

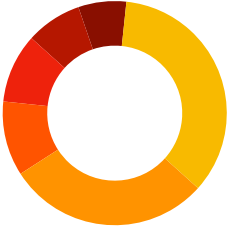
# ESG ACCORD

Your compliance, ESG & Sustainability, in accord

## ESG & Sustainable Finance:

**A Compliance Guide for ALL  
firms striving to deliver best  
practice financial advice and  
outcomes that genuinely meet  
ALL client preferences**

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## INTRODUCTION

The investable universe of funds has dramatically changed in the last couple of years in response to the increasing availability of metrics for ESG and Sustainability.

The investment space is now awash with newly authorised ESG and Sustainable funds. In addition, many existing funds have been retro-fitted to include a host of newly available metrics.

This means it is now highly likely that ESG and Sustainability risks are, and will continue to be, financially relevant to a fund's investment process - even when they are not specifically marketed as ESG and Sustainable Funds.

For these reasons, this guide is for ALL firms striving to deliver best practice financial advice and outcomes that genuinely meet ALL client preferences.

### We aim to give you insight on:

- **EQUIVALENCE.** What actions do you need to take in response to the UK's stated EU equivalence for ESG and Sustainable Finance?
- **PROD.** Why your existing compliance procedures need to catch up with the changes in the investment space
- **ACTION.** What to do to update your compliance and prepare your firm for longevity in the face of additional regulatory actions or guidance

**The rules work both ways for inclusion and exclusion rationale and reporting for ESG and Sustainability risks within the investment process of Article 6 funds. Effectively this means ESG and Sustainability disclosures for ALL funds - not just those marketed as Green or ESG!**

## EQUIVALENCE

The Government and Regulators are increasingly focused on Sustainability and this extends deeply into the financial services industry.

In April 2021 Rishi Sunak wrote to the FCA & PRC;

**"The UK is aiming to ensure every financial decision takes climate change into account."**

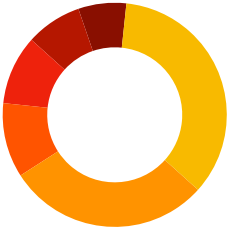
The FCA is already looking beyond its climate remit. The FCA response to the Committee's report, 'Net Zero and the Future of Finance' includes;

**"We will also need to deepen our work on ESG issues, beyond climate change. For instance, we will need to consider more fully the role of finance in dealing with other environmental issues, such as biodiversity (as set out in the Dasgupta Review, February 2021), as well as social issues, such as racial equality, the living wage and diversity and inclusion."**

The EU has moved ahead with their Sustainable Finance rules and it is expected that the UK will mirror many of the EU's proposals. This makes it easier for large cross-border financial services firms and meets Government plans for a sustainable economy.

EU Categories for financial promotions (refer to the taxonomy):

- **Article 6** - covers funds that don't integrate any sort of sustainability into their process. These must be clearly labelled as non-sustainable with reasoning. Likewise, the rules for rationale and reporting work both ways for the ESG and Sustainability exclusion or inclusion. Effectively this means ESG and Sustainability disclosures for ALL funds - not just those marketed as Green or ESG!
- **Article 8** - "products promoting environmental or social characteristics"
- **Article 9** - "products with a sustainable investment objective"



## EQUIVALENCE continued...

The UK has a reputation for gold-plating regulations from the EU (and has on-shored Basel III). It is very important to the UK that this is not lost so we must have stronger (gold-plated) participation and conduct for this to continue.

In June 2021 the FCA wrote to AFM chairs for Authorised ESG & Sustainable Investment Funds: Improving quality and clarity. There are guiding principles for asset managers for funds marketed with a sustainability and ESG focus to describe their investment strategies clearly and any assertions made about their goals are reasonable and substantiated.

The FCA has released its Sustainability Finance Strategy which aims;

**“...to make sure that our regulatory approach creates an environment in which market participants can manage the risks from moving to a more sustainable economy and capture opportunities to benefit consumers.”**

The strategy is based on three themes;

- **Transparency:** Promoting good disclosures along the investment chain. TCFD implementation, listing rule for premium listed issuers, UK Gov Roadmap, upcoming consultations. Co-leading work with IOSCO and FSB, engagement with IFRS Foundation initiative
- **Trust:** Ensuring that the market delivers sustainable finance instruments and products that genuinely meet investors' sustainability preferences. Working on guiding principles for the design delivery and disclosure of ESG / Sustainable Finance investment products

- **Tools:** Government, regulators and industry all working together to share experience, develop guidance and tools, and provide mutual support as we address the challenges of climate change. Close collaboration with industry, Gov and other regulators. Co-chairing Climate Financial Risk Forum with BoE, forum for mutual support and shared experience

The FCA has introduced the concept for **UK Fund Labels**. These categories are to cover ALL funds to aid consumer choice, capture opportunities to benefit consumers, reduce greenwashing and consumer risk.

At ESG Accord, we have considered UK EQUIVALENCE and Fund Labels and believe that the following would be a sound basis to implement a fund labelling system:

The Investment Spectrum:

- No ESG & Sustainability
- ESG
- ESG+ Screened Underpins
- Responsible & Sustainable
- UN SDGs & Impact Investing
- Ethical Screening

## PROD

PROD is part of the FCA objectives to deliver better outcomes for investors. By using the term 'target market' the Regulator aims for the Manufacturers (Asset Managers) and Distributors (Advice Firms) to match target market descriptors with their client needs.

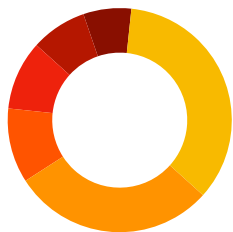
As set out in our introduction to this guide, the investable universe has dramatically changed in the last couple of years in response to the advancing availability of metrics for ESG and Sustainability.

The current MiFID II PROD structure for target markets is based on the investable universe.

**Now is the time for a Target Market review!**

### **PROD 3.3 Distribution of product and investment services sets out items for UK Financial Advisers.**

We encourage all advice firms, compliance firms and para-planners to read the following PROD overview. From this it is clear that existing compliance processes need to catch up with the evolved investment space.



## **PROD continued...**

### **Key areas under current PROD requirements:**

#### **3.3.1:**

Distributors must understand financial instruments, they must assess compatibility with the needs of their clients and take account of the Manufacturer's identified target market.

#### **3.3.3:**

Distributors should obtain information from Manufacturers to understand and have knowledge to ensure distribution is in accordance the needs, characteristics and objectives of the target market.

#### **3.3.9**

Distributors should determine the target market even if not defined by the Manufacturers.

#### **3.3.10**

Distributors identify target markets and distribution strategy with the information from the Manufacturers and the information they hold on their own clients.

#### **3.3.11**

For the target market and distribution strategy, Distributors should take into consideration the nature of the financial instruments and recommend how they will fit with their clients' needs and risk appetite.

#### **3.3.12**

Distributors must identify target markets for each financial instrument at a sufficiently granular detail.

#### **3.3.15**

Distributors must have adequate product governance to ensure financial instruments and services are compatible with the needs, characteristics and objectives of the identified target market. Their distribution strategy is consistent with target market. Distributors must identify and assess the needs of clients so their interests are not compromised by commercial or funding pressures. They must identify groups of clients whose needs, characteristics and objectives for which the financial instrument or investment service is not compatible (negative target market).

#### **3.3.16**

Distributors should periodically review product governance arrangements under PROD 3.3.15R and take appropriate actions when needed to ensure they remain robust and fit for their purpose.

#### **3.3.21**

The management must have effective control over the product governance when determining the range of financial instruments offered or recommended and the services it provides to each target market.

#### **3.3.22**

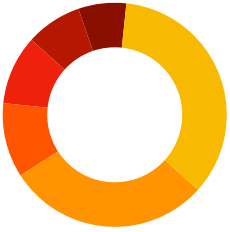
Relevant staff must have the necessary expertise to understand the characteristics and risks of the financial instruments they will distribute, the services provided and the needs, characteristics and objectives of the identified target market.

#### **3.3.26**

To regularly review the financial instruments which are distributed and the services provided, this must take account of any event that could materially affect the potential risk to the identified target market.

#### **3.3.27**

Distributors must assess at least if the financial instrument or investment service remains consistent with the needs, characteristics and objectives of the identified target market and if the intended distribution strategy remains appropriate.



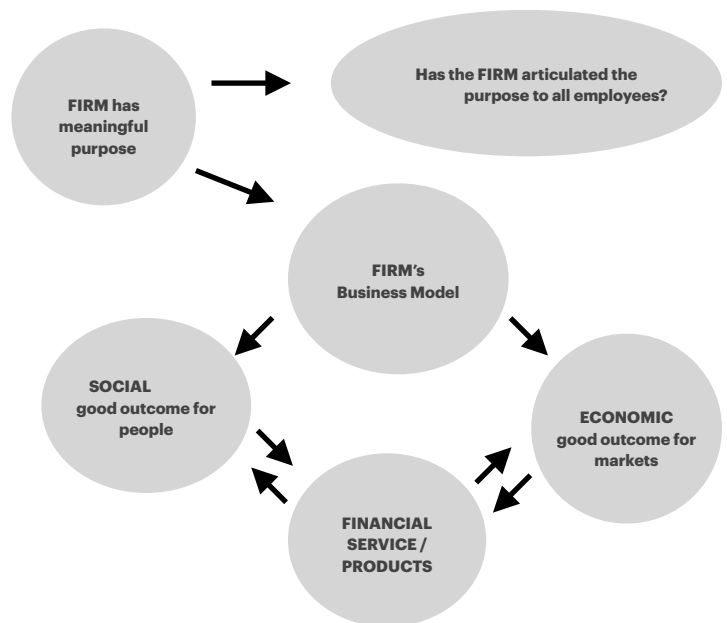
## ACTION

PROD participation is linked to the culture of a company/firm, by how (and if) the firm articulates its purpose and values through its systems, controls, and arrangements.

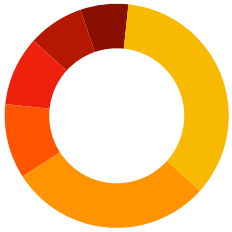
Good research and due diligence starts by bringing attention to the KYC and PROD requirements. The outcome from a firm's KYC and PROD procedures drives the MiFID II participation/dialogue/due diligence with fund groups. And this equals delivering best practice advice to clients which genuinely meets their needs.

- **Decide what advice your firm will give.** Maybe it will be the whole spectrum of investment strategies under Sustainable Finance, or could stop short of full ethical investment advice and instead refer to a specialist firm.
- **Review your firms PROD Target Markets.** Do the selected funds target markets still match your client segmentation? How will you categorise your clients' preferences to span the full spectrum of funds, including ESG and Sustainable Finance?
- **Let your clients know what advice you can offer.** This can be a simple website statement or dedicated section containing information on ESG and Sustainable Finance options.
- **Update your Internal Compliance Statement and Due Diligence for Fund Groups.** Are you asking sufficient granular detail covering the Investment Space / ESG & Sustainability Spectrum?
- **KYC.** Assuming the full spectrum of funds broadly spans 6 Levels (see Page 3), you'll need a comprehensive series of questions which cover these levels and gather information about client preferences.

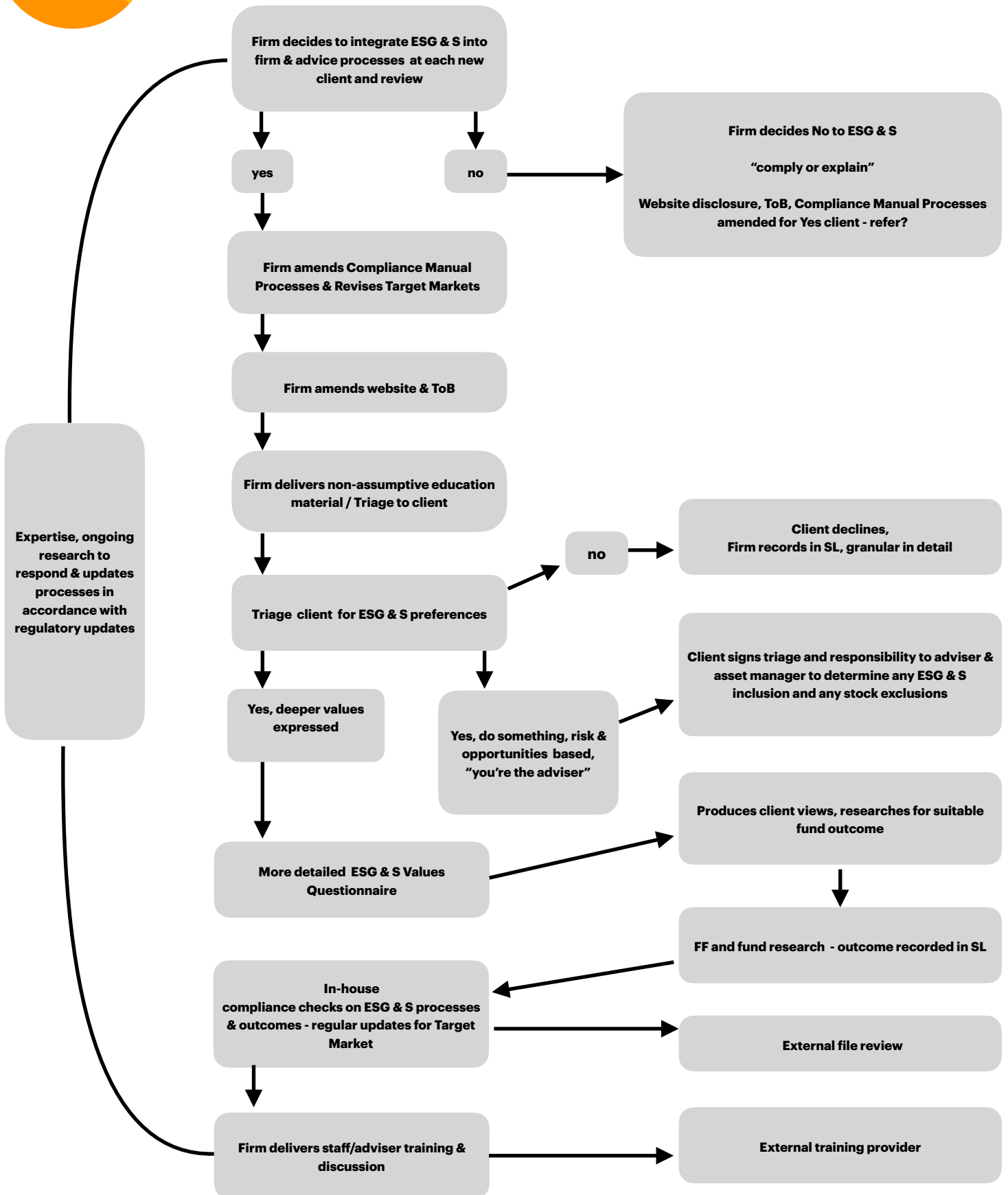
- **Offering client education.** This is a requirement from the FCA. How will you ensure and record that your clients understand what they are being asked?
- **Revisit Purpose & Governance - Drivers for culture / best practice\***
  - **Leadership** - top down, SM&CR, to act in the best interests of ALL clients.
  - **People policies** - incentivised behaviour, cumulative effect (recruitment, diversity, progression etc).
  - **Governance** - The firm's systems and controls arrangements. How decisions are made and implemented, avoid group think, manage & reduce risk to the firm from assumptive behaviours, accommodate all views, look at the board committees.
  - **Purpose** - a combination of the business model and the way a firm thinks about the social or economic contribution it provides.



\*Interpretation from SOURCE <https://www.fca.org.uk/news/speeches/regulatory-perspective-drivers-culture-and-role-purpose-and-governance>



# ESG & Sustainability - Example Integration into Financial Advice Firm





## **ESG ACCORD: For ALL firms striving to deliver best practice financial advice and outcomes that genuinely meet ALL client preferences.**

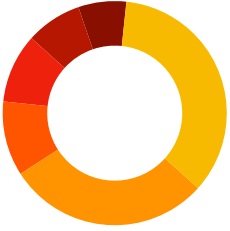
**Here are three key barriers to behaviour change: knowledge, cost and hassle. This is how ESG Accord can help you:**

- **Active engagement with clients** - deepen your client retention over generations by upping your KYC to current PROD requirements via our Triage & Values Questionnaires (VQ) & Due Diligence Questionnaires
- **Clear communications** - website & ToB amendments, our Triage, VQ & Due Diligence Questionnaires model process to help you deliver and fully record best practice outcomes
- **Integrity** - deliver your advice from a clear & neutral perspective
- **Specificity** - ready made templates, granular in detail, spanning the Sustainability spectrum, raise your market participation in this fast evolving space. Have greater ability to match funds to target (and negative target) markets
- **Demystifying** - OK, you don't know what you don't know and what is it that you should learn so you can talk about all this? Our compliance framework will help you see through the fog! If you have any training needs - we are here to help
- **Modelling behaviour changes** - New clients and annual reviews; start using our VQ's, see how positively staff and clients react, share the news, tell the story - a compelling incentive for client engagement at multi-generational advice
- **Tailored messages** - this is for the longevity of your firm! Your client bank - wealth shift - intergenerational planning
- **Clear calls to action** - simple action via our templates, future-proofed compliance framework, sign up for a year, we will up-date and respond to incoming regulatory changes

- **Behaviour change** - make behaviour change a central part of a comprehensive strategy
- **Fairness** - The ESG Accord framework covers the full ESG and Sustainable Finance spectrum - it is for ALL clients - putting client values first in a repeatable, reportable, compliance friendly way



- **Cutting costs:** Saving many work-hours and staff training costs to your firms; we've made all the templates you'll need
- **Foresight and phasing** - when you've got the right framework you can make the real planning decisions - which clients first, when to introduce? Exit planning strategy for firm - retain your value by demonstrating appropriate client segmentation
- **Making it easy** - Raised likelihood of suitable outcomes!
- **Get in touch.** Let's book a no obligation meeting
- **admin@esgaccord.co.uk**
- **www.esgaccord.co.uk**



## RESOURCES

[www.esgaccord.co.uk](http://www.esgaccord.co.uk)

[LinkedIn - ESG ACCORD](#)

[LinkedIn - Elly Dowding](#)

[LinkedIn - Lee Coates OBE](#)

### Trade body

- UK Sustainable Investment & Finance Association.  
<https://uksif.org/>

### Regulatory issues

- Letter from Rishi Sunak to the FCA. [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/972445/CX\\_Letter\\_-\\_FCA\\_Remit\\_230321.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/972445/CX_Letter_-_FCA_Remit_230321.pdf)
- FCA Handbook PROD 3.3 <https://www.handbook.fca.org.uk/handbook/PROD/3/3.html?date=2018-04-01&timeline=True>