive impacts, Measures positive impacts (and additional impact criteria), Positive selection bias, UN SDG focus, Invest over 25/50% in solutions companies, (see impact options)

Responsible Ownership: Responsible ownership policies, Climate Action 100+ member

Note: Strategies vary. Positive selection helps redirect capital, 'impact focus' shows greater emphasis on outcomes

Client 3
'Climate focus/wants to avoid oil companies'

Policies: Excludes coal, oil and gas majors, - additional extensions: Excludes fracking, Tar sands, Arctic drilling. Favours cleaner greener companies, Sustainability theme

Approaches: Positive selection bias, Combines ESG strategy with other SRI criteria

Responsible Ownership: Climate Action 100+ members, Reviewing carbon/fossil fuel exposure for all funds

Note: Funds that do not say they exclude oil companies may invest in oil companies. Be careful about the term 'fossil free' which is currently almost unachievable

Client 4
'Focused on people/social issues'

Policies: Social policy, Human rights policy, Avoids oppressive regimes, Child labour exclusion, ESG Integration strategy, Anti Bribery & corruption policy

Approaches: Favours companies with strong social policies, Invests in social housing, Positive social impact theme (at top end of spectrum), UN SDG focus

Responsible Ownership: Diversity engagement strategy eg gender & race

Client 5
'Focused on ethics/personal values'

Policies: Ethical policy, also use individual filters eg Excludes tobacco, Armaments, Gilts, Gambling

Approaches: Combines ESG integration with other SRI Strategies

Note: Multiple options – ethical and themed funds generally consider these issues or have strategies that direct investment away from controversial sectors

Client 6
'Wants fund manager to encourage change/be 'responsible owners' across all investments'

See '**Corporare Activity**' filter for company-wide activity eg Responsible ownership policy, Encourage carbon/ greenhouse gas reduction, Responsible ownership as a key differentiator, Vote all shares at AGMs, PRI/Climate Action 100+ membership

Client 7
'Focused on animal issues'

Policies: Ethical subsection: Animal welfare policy, Animal testing exclusion, Excludes animal testing except for medical purposes, vegetarian/vegan

Note: Also consider funds with positive/sustainability themes

Example clients

Is this SRI Style likely to meet this client's needs?

	Sustainability themes			Values led		Tilted		Limited
SRI Style name	**Sustainability Theme**	**Environmental Theme**	**Social Theme**	**Ethical**	**Faith Based**	**Sustainability Tilt**	**ESG Plus**	**Limited Exclusions**
Client aim								
1. General interest in sustainability	√	√	√	√	?	√	√	?
2. Keen interest in sustainability & positive outcomes	√	√	√	?	X	?	?	X
3. Wants to avoid coal, oil and gas majors	√	√	?	?	?	?	?	X
4. Focused on social/people issues	√	?	√	√	?	?	?	X
5. Wants to avoid arms, tobacco & other damaging industries	√	?	?	√	?	?	?	?
6. Wants to encourage companies to improve	√	√	√	?	X	?	?	?
7. Animal welfare focus	?	?	?	?	?	?	?	X

Key:

√ Yes/Most funds in this style with meet this aim

? Maybe/Many of the funds in this style will meet this aim

X No/Most funds in this style will not meet this aim

Fund strategies vary within these SRI Styles and there is cross over between many of the Styles. Please see additional fund information.

Appendix 3 About Financial Advisers (some notes)

Financial advisers vary significantly. On this topic they could be split into four groups:

- Expert / specialist
- Interested but not expert
- Not particularly interested but open to client requests
- Hostile (believe this area is 'wrong' for clients)

I believe most need help in this area and would welcome greater clarity from regulators.

Below is an 'advice process' (again refined over the years) for retail financial advisers. This refers people to our tool, but could equally be used to map to alternative reference points.

One of the key elements is that it works with the flow of both a relatively natural 'discussion' in a client meeting or a client responsive online or paper based process.

Enthusiasm and support for this area is higher than it was although the surge of enthusiasm seems to have waned in some quarters since the anticipated MIFiD II advice process changes did not come into force.

> **Note** - I would strongly recommend this is revisited. Advisers **should** be discussing this area with their clients. If they do not clients may not learn of the existence of sustainable options, which may lead to complaints. Clients should always have the option to invest in line with their other lifestyle decisions.

Many advisers have found this area difficult for many years, in part because they have not been obliged to offer it so have not upskilled, but also because clients are often ahead of them in terms of the issues they care about, which risks their position as 'experts' being undermined. (Expert advisers deal with this by having interesting exchanges with clients.) This can also get difficult when a client opinion differs from their advisers' views. It must always be the case that a client's opinions are respected.

Dealing with 'real' people with **wide ranging** (and occasionally extraordinary) **personal opinions** (and often low financial awareness) is what sets 'retail' sustainable investment apart from other sustainable investment

markets. This makes it both more difficult and more interesting. (It is worth noting that this area is different from DC pensions also where decision making is somewhat buffered by employers or trustees.)

The FCA needs to recognise that the diverse range of interests and concerns held by individuals will not be altered by regulators or advisers.

Intermediaries will always have to deal with a wide range of queries, many of which they may not be entirely comfortable with (eg sometimes that will be high profile issues like climate, other times it will be about animal testing, nuclear power – or the latest related news item / activity in a nearby large business – or something the adviser vehemently disagrees with.).

What you/we designed here should aim to help not hinder intermediaries – reflecting the realities of dealing with 'regular people'. Retail clients do not talk, think, or behave like investment professionals as that is not their chosen area of expertise.

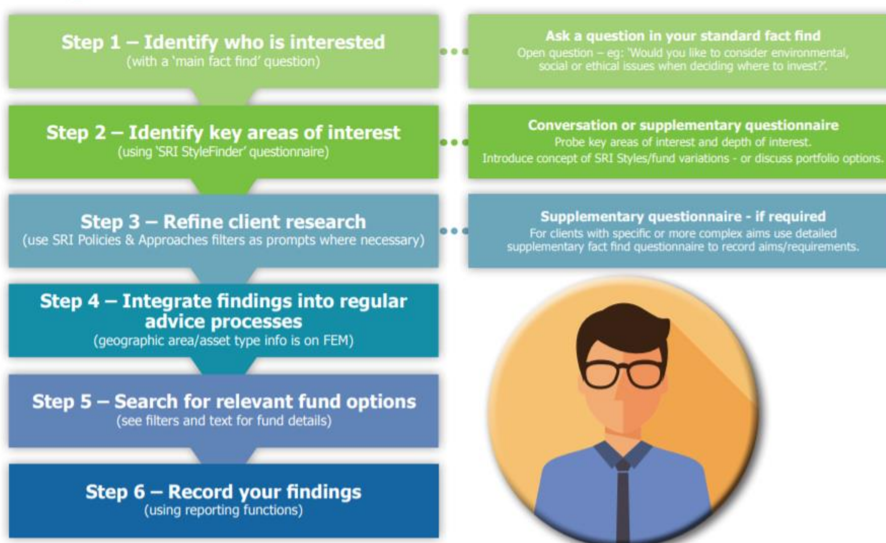
So language matters. If this work has the hallmark of 'institutional investors' (or other B2B language) on it the chances of it working well in the retail intermediated or direct markets will be greatly reduced (as clients risk thinking they are being hoodwinked.)

The litmus test should always be 'could you describe this to your family or friends?'

> For example, try to imagine explaining the difference between 'alignment' and 'transitioning' to a (potentially uninterested) adviser – knowing that they would have to pass that on to their potentially very interested clients.
>
> The reality is that they are very similar even if they are fed by different data sets. Both are aiming to drive change, and recognise that this will take time – as such an interested client should be encouraged to explore both.

Advisers and other intermediaries could be either tremendous allies or show stoppers.

(I'd be happy to expand on this if you wish).



Link to our SRI StyleFinder tool: https://stylefinder-tool.fundecomarket.co.uk/

Other links: www.FundEcoMarket.co.uk and www.sriServices.co.uk

Other intermediaries. Platforms and other intermediaries face different but connected challenges. I am happy to discuss or offer notes if useful.

Appendix 4 About clients (some additional notes)

Client needs and opinions vary significantly (as the tables above illustrate). It is incumbent on us to ensure that **clients views are matched to the investment options that best meet their needs**, from both a financial and sustainability / ESG perspective.

Clients should not be expected to know what funds are available or how they work – even if they know a great deal about sustainability.

Who is interested? There is a general assumption that we currently talk about the young and the wealthy clients who are more interested in this area than others. I would contest that view and say that whilst those are sensible marketing messages there is little evidence that those are the 'most' or 'only significant' group of potential clients – or the best to target. We really need to look at 'all' people and investors. The example press release below Some aspects are irrefutable – investors are wealthier than most and younger people know more about environmental and social issues because of changes in education, media etc.

The first investors in this area were largely people working in public services such as teachers, medical professionals. As such we should be careful not be too drawn in to often imperfect market research …

You may find the media release below of interest. Whilst I do not favour putting too much emphasis on a single piece of research I can say these numbers were replicated regularly. This research is from an NOP survey in 2003. I'm happy to discuss any time.

- *'83% of respondents believe financial services companies should encourage companies they invest in to take social ethical and environmental issues seriously'*
- 74% of respondents would like more information social ethical and environmental policies
- 45 to 54 year olds feel most strongly about their investments and company SEE policies (ie these people would now be 65-75)

22nd September 2003

FRIENDS PROVIDENT CONSUMER RESEARCH REVEALS HIGH INTEREST IN SOCIALLY RESPONSIBLE INVESTMENT

Friends Provident, leaders in retail ethical investment, announced the results of recent consumer research into awareness and attitudes towards the social, ethical and environmental (SEE) policies of the service and product providers they use.

The research found high interest amongst consumers, indicating substantial growth potential for SRI, but pointed to low levels of advice received from financial advisers.

Key findings:

- 91% of respondents believe it is important that companies take social, ethical and environmental issues seriously
- 76% of respondents would **not** like their money invested in companies which have poor social, ethical or environmental policies
- 83% of respondents believe financial services companies **should** encourage the companies they invest in to take social, ethical and environmental issues seriously
- 76% of people would prefer to buy from companies who try to reduce the negative impacts of their activities on society and the environment
- One in four (25%) respondents actively look to buy from companies which take social, ethical and environmental issues seriously, and a further 59% would like to do so but do not normally have enough information to buy on that basis
- Only 8% of respondents had ever received advice on ethical investment from a financial adviser

Julia Dreblow, SRI Manager at Friends Provident, said:

"This is clear evidence that social, ethical and environmental issues are important to the consumer.

"Consumers want companies to take SEE issues seriously and would like to be able to buy products and services equipped with information about the way they run their businesses. In addition people are very supportive of the principles of ethical investment, namely 'avoidance of companies with poor policies' and 'encouraging better practices', although this contrasts starkly with the 1% of investors' money that actually goes into screened funds – a fact potentially explained by the low level of advice on this area that appears to be available.

"So, on the one side we have consumers wanting SRI/ethical advice and on the other side, not much advice is offered. I hope that on seeing this, financial advisers will rise to this challenge."

In addition the research, which was split into three areas, indicated that:

Companies and Social, Ethical and Environmental Issues (SEE)

- 74% of respondents would like more information about the SEE policies of the companies that they buy products or services from
- The older age groups tend to be more proactive in using companies with better SEE policies (65 plus)

Social, Ethical and Environmental Issues and Finances

- One in five respondents (22%) were **not** aware that most investment funds put their money into all types of companies irrespective of their social, ethical and environmental policies
- Of the 76% of respondents who would **not** like their money invested in companies that have poor SEE policies 56% strongly agree with this sentiment
- Of the 83% who felt that financial services companies should encourage the companies they invest in to take social, ethical and environmental issues seriously, 58% agree strongly

- 45-54 year olds feel most strongly about their investments and companies' SEE policies

Financial Advice

- 47% have, or had ever had a financial adviser

- AB respondents were more likely to have a financial adviser than any other social class, with 25% currently having a financial adviser and 36% having had a financial adviser in the past. Unsurprisingly, the majority of DE respondents, 70%, had never had a financial adviser

The telephone based research was conducted by NOP on August 1-3, 2003 and provided analysis by age, sex and social class across 998 adults aged 15+. Few differences between regions, age or sex were evident, calling into question perceived stereotypes about such issues mainly being of concern to women or 'younger people'.

- Ends -

For further information, please contact:

Julia Dreblow	Friends Provident	07802 642065 020 7506 1407
Jim Murdoch	Friends Provident	01722 311 447

Issued on behalf of Friends Provident Life and Pensions Limited.

Notes to Editors

- Friends Provident launched the UK 's first range of retail ethical funds – the Stewardship range in June 1984
- Stewardship has the most retail funds under management of any ethical fund range, totalling £1.2bn of the £3.5bn retail ethical fund market (Source: EIRIS Aug 2003)
- An external panel of experts – the Committee of Reference - decides Stewardship's ethical screening policies. This group also approves all companies before the fund managers can buy shares or bonds for the Stewardship funds
- The Committee is supported by an 11 strong Governance and SRI team at ISIS Asset Management, the largest of its kind in Europe

Appendix 5 'SRI Styles directory' web page text

Funds which focus on a specific issue or theme – often alongside screening criteria and engagement:

- **Sustainability Themed funds** focus significantly on (environmental and social) sustainability issues, opportunities and themes when selecting investments. These funds tend to have forward looking strategies, favouring companies that show 'sustainability leadership', are 'solutions companies' or help to facilitate the 'transition' to greener lifestyles. They may also have 'ethical' exclusion criteria and encourage positive change through stewardship activity.
- **Environmental Themed funds** significantly integrate environmental issues into investment strategies. Their focus is often around longer term environmental and resource related issues, risks and opportunities. May focus on a single issue, industry or resource. May have 'ethical' exclusion criteria and encourage positive change through stewardship activity.
- **Social Themed funds** focus on 'people issues', investing in assets that help to address social challenges such as employment, education, housing and other basic necessities of life. Strategies vary.

Funds which focus on 'ethical' or 'values based' issues – normally by employing negative and/or positive screening criteria – typically alongside ESG considerations and engagement activity:

- **Ethical Funds** – focus on 'values based' issues typically alongside considering ESG (environmental, social and governance) and sustainability related issues. These funds set out where they aim to invest and avoid in their published criteria. Some have extensive exclusions others may make more balanced decisions – balancing pros and cons. The most common exclusions are armaments and tobacco – which typically sit alongside a range of environmental and social exclusions or positive criteria. Strategies vary. Some funds exclude more than others. Fund strategies are often complemented by responsible ownership (stewardship) activity.
- **Faith Based funds** invest in line with specific religious principles (e.g. Shariah Law)

Strategies that significantly integrate 'issues' – but may invest widely across most sectors and/or rely substantially on stewardship activity:

- **Sustainability Tilted funds** integrate (environmental and social) sustainability considerations into their investment processes favouring companies and typically aim to be 'overweight' in companies the managers believe have higher standards and 'underweight' (invest less in) companies with lower standards. They may also have 'ethical' exclusion criteria and encourage positive change through stewardship activity.

- **ESG Plus** Funds combine environmental, social and governance risk mitigation strategies alongside other strategies which demonstrate the fund is intended for clients with an interest in ESG issues. The additional activity may be extensive responsible ownership activity and/or exclusion criteria. Strategies vary. See fund entries for further information.

Limited avoidance

- **Limited Exclusions** is our classification for funds that exclude only a very small proportion of an index or allowable universe – and invest otherwise in a 'conventional' fashion. Some funds exclude companies with the worst possible ESG scores, others may avoid a single industry eg tobacco or cluster munitions manufacturers. These funds are significantly different from other SRI Styles as they have a very 'limited' impact on stock selection.

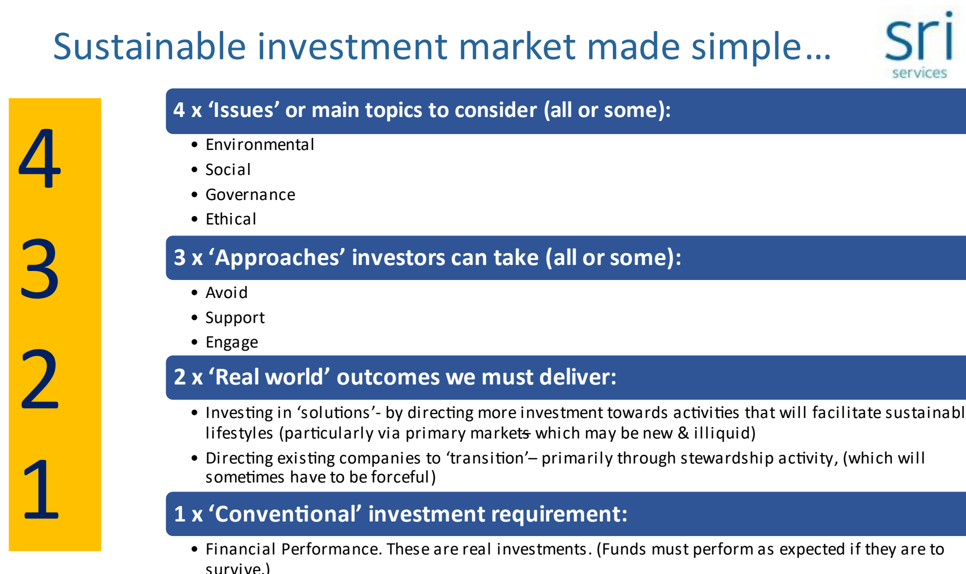
Fund Manager company listings

- **Responsible Ownership** entries on Fund EcoMarket refer to company wide strategies – listing individual fund management companies by name. These listings are not complete. For information on 'responsible ownership' (Stewardship/voting/engagement) activity that applies to individual funds see the 'Responsible Ownership' filter information within each fund entry. Responsible ownership activity is often integral to fund strategies as many fund managers aim to encourage to raise their standards, however practices vary.

Appendix 6

Explaining 'the sector' to newcomers:

We need to be able to 'frame' this area for those who are new to it or know little about it. You may find the following 'aide memoire' useful:



Example script :

"This area is complicated. Fund managers can choose to focus on any or all of the following ***four*** *areas: environmental, social, governance ethical issues - many of which have dozens of sub categories.*

There are however only ***three*** *main ways fund managers can deal with any (or all) of these issues. - they can focus on choosing companies they believe are doing a good job, stay away from stuff (industries, business behaviours etc) that they don't like or keep hold of a company and try to improve them (which we call responsible ownership or stewardship).*

And there are ***two*** *things we need to do as investors who care – ways in which investment interacts with the real world – we can (and must) drive more money into solutions that will help us make our lives sustainable (although this is a bit complicated in secondary markets like equities) and we need to help change what existing businesses do so that they become sustainable.*

These can be combined in many different ways – hence the complexity of this market. But there is ***one*** *thing all funds must have in common – they are all investments - so they need to make money. No fund can survive simply because it sounds nice!"*

Appendix 7 - Further comments on content

1.17 – GSIA. GSIA information has particular value in part because it is built out of the sustainable investment community – specialists who are committed to driving change (as opposed to newer entrants or those taking a shapshot 'as at today').

It is relevant that people understand – as you note - the terms used by GSIA refer to 'approaches' that may be employed by funds - and not entire 'fund strategies'. However although they collate market stats by strategy there remain issues with crossover, double counting etc. This links through to the challenges with Figure 3 – which appendix 1 may also help you to unpick.

Highlighting the broad strategy differences is however crucial as without it there is an expectation all funds should be the same - and an incorrect assumption that variations equate to greenwash.

Box 2 – page 13. **Sustainability disclosure and classification initiatives.** I'm biased, but I think it would be useful if you added Fund EcoMarket information. (We will be updating our site soon so could supply new text).

> Our 'SRI Styles' are a classification/labelling system - and the 'More Info' fund pages are effectively a disclosure system (for the retail community.)

Appendix 8 – Further comments on content

Bullet 2, section 4.6 – be careful with comments like 'objective… to reduce the carbon intensity of investments …' . This may not reflect what a client really wants. Some will simply want a low carbon fund, others will want to be encouraging carbon emissions, supporting leaders.

4.7 This is excellent work.

4.8 – you need to be careful here. Clients want to know what funds do and do not do. Crunching complex strategies down to one or two metrics or data points is full of risks. Clients may all flock to the funds with the best scores and therefore undermine the concept of encouraging progress. Also keep in mind that at fund level emissions can easily be 'gamed' by simply selling out of polluting stocks and buying lower emitting ones – particularly if the focus is scope 1 & 2 only (eg sell oil, buy banks) – which would not have the desired effect, and if explained would leave some clients feeling cheated as banks finance big oil.

Although metrics are useful (particularly for major investors) retail clients are generally better served by having access to 'written information'. We also need to be careful not to overwhelm sustainable fund managers many of whom are doing a great deal already.

Disclosure notes:

- It may make sense to see how AFM wide transition plans work out. (This could be fraught with complexities which many managers could be ill placed to deal with.)
- Clients may benefit from a requirement to list companies (and other assets) held / bought / sold over a 12 month period (eg published once a year at a fixed time). (This is something the DLAG should debate).
- You should consider what the intended user of any documents would actually read in full. I'd suggest clients will often have a good grasp of (and therefore use) information like 'the fund will/won't invest in companies that [do xyz] / are involved in [abc industry/activity] to improve standards'. References to metrics may be seen as 'more of the same investor speak' (an ignored) or worse - may lead to undesirable outcomes. All should ultimately point towards real world outcomes. (Funds of this kind were for a long while considered to be growing in popularity because people could talk about them in the pub with their friends. Generating more 'metrics' risks making them dull.)

4.9 – I have multiple concerns here, eg:

Many retail clients would be more than **capable of understanding metrics** if supplied with relevant explanations – however they would probably feel they are of little relevance if it did not clearly relate to real issues, risks or opportunities (financial or ESG).

Either way I do not feel that investor education is the 'key' (see comments in the introduction). There are exceptions of course, but broadly the **investment industry** to **work out how to make itself understood**.

Probably more important is the need for many more **investment professionals** (including advisers, trustees etc) **to learn more about sustainability** – and understand how investment markets impact the real world. This requires a very different skillset and mindset. (There remains a lot of pressure to make sustainability issues conform with traditional 'investment methods and thought processes'. I think that time has probably passed now.)

Explaining some terminology will be important - both purely about sustainability and about the sustainability/finance cross over zone.

You should also not seek to '**disentangle ethical and sustainable investment'**. The difference between these approaches is generally minimal and often relate more to sharp elbows or limited experience than reality.

Strategies vary of course but in practices there are **very few** (highly regarded, actively managed) **sustainable funds invest in the sectors** (or types of companies) that are **commonly excluded from 'ethical' funds**. Such companies are rarely 'sustainable' – by nature. And funds in both camp can be pragmatic – allowing some exposure to 'undesirable' activities where considered appropriate.

Funds marketed as 'ESG' can take a different view (as ESG ratings, which have been very successfully sold, can throw up some **perverse and often uncorrelated/different results** – consider the BP/Tesla debate). These strategies are regularly questioned by interested clients and advisers – and criticised for greenwashing if not properly explained. (Note there is no single 'correct' strategy as clients' views, like fund managers' views, vary.)

It is also important to remember that 'ethical exclusions' (eg arms, tobacco etc) are popular with retail clients (see Fund EcoMarket search list).

Many 'ethical issues' **could also be re-categorised** (by fund managers or others) as 'environmental' and 'social' because of their impacts on the planet or people. Gambling, pornography, alcohol, armaments (war!) are social issues. It is not popular to think like this now – but keep in mind 'human rights' were seen as an 'ethical issue' not long ago.

As such there is often **no clear water between ethical and sustainability strategies.** (Faith funds and the animal welfare / testing issues are notable exceptions.)

(I would encourage the FCA not to get caught up in the side-lining of ethical funds. Many ethical funds have the highest sustainability standards. We should also consider the signal it sends when 'ethics' and 'ethical options' are notably side-lined.)

Appendix 9

About fund diversity / variations

The Figure 3 labelling system would not be able to easily reflect the variety of fund options that are available today – or those that are likely to launch over the coming years.

The following highlights some of this diversity of approach and illustrates why classifying by up to 3 very specific approaches would be both difficult and undesirable.

> This is in part because in reality some are **very similar** (see feedback on concerns elsewhere **-** and also because we do not necessarily want to encourage **huge capital flows** into a small cohort of stocks – what we need to aim for is a **market wide increase in investee company standards**.

The range of options available today:

Funds promoted as being about 'sustainability': The following offer a flavour of the different 'methodologies' and 'strategies' sustainable funds offer UK retail investors **today** (more are likely to follow):

> sustainability themed (broad / general 'solutions' focus), sustainability tilt (weighted selection), impact, single specific/narrow theme/sector or issue (eg waste, nature, technology, carbon offset, energy/energy transition, infrastructure), broader specific issue/theme (eg climate transition, sustainable development, leaders, balanced, aligned, impact aligned), linked to a single index or methodology (eg Paris, SDG an MSCI index), use multiple indices...

Other relevant fund types that are explicitly helping to deliver a more sustainable future. Note - these funds have diverse strategies (as the names suggest). They emphasise different areas and may be very similar (or very different) to many sustainable funds if you look at their holdings, engagement etc…

- ethical fund,
- social funds,
- environmental funds,
- ESG funds,
- responsible funds.

Active funds - in practice

Many of the 'more established' and 'investor responsive' funds (that have survived) understand that they need to both look after existing clients and be up to date with emerging issues to attract new clients. This is generally done by evolution not revolution. In many cases new issues have been studied and integrated over time.

These funds tend to shy away from simplistic single issue/approaches and language as they know the trouble this can cause (see current greenwash debate).

Their sophistication (complexity) is in many cases part of what has enabled them to survive as they have dealt with emerging concerns as they happen. Newer incumbents may dislike their approaches, but I believe many new entrants could learn from approach that put specific issues and client concerns are at the heart of processes – rather than the availability of mass market metrics.

Example approaches that **a single fund** may employ:

- If it invests in companies with operations controversial or oppressive regimes they are likely to use / reference ILO conventions (norms) and / or Freedom House (research & rankings) for human rights issues (building in screens accordingly)
- They are likely to exclude all companies that breach the UNGC (norm) (although few explain what this means – who specifically/why etc)
- ESG risk is likely to be integrated across the board (ESG integration)
- they are likely to 'exclude' certain areas (eg arms and tobacco)
- they are likely to be pragmatic and pick 'best in sector' companies in sectors that are neither firmly positive or negative (eg banks, supermarkets, tech)
- They may have multiple (1-20) 'themes' (with or without sub themes) that they use to help identify and articulate opportunities / stock selection

- They are likely to engage with management when a company they hold 'could do better' or may face future risks (responsible ownership)
- They may have an overarching aim of helping to 'make a difference', 'drive positive change', 'redirect capital' (terms previously used) or 'deliver [positive] impacts' (the more current term – which can however open a can of worms as not easily mapped to retail funds without risk of misleading)
- They may use any combination of directly (primary) research or use or reference information from data providers or index providers. (Many do not entirely trust data feeds as they have previously found errors.)
- They may or may not be comfortable referencing 'conventional' benchmarks
- They are liable to have different de minimus limits for different issues (in recognition of the fact absolute avoidance is very difficult in the real world – and that companies can change overnight eg when an investee company makes an acquisition

Appendix 10

Top 100 filter searches on Fund EcoMarket during 2021

(As described in introduction)

1. OEIC/Unit Trust
2. Sustainability Themed
3. Equity
4. Mixed Asset
5. Global
6. Environmentally Themed
7. UK
8. Sustainability policy
9. Ethical
10. Environmental policy
11. Investment Trust
12. Fixed Interest
13. Passive Equity
14. Coal, oil &/or gas majors excluded
15. Climate change / greenhouse gas emissions policy
16. SICAV/Offshore*
17. Equity Income
18. Armaments manufacturers avoided
19. ETF
20. Unclassified
21. Not Set
22. Europe
23. Tobacco production avoided
24. USA
25. Asia Pacific
26. Emerging Markets
27. Animal testing exclusion policy
28. Sustainability Tilt
29. Ethical policies
30. ESG Plus
31. DFM/Portfolio Planner*
32. Fracking and tar sands excluded
33. Invests in clean energy/renewables
34. Animal welfare policy
35. Europe >50% UK
36. Asia Pacific ex Japan
37. Europe Ex-UK
38. Pension
39. Arctic drilling exclusion
40. Child labour exclusion
41. Gambling avoidance policy
42. Infrastructure
43. Avoids companies with fossil fuel reserves
44. Deforestation / palm oil policy
45. Social Themed
46. Property
47. Social policy
48. Favours cleaner, greener companies
49. Pornography avoidance policy
50. Human rights policy
51. Limits exposure to carbon intensive industries
52. Environmental damage and pollution policy
53. Aims to generate positive impacts (or 'outcomes')
54. Clean / renewable energy themed
55. Excludes animal testing except for medical purposes
56. Unsustainable / illegal deforestation exclusion policy

57. Indian sub-continent
58. Ethical - Balanced
59. Governance policy
60. Strictly screened ethical fund
61. Positive environmental impact theme
62. Not set
63. Sustainability themed
64. Other
65. Latin America
66. Alcohol production excluded
67. Responsible Ownership (FM company)
68. Plastics policy / reviewing plastics
69. Avoids companies with poor governance
70. Japan
71. Ethical - Negative
72. Faith Based
73. Africa
74. Oppressive regimes exclusion policy
75. Rathbone Ethical Bond
76. Anti-bribery and corruption policy
77. Positive selection bias
78. Nuclear exclusion policy
79. Measures positive impacts
80. Liontrust Sustainable Future Managed Growth Fund
81. In house responsible ownership/voting expertise
82. Balances company 'pros and cons'/best in sector
83. Health & wellbeing policies or theme
84. Invests in environmental solutions companies
85. Available via an ISA (OEIC only)
86. Negative selection bias
87. ESG integration strategy
88. Hedge
89. Water / sanitation policy or theme
90. Cash (or =)
91. Sustainable transport policy or theme
92. Positive social impact theme
93. Responsible supply chain policy or theme
94. Life
95. Janus Henderson Global Sustainable Equity
96. Avoids genetically modified seeds/crop production
97. Employ specialist ESG/SRI/sustainability researchers
98. Civilian firearms production exclusion
99. EdenTree Responsible & Sustainable European Equity Fund
100. Encourage board diversity e.g. gender