

## Interview with Michael Maldener, Managing Director and Conducting Officer of Nordea Investment Funds S.A., and Cecilia Siegbahn, Regulatory Expert

### EU ESG Regulation

Please note that the conference call occurred on the 10<sup>th</sup> of March 2021. All market commentary and information refers to the period before then.

#### Key takeaways

- March 10<sup>th</sup> is a landmark date introducing broader transparency around sustainability-related disclosure in the Asset Management Industry.
- The next landmark, when the RTS comes into force (expected to be January 1, 2022) is just around the corner – start preparing now.
- Advisors get prepared for MiFID II Delegated Acts changes on internal governance, data processes and training of staff.
- Become familiar with your firm's strategy and consider what Nordea can do to help you make this change.

#### What has changed today, March 10<sup>th</sup>?

As of March 10<sup>th</sup> 2021, asset managers have to publish various disclosures. At the entity level, we have published our PAI statement – how we integrate PAI, or Principle Adverse Impact, into our investment process. (Fund level PAI will not be published until 2022.) We have published updated precontractual material - prospectuses - that show how we consider sustainability factors in our funds, and we have added various sustainability-related policy documents to our website. The third leg of the disclosures will be periodic reporting, but that doesn't start until 2022.

#### Where do we stand regarding the PAI as of now?

We have published our policy on PAI at entity level on our website. At NAM we do integrate PAI, or Principle Adverse Impact, into the investment process of all our strategies. However, since we have made our entity-level PAI statement from the bottom-up, we have already considered the impact at fund level, even though the fund-level disclosures will not be published until 2022. This fund-level PAI has also been part of our classification of funds into Article 8 and 9, so that's another reason we have already looked more deeply at the PAI.

The reporting requirements presented in the final draft of the Level II regulation is much less onerous than the initial expectation. At first, the scope included thirty-two mandatory sustainability indicators to consider as well as 2 out of a list of voluntary ones. Now, the scope has narrowed to fourteen mandatory indicators as well as the two voluntary ones – although there are a few additional voluntary ones related to specific asset classes, such as sovereign bonds or real estate. However, even with this much narrower set of requirements that acknowledges the data challenge, the burden is still quite substantial.

As an example, we are still missing KPIs for topics such as biodiversity and waste. If you consider a software company, we need to ascertain whether this investment's activities negatively effect biodiversity. At this stage, the data simply isn't there. However, the introduction of the NFRD, next levels of taxonomy and voluntary standards will help. The other helpful aspect is that this is assessed on a "best efforts" basis; if we can demonstrate that we have tried to get the data, up to a point this will be sufficient.

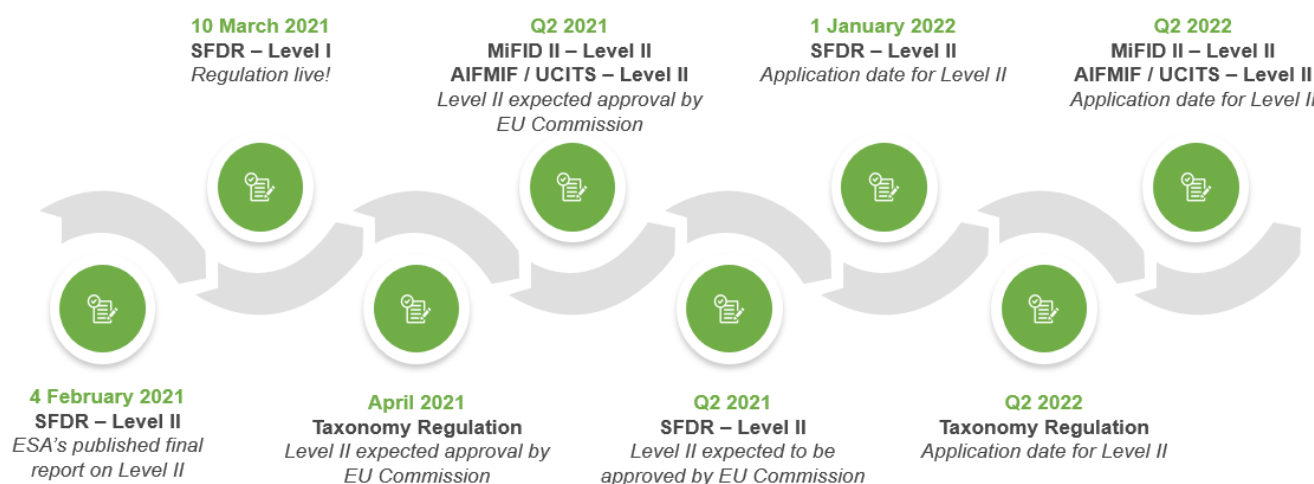
## How prescriptive is the regulation, at the granular level?

This is an interesting one. When we have classified funds as Article 6, 8 or 9, it is clear that there is quite a lot of discretion given to individual managers. There is a wide range of ESG approaches and the way they are used; the message is that there is discretion if how you choose to apply ESG criteria, but you need to be precise in your documentation and disclosure.

We see much more scope for standardisation within the actual reporting and disclosure requirements. The SFDR level II requires the pre-contractual disclosures to be in a very standardised format with little to no discretion for the product manufacturer. This will give much greater transparency and allow investors to make easier comparisons between different products. However, the regulation isn't yet as prescriptive as we would like and at this time no market practice has been established.

## What are we expecting next?

In Q2 2021 we expect the publication of a number of key “next steps”. We expect the publication of Taxonomy's RTS (Regulatory Technical Standards), which will, when in force, be very useful in making available the data we need to support our own SFDR disclosures for sustainable investments. We also expect to see level 2 approvals for the MiFID II and AIFMIF/ UCITS regulation and also the level 2 approval for the SFDR. This SFDR level 2 regulation, which will require more detailed disclosure in areas we are already reporting on, will become applicable at the start of 2022, while the others are expected to have a 12-month lead-time, bringing them into force in Q2 2022.



## What should fund distributors and advisors be doing now?

The real game-changer for distributors and advisors will be the changes to MiFID II - the requirement to include sustainability preferences into the suitability assessment for clients. Checking sustainability preferences will become an integral part of giving financial advice. Advisors need not only to be able to assess client preferences, but also to know which solutions meet the client's needs and to answer questions about why. In order to implement this, distributors are having to consider their internal governance, data processing and training of staff.

While we are still waiting for the final details of the MiFID changes, this is the time for distributors to be ensuring they have in place the right systems and structures to support advisors through this process.

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