MAYER | BROWN
Sustainability & Structured Products
THE VIEW FROM EUROPE AND GERMANY
20 May 2020

Overview

1. **Introduction**
   1.1 Sustainability in the context of financial products
   1.2 Overview of sustainable debt investing
   1.3 Market overview
2. **European Union**
   2.1 Regulatory response by the European Union
   2.2 Action Plan on the Financing of Sustainable Growth
   2.3 Taxonomy Regulation
   2.4 Disclosure Regulation
   2.5 Low Carbon Benchmark Regulation
   2.6 EU Green Bond Standard and the EU Ecolabel for financial instruments
   2.7 MIFID II amendments: ESG preferences and target market
3. **Consequences for Sustainable Structured Products**
4. **Further developments**

1.1 Sustainability in the Context of Financial Products

- Overall goals of the EU in the fight against climate change:
  - Meeting the 1.5°C (<2°C) goal of the Paris Climate Change Agreement
  - Turning Europe into a climate-neutral continent by 2050
- Objectives regarding financial products:
  - Increasing **transparency** for investors when considering sustainable financial instruments in their investments (*ESG preference*)
  - Encouraging **capital flow** into areas that promote the UN's Sustainable Development Goals and addressing the financial risks of climate change
  - Taking sustainability into consideration with regard to the **risk management** of financial market participants
  - Promoting **trust and integrity** in the developing sustainable finance industry

1.2 Overview of Sustainable Debt Investing

Sustainable Finance (ESG Investing)

Green (Environmental) Finance

Specific goals such as *pollution*, *biodiversity* etc.

Climate Finance: *mitigation and adaption*

Types of green debt instruments:

- Bonds with green use of proceeds
- Structured Products linked to a green index
- (Structured) bonds linked to green performance indicators (ESG KPIs) of an issuer

Social Finance

Social issues and outcomes, e.g. employee health and safety, labor standards in the supply chain, product safety

Currently: COVID-19 related financing

Governance Finance

Business ethics, corruption and political instability, conflicts of interest, tax transparency

Impact Investing

This graph represents a snapshot of current terms and categories used by market participants and regulators (including "green", "ESG", "ethical", "SDG", "impact", "sustainable" etc.). It is by no means binding and any of the included terms may be used differently in any given context. The purpose for this presentation is to provide a context for the Structured Products discussed in the following slides.

1.3 Market Overview (1/2)

- The market segment of sustainable debt investing, specifically green finance experienced a significant upswing following the **Paris Agreement** in 2015
- The Paris Agreement created substantial demand for sustainable financial instruments
- Data from the European System of Central Banks demonstrates the associated growth of such instruments in Europe, particularly with regard to green bonds:
  - Increasing volumes of green bonds and other sustainable investments (including climate bonds)
  - Increasing interest by investors, both retail and institutional, in integrating their ESG preferences and requirements into their investment approach

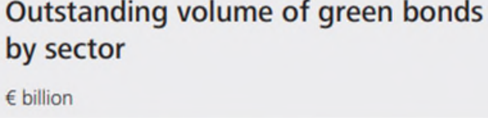
The five largest issuers of green bonds in Germany as of Q2 2019

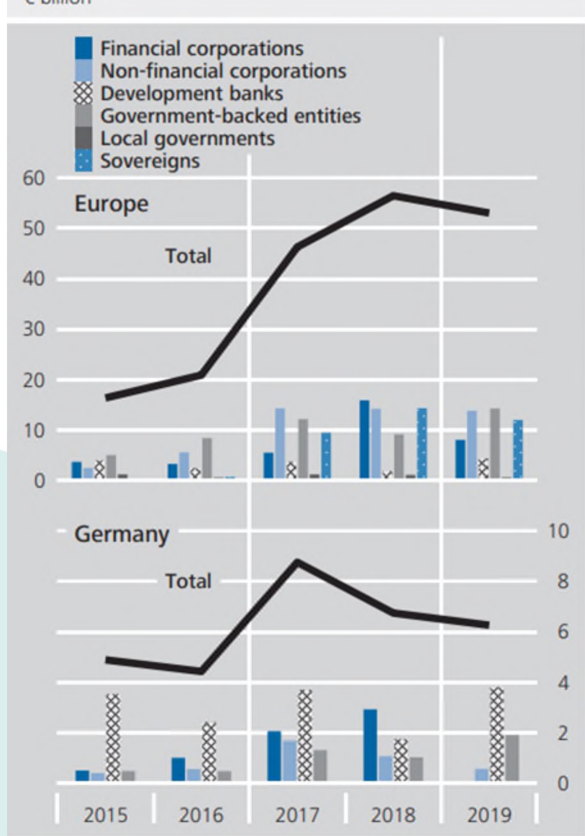
Issuer	Number of bonds	Issue volume (EUR billion)
KfW*	22	18.0
NRW.BANK	7	3.3
Berlin Hyp	6	3.0
LBBW	4	2.7
Deutsche Hypo	4	1.1

Source: Climate Bonds Initiative as at 30 June 2019. Deutsche Bundesbank
* also one of the top issuers worldwide in 2019

- New developments in the market for Structured Products, including first retail green offerings (see e.g. LBBW: Stufenzins-Anleihen Nachhaltigkeit in October 2019) and Structured Products based on green indices (e.g. Solactive: LBBW Research Nachhaltigkeits-Favoriten Aktien-Index)

1.3 Market Overview (2/2)



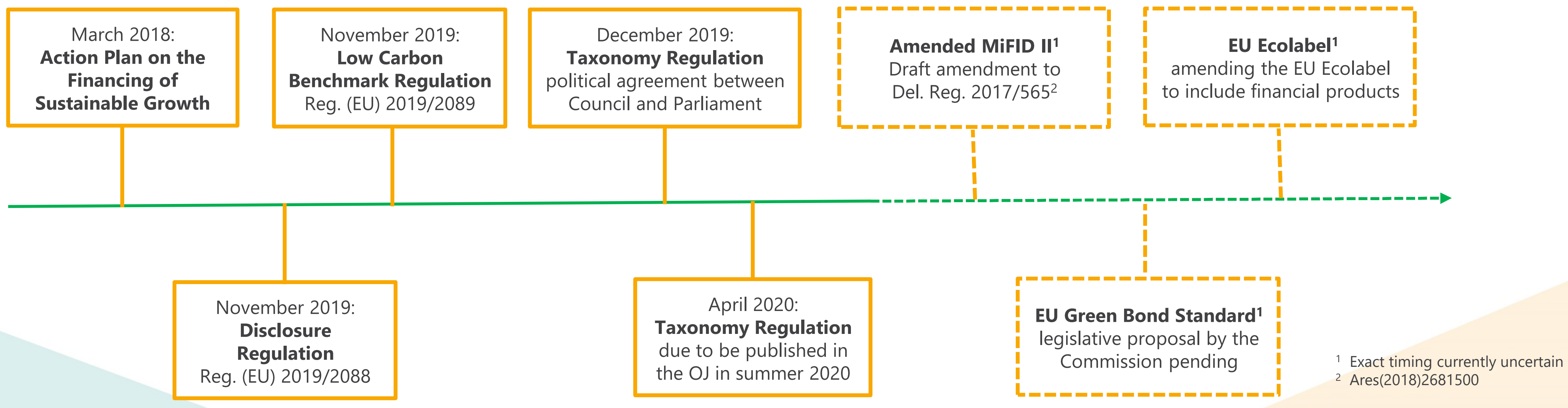


Source: Climate Bonds Initiative, as at 30 June 2019.
Deutsche Bundesbank

- The lack of a consensus on what exactly defines a sustainable investment has been identified as one of the major obstacles for the development of the market for sustainable investments
- The International Capital Market Association (ICMA) published the **Green Bond Principles** (GBP) in 2014 to increase the transparency, integrity and acceptance of green bonds
- The GBP are a set of recommendations for principles and procedures concerning the issuing of Green Bonds and the ensuing use of proceeds
- Other principles have been published, but the ICMA's GBP are the prevailing set of rules used in the German bond market at this time
- No similar standards for (retail) structured products within the EU currently in place

2.1 Regulatory Response by the European Union

- In March 2018 the EU published a comprehensive **Action Plan on the Financing of Sustainable Growth** (COM/2018/097 final) which laid out a master plan to be implemented by a variety of individual regulatory measures:



[1] Exact timing currently uncertain
[2] Ares(2018)2681500

- A change regarding capital requirements and implementation of other sustainable risk regulation for banks are also under discussion
- A number of consultations regarding level 2 measures for the above regulations as well as a consultation on an updated Action Plan are currently being conducted

2.2 Action Plan on the Financing of Sustainable Growth

- Redirection of private capital into sustainable investments
  - To achieve the EU's objectives by 2030, an **investment gap** estimated at EUR 180 to EUR 270 billion per year must be closed by the private market
- Establishment of a regulatory framework:
  - Development of an EU classification system (Taxonomy Regulation)
  - Introduction of sustainability related transparency obligations for financial market participants and financial advisors (Disclosure Regulation)
  - Creation of uniform reference values for low carbon benchmarks (amended Benchmark Regulation)
  - Integration of sustainability in the investor advisory process (proposal for an amendment to the Delegate Regulation (EU) 2017/565 - MiFID II)
  - EU Green Bond Standard and EU-Ecolabel

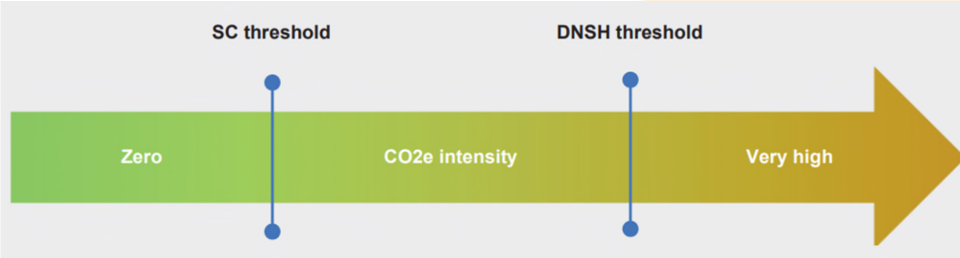
2.3 Taxonomy Regulation (1/3)

- An investment is environmentally sustainable if it finances one or more **economic activities** that are considered environmentally sustainable under the Taxonomy Regulation
- According to the Taxonomy Regulation, an **economic activity**[2] is environmentally sustainable when it:
  - Substantially contributes to one the six defined **environmental objectives**
  - **Does no significant harm** to any of the other five objectives
  - Complies with **minimum safeguards**
- For the time being, the regulation is limited to the determination of environmental sustainability (at a later stage the objectives "social" and "governance" will be included)
- Suggested details can be found in the Technical Report of the TEG on Sustainable Finance and its Technical Annex

The six environmental objectives under the Taxonomy Regulation:

Climate Change Mitigation	Climate Change Adaptation	Sustainable Use and Protection of Water and Marine Resources
Transition to a Circular economy, Waste Prevention and Recycling	Pollution Prevention and Control	Protection of Healthy Ecosystems

Example of quantitative DNSH analysis[1]:

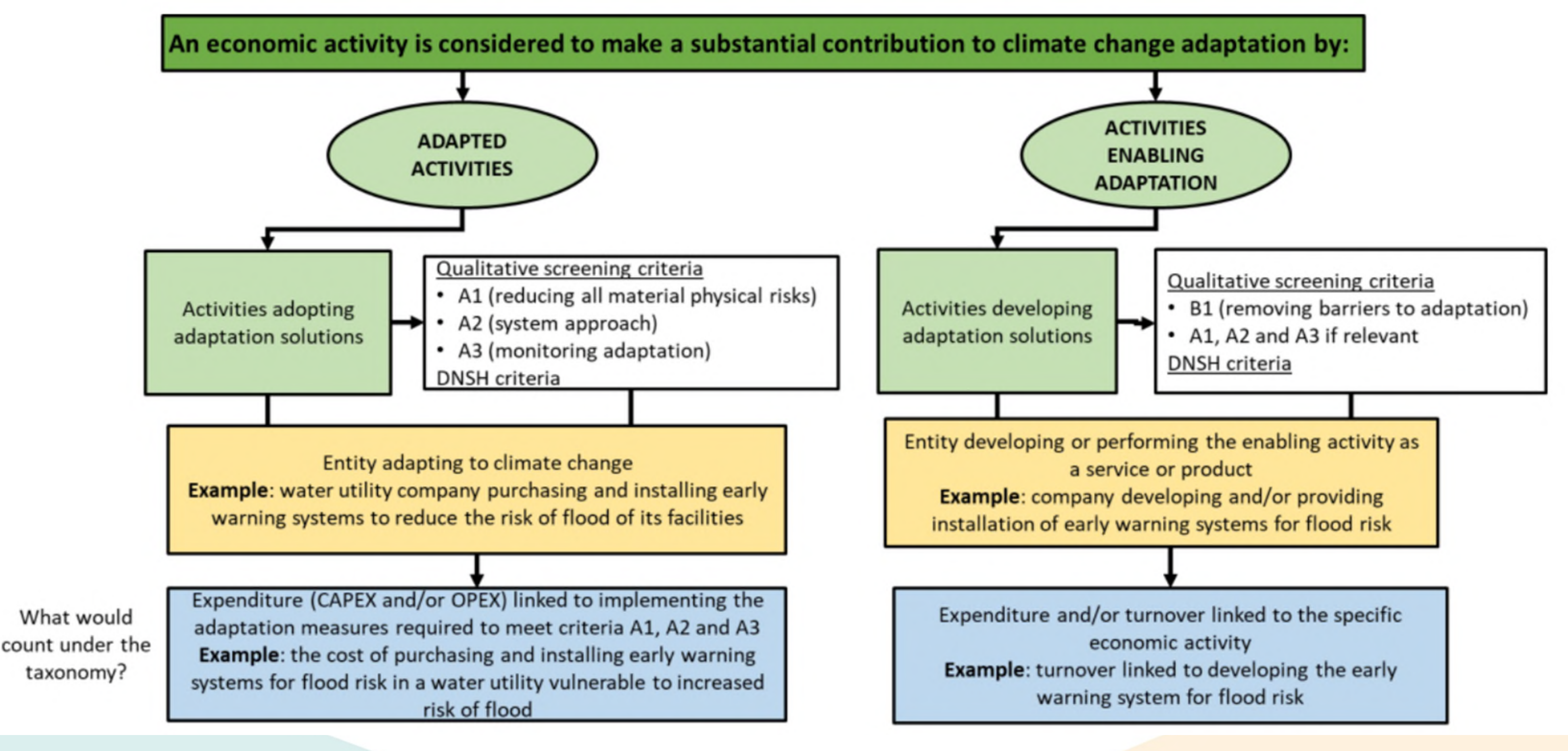


[1] Source: Taxonomy – Final report of the Technical Expert Group on Sustainable Finance, March 2020.

[2] Out of the 21 sectors of the economy according to the EU's NACE classification, 7 were selected at this stage which have particularly high carbon emissions. The Technical Expert Group has identified 67 economic activities in these sectors which contribute significantly to the environmental objectives.

2.3 Taxonomy Regulation (2/3)

Example of the technical implementation in the Technical Annex with respect to climate change adaptation:



Source: Taxonomy Report: Technical Annex – Updated methodology & Updated Technical Screening Criteria, March 2020, p. 22.

2.3 Taxonomy Regulation (3/3)

- Scope of the Taxonomy Regulation through references in the Non-Financial Reporting Directive and the Disclosure Regulation:
  - **Who?** EU and its Member States as well as companies already required to report under the Non-Financial Reporting Directive and financial market participants and financial products pursuant to the Disclosure Regulation
  - **What?** Financial Products (meaning a portfolio management, an AIF, an IBIP, a pension product, a pension scheme or a UCITS):
    - Pre-contractual documentation (e.g. investor information documents, as provided for by the relevant EU regulations for the specific product/service)
    - Websites
    - Periodic reports
- Required compliance for activities related to climate change mitigation and adaptation starts in 2022 and for other environmental objectives in 2023. However, disclosure of information in 2022 relates to activities in the financial year 2021.

2.4 Disclosure Regulation (1/2)

- Scope of the Disclosure Regulation:
  - **Who?** Financial market participants and financial advisers
  - **What?** Sustainability-related information with respect to financial products
  - **Where?** Websites, pre-contractual disclosures, reports
- Transparency obligations are either product-related or process-related with regard to financial market participants and financial advisers
- Noteworthy provisions with regard to **financial products**:
  - Art. 7: financial market participants should disclose, by 30 December 2022 at the latest, clear and substantiated explanations for any financial product as to whether and - if so - how in a financial product the most significant negative impacts on sustainability factors are taken into account
  - Art. 8: for financial products that promote, amongst other, environmental or social characteristics, information on how these characteristics are met.
  - Art. 9: for financial products that seek to have a positive environmental and social impact, financial market participants should disclose the sustainability benchmark they use to measure sustainability performance and, if no benchmark is used, explain how the sustainability objective is achieved

2.4 Disclosure Regulation (2/2)

- Noteworthy provisions with regard to **indices**:
  - Art. 8: financial market participants that issue financial products with environmental or social characteristics must disclose whether and how the particular index - be it a sustainability index or a standard index - is oriented towards these characteristics
  - Art. 9: pre-contractual disclosures have to include information on how the index is aligned with the sustainable investment objective and how it differs from a broad market index
  - Art. 11: periodic reports must include a comparison between the overall sustainability impact of the financial product with the impacts of the chosen index and of a broad market index through sustainability indicators

2.5 Low Carbon Benchmark Regulation

- The Amendment to the Benchmark Regulation (=Low Carbon Benchmark Regulation) establishes minimum standards with regard to certain low carbon benchmarks
- Notably, the changes to the Benchmark Regulation include:
  - Distinction between low carbon and positive carbon impact benchmarks, implementation of two new types of climate benchmarks:
    - **EU Climate Transition Benchmarks (CTB)**
    - **EU Paris-aligned Benchmarks (PAB)**
    - Both of which are subject to transparency and basic methodological requirements
  - General ESG transparency obligations for all benchmarks (Art. 27 (2) of the Low Carbon Benchmark Regulation)
- Original date of application was 30 April 2020, however as a response to a joint letter by several industry associations, ESMA issued a no action letter on 29 April 2020 regarding any supervisory action until the corresponding level 2 measures have been put into place

2.6 EU Green Bond Standard and the EU Ecolabel for Financial Instruments

- The European Commission aims to adopt an EU-wide **Green Bond Standard** (legislative proposal pending):
  - EU Technical Expert Group on Sustainable Finance published a proposal in June 2019 with recommendations
  - Any EU Green Bond would have to be aligned with the Taxonomy Regulation
  - Potentially mandatory disclosure of sustainability-related information under the Prospectus Regulation
  - Adherence shall remain voluntary
- **EU-Ecolabel** for financial instruments to be introduced (under consultation):
  - Amendment to the existing Ecolabel Regulation (Reg. (EC) 66/2010)
  - The Joint Research Centre (JRC) presented a Technical Report in December 2019 which includes suggested criteria
  - Current suggested scope does not include Structured Products
  - Voluntary distribution

2.7 MIFID II Amendments: ESG Preferences and Target Market

- With regard to the distribution of financial instruments (i.e. not only financial products in the narrower sense of the Taxonomy Regulation), amendments to MIFID II are being intended:
  - Investment firms providing investment advice or portfolio management shall as part of their suitability assessment also ask the client for its "ESG preference" and investment firms should offer such products that corresponds with such ESG preference
  - Investment firms shall also provide clients in good time before the provision of investment services with a general description of the nature and risks of financial instruments, also taking in account in particular any "ESG considerations"
- In addition, amendments to the target market determination as part of the product governance requirements are intended with respect to an ESG financial instrument
  - Based on such anticipated changes, for example, the German industry developed amendments to the minimum target market standards providing for two sustainable product types:
  - **ESG Products** (in principle corresponding to Art. 8 Disclosure Regulation products promoting environmental or social characteristics) having an underlying with an ESG strategy
  - **ESG Impact Products** (in principle corresponding to Art. 9 Disclosure Regulation products with sustainable investment objectives) having a direct funding impact towards a sustainable economic activity

3. Consequences for Sustainable Structured Products (1/2)

- Due to anticipated changes to MiFID II, distributors will rely on issuers to supply ESG products, since any investor asking for a product with an ESG preference must be offered such product
- (Retail) structured notes are not financial products within the meaning of the Disclosure Regulation or the Taxonomy Regulation
  - Pending further guidance on the interpretation of Art. 4 of the Taxonomy Regulation regarding the scope of the term "corporate bonds" in this context (however the language of recital No. 15 of the Taxonomy Regulation indicates that a corporate bond is issued by non-financial companies only)
- However, since these products are typically marketed to investors through financial advisory (where the amended MiFID II will apply), these products will most likely have to adhere to them same standards "voluntarily"
- The issuer of a structured product will typically use the proceeds to (re-)finance sustainable economic activity of a third party under an established (voluntary) framework in accordance with e.g. the Green Bond Principles or other new (voluntary) industry guidelines

3. Consequences for Sustainable Structured Products (2/2)

- The eligibility of such products as sustainable investments will be indirectly regulated by the Taxonomy Regulation
- The EU Green Bond Standard may replace any pre-existing industry standards for the EU market (including frameworks)
- A financial product may be automatically considered to be a sustainable financial product, if the issuer can demonstrate that 50% (all of this still under discussion) of its economic activity are sustainable within the meaning of the Taxonomy Regulation

4. Further Developments

- On 11 December 2019, the newly elected European Commission proposed a **European Green Deal** which comprises several policy initiatives
- As part of the European Green Deal, an **EU Climate Law** has been proposed which aligns the EU's efforts between different policy areas, the impact of which in the field of sustainable finance remains to be seen
- There is a possibility that international carbon markets will experience renewed interest as a result of the Paris Climate Agreement which, together with the strengthening of the EU's carbon price, could lead to increasing interest in **carbon as a commodity**
- A consultation is currently being conducted regarding possible amendment to the **Non-Financial Reporting Directive** in line with the Commissions overall efforts to strengthen sustainable finance

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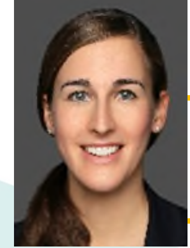

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Team video: **https://www.youtube.com/embed/3ZtAealmfBI**

INDEX, ESG AND VOTING – NOT SO PASSIVE AFTER ALL

May 2020

www.solactive.com

CONTENT

About us 3

ESG Indexing - Basics 4

Recent Trends 5

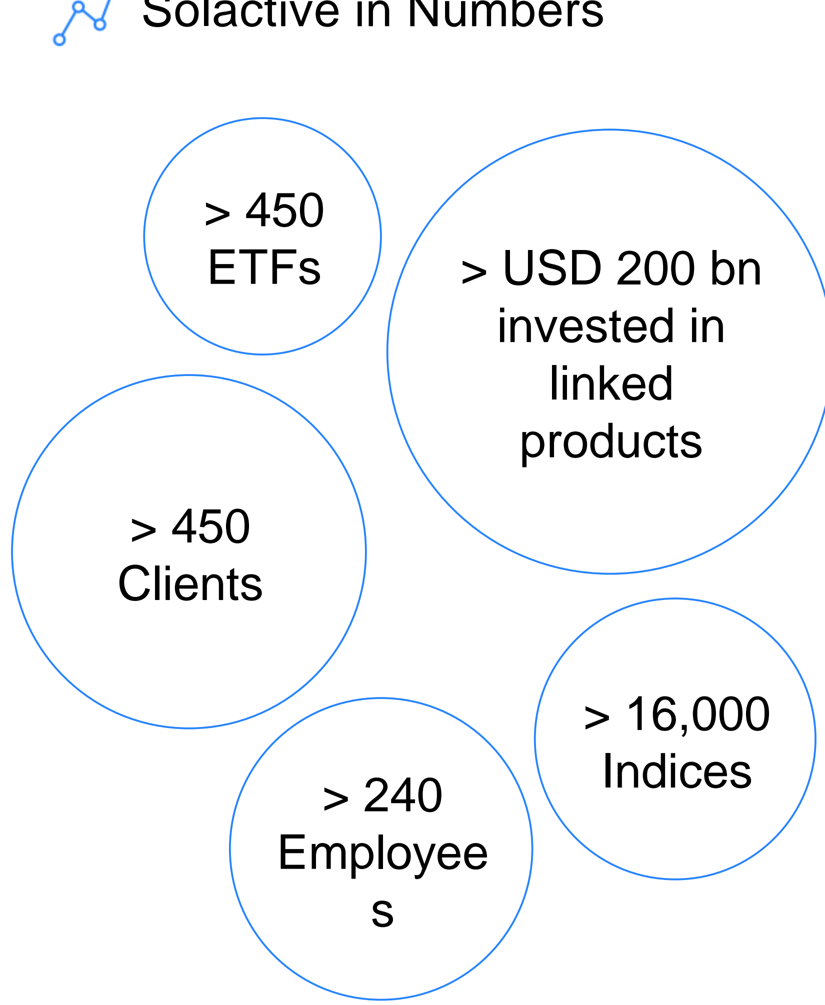
Outlook 8

COMPANY PROFILE

Key Facts

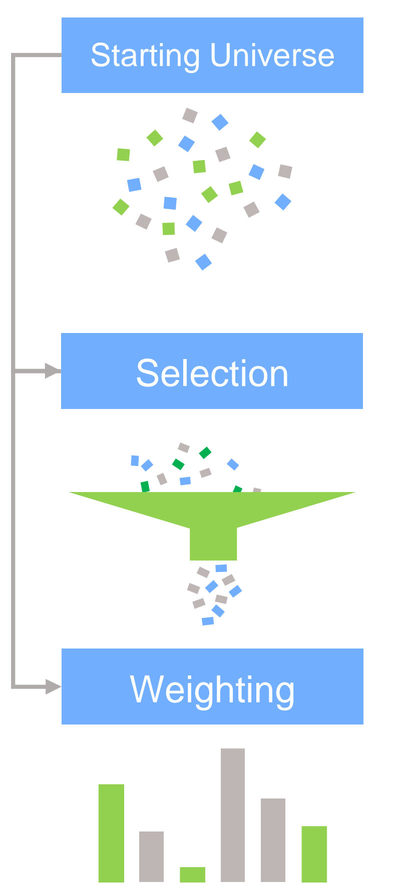
- Solactive is a Germany-based index provider operating globally and growing at a fast pace.
- Since 2007, we have been developing tailor-made and multi-asset class index solutions for ETFs and other index-linked investment products at competitive prices.
- Currently present in Frankfurt, Dresden, Berlin, Toronto and Hong Kong to give a 24h coverage. Our ambition is to continue expanding our footprint in order to better serve our clients around the world.

Solactive in Numbers



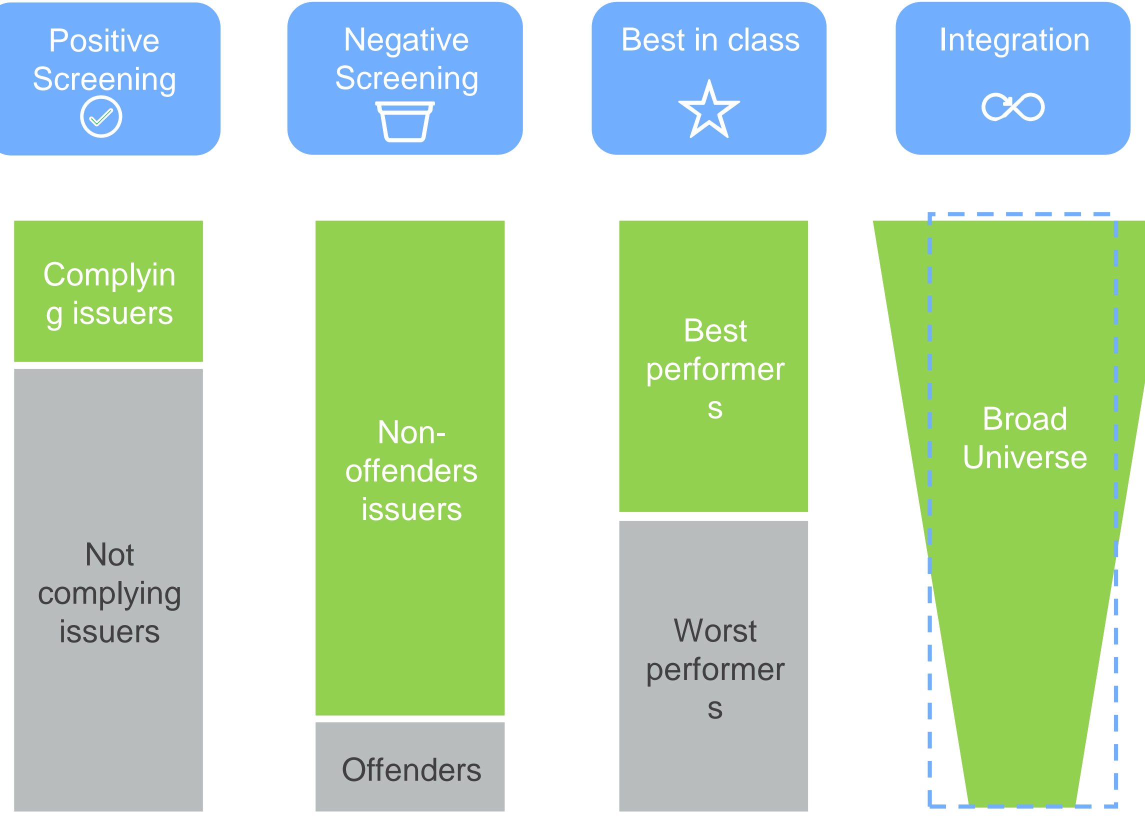
ESG INDEXING - BASICS

Flexible construction of an ESG index



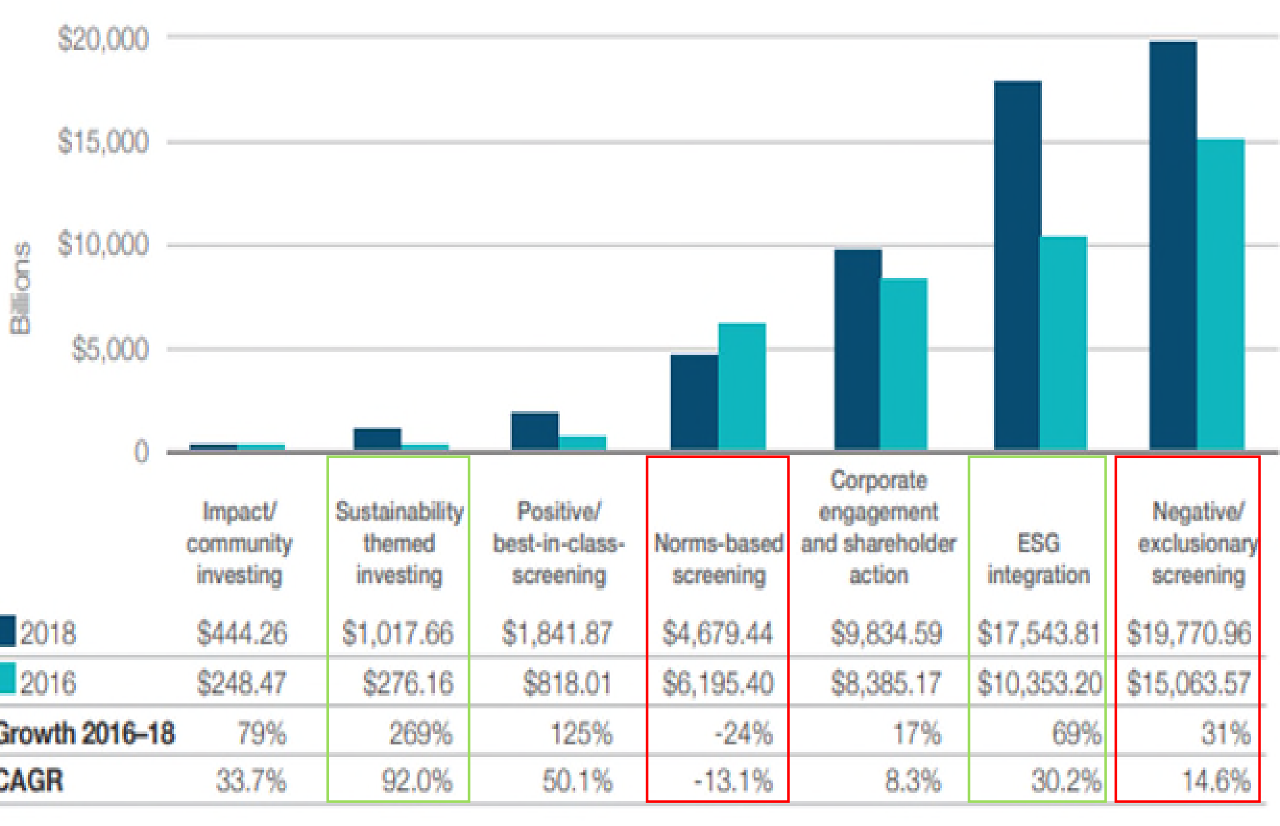
- Example cases:
  - Starting with an ESG compliant universe, based on the UN Sustainable Development Goals.
  - Narrowing the universe by selecting the best-in-class companies, i.e the best ESG scores in each sector.
  - Final composition is weighted according to Market Cap, ESG scores or a combination of both (“ESG tilt“).
- Other smart beta factors, such as low volatility and high dividend criteria, can also be incorporated → important for pricing aspects of structured products.

Four ways of taking ESG data into account for indices:



THE EVOLVING LANDSCAPE – STRATEGIES & ASSETS

Global growth of sustainable investment strategies 2016-2018



	Impact/ community investing	Sustainability themed investing	Positive/ best-in-class-screening	Norms-based screening	Corporate engagement and shareholder action	ESG integration	Negative/ exclusionary screening
2018	$444.26	$1,017.66	$1,841.87	$4,679.44	$9,834.59	$17,543.81	$19,770.96
2016	$248.47	$276.16	$818.01	$6,195.40	$8,385.17	$10,353.20	$15,063.57
Growth 2016–18	79%	269%	125%	-24%	17%	69%	31%
CAGR	33.7%	92.0%	50.1%	-13.1%	8.3%	30.2%	14.6%

- Increased asset flows
- Migration from “traditional” exclusions-based approaches to ESG integration.
- Climate-focused strategies in high demand recently → introduction of two new EU benchmarks will continue to drive demand.
- COVID-19 will lead to increased focus on governance side.

Source: 2018 Global Sustainable Investment Review

THE EVOLVING LANDSCAPE – REGIONAL ASPECTS

European Union

- Demand driven by market and regulatory initiatives
- Asset Owners:
  - Fiduciary Duty
  - Major Role in driving demand for standardization on the data side as well.
- Regulators:
  - Many political initiatives: EU green deal, climate stress testing by the Bank of England, EU action plan for sustainable finance.
  - Major development for indexing industry: Introduction of two new EU Climate Benchmarks + Disclosure requirements for ESG indices:
    - Climate Transition Benchmark
    - Paris-Aligned Benchmark
    - Disclosures regarding ESG factors used in the methodology + key ESG KPIs

United States

- Market-driven demand
- Asset Owners take leading role as well:
  - CalPERS and New York State Common Retirement Fund adopted rules to consider ESG factors in their investment decisions.
- But regulatory initiatives are sprouting slowly:
  - ESG Disclosure Simplification Act of 2019: would require SEC to define ESG metrics that companies have to disclose.
  - SEC proposed changes to regulation S-K: intended to simplify issuers’ reporting on material risk factors → would require companies to report on human capital management issues as a material risk.
  - Illinois Sustainable Investing Act (ISIA): state agencies to consider sustainability factors in all aspects of their investment decisions if profitable and risk-minimizing.

EU BENCHMARKS – THE SMALL PRINT

Starting Universe: Solactive GBS Developed Markets Europe Large & Mid Cap Index

Climate Transition Benchmark (CTB)		**Paris-Aligned Benchmark (PAB)**
Selection		
Baseline exclusions: controversial weapons & societal norms violators		
No activity exclusions	Electricity producers with carbon intensity of lifecycle GHG emissions higher than 100gCO2e/kWh (>50% Revenue)	Natural Gas (>50% Revenue from Coal exploration or processing activities)
	Oil (>10% Revenue from Oil exploration or processing activities)	Coal (>1% Revenue from Coal exploration or processing activities)

Weighting

Constraints

CTB	PAB
Carbon intensity reduction at inception: 30% vs benchmark	Carbon intensity reduction at inception (vs. benchmark): 50%

Sectors: Exposure to High Climate Impact Sectors ≥ exposure in the Benchmark. High Climate Impact Sectors: Agriculture, Forestry and Fishing, Mining and Quarrying, Manufacturing, Electricity, Gas, Steam and Air Conditioning Supply, Water Supply, Sewerage, Waste Management and Remediation Activities, Construction, Wholesale and Retail Trade, Repair of Motor Vehicles and Motorcycles, Transportation and Storage, Real Estate Activities.

Individual: Companies in the index receive a minimum weight of half the weight in the Benchmark and a maximum weight of twice the weight in the Benchmark.

Year-on-year self decarbonisation

At least 7% on average per annum. This is not measured against a benchmark but describes decarbonization of the index itself over time.

EXPANSION OF THE PRODUCT ECOSYSTEM

Index

- Methodology guided by clients' specific view on ESG.
- Liquidity, representation of underlying market, tracking error, risk metrics, smart beta etc.).

Voting

- Custom voting policy assures extension of ESG principles and views used to construct the index.
- Efficient implementation through third-party proxy voting agents.

Additional Services

- Reporting of key ESG indicators on the index and fund level (e.g. driven by EU regulation) increases transparency.
- Monitoring of company policies through proxy voting agents.

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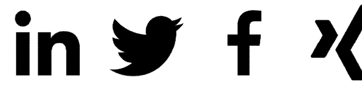

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U.S. Regulatory Focus on “ESG”

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Regulatory Focus on "ESG"

- U.S. Regulators are concerned about deceptive advertising relating to "ESG"
- SEC Office of Compliance Inspections and Examinations ("OCIE") 2020 Examination Priorities Letter:
  - "OCIE has a particular interest in the accuracy and adequacy of disclosures provided by registered investment advisers offering clients new types or emerging investment strategies, such as strategies focused on sustainable and responsible investing, which incorporate environmental, social, and governance (ESG) criteria."

Varying SEC ESG Viewpoints

- SEC Commissioner Hester Peirce's June 2019 speech:
  - "Self-identified ESG experts" producing scorecards and ratings, with no precise metrics, and lots of judgments;
  - Public companies bombarded with ESG surveys, some with hundreds of questions, using a company's resources in order to respond; and
  - Others produce ESG ratings without contacting the company at all, basing the results on misinformation.
- ESG scores/ratings affect whether and how companies are included in ESG-related indices and funds

SEC Investor Advisory Committee Recommendation

- The Investor-as-Owner Subcommittee of the SEC Investor Advisory Committee's recommendation relating to ESG disclosure (May 14, 2020)
  - Acknowledges "patchwork" nature of current ESG disclosure outside of the United States and a "lack of clear disclosure obligations" in the United States
  - Acknowledges the problem of "plethora" of ESG data providers in the United States, all with different standards and criteria
  - These providers create a burden on companies with their questionnaires and response requirements
- Recommendation:
  - SEC should "begin in earnest an effort to update the reporting requirements of issuers to include material, decision-useful, ESG factors."

Recent SEC Statements on Indices

- SEC Chair Jay Clayton speech on Nov. 4, 2019:
  - Chair Clayton questioned whether investors and their advisers understood how indices are constructed from a technical perspective (e.g., weightings and adjustments), the opportunities and risks of an investment referencing the index and the types of key value adjustments that the index administrator may make, such as what types of companies are included in the index.
    - Chair Clayton also asked whether more disclosure should be encouraged or required
- Dalia Blass, Director, Division of Investment Management, in a speech on Dec. 3, 2019, in the context of funds linked to indices with constituents in emerging markets, suggested that funds address the following risks in their disclosure documents:
  - What are the risks in using unreliable or outdated information when assessing if a constituent should be included in an index?
  - What if the issue is not just the quality of the information but that the index provider has access to partial or very limited information?

Recent SEC Statements on Indices *(cont'd)*

- What are the limitations, if any, in assessing the index provider's due diligence process?
  - These concepts could also apply to an ESG-based index.

Request for Comment on the Names Rule

- SEC Request for Comment on Rule 35d-1 under the Investment Company Act of 1940 (the "Names Rule")
  - As a general matter, the Rule requires a fund to invest at least 80% of its assets in the manner suggested by its name
  - The Rule does not apply to fund names that describe a fund's investment objective, strategy or policies
  - Regulation of fund names is intended to address concerns that certain fund names may mislead investors about a fund's investments
  - The SEC stated that the number of funds with investment mandates that include criteria that require some degree of qualitative assessment or judgment of certain characteristics (such as funds that include one or more environmental, social, and governance-oriented assessments or judgments in their investment mandates (e.g., "ESG" investment mandates)) is growing. These funds often include these parameters in the fund name.
  - The SEC staff has observed that some funds appear to treat terms such as "ESG" as an investment strategy and thus not subject to the Rule, while others appear to treat "ESG" as a type of investment that is subject to the Rule.

Request for Comment on the Names Rule *(cont'd)*

- Concern with misleading index name:
  - The constituents of indices underlying a fund may not always be closely tied to the investment suggested by the fund's name
  - Raises questions under the Rule when the fund name uses the name of the index

SEC Request for Comment

- The SEC specifically asked whether the Rule should apply to terms like "ESG" or "sustainable."
  - Are investors relying on these terms as indications
    - Of the types of assets in which a fund invests or does not invest (e.g., investing in carbon-neutral companies, avoiding oil and gas companies);
    - Of the fund's investment strategy (e.g., investing with the objective of bringing value-enhancing governance, asset allocation, or other changes to the operations of the underlying companies);
    - That the funds' objectives include noneconomic objectives; or
    - Of a combination of the above?
  - Should the Rule impose specific requirements on when a particular investment may be characterized as ESG or sustainable, and, if so, what should those requirements be?
  - Should there be other limits on a fund's ability to characterize its investments as ESG or sustainable? For example, ESG (environment, social, and governance) relates to three broad factors. Given that, must a fund select investments that satisfy all three factors to use the "ESG" term?

SEC Request for Comment *(cont'd)*

- For funds that currently treat "ESG" as a type of investment subject to the Rule, how do those funds determine whether a particular investment satisfies one or more "ESG" factors, and are these determinations reasonably consistent across funds that use similar names?
  - If "ESG" is treated as a strategy, not subject to the Rule
- Instead of tying terms such as "ESG" in a fund's name to any particular investments or investment strategies, should the Rule instead require funds using these terms to explain to investors what they mean?

Regulation S-K – Proposed Rule Changes

- Regulation S-K governs disclosure in registration statements and reports filed under the Securities Exchange Act of 1934.
- On January 30, 2020, the SEC proposed changes to the Management's Discussion and Analysis ("MD&A") disclosure rules and the Selected Financial Data and Supplementary Financial Information rules.
- What the proposal does, in broad outline, is keep to a "principles-based" approach, rather than prescribing specific items to be disclosed.
- Reaction from SEC Commissioners shows the two ends of the spectrum:
  - Hester Peirce: MD&A provides a narrative explanation of a company's financial statements; the principles-based approach allows management to disclose information material to an investment decision;
    - "[t]he concept of materiality is at risk of degradation … [w]e face repeated calls to expand our disclosure framework to require ESG and sustainability disclosures regardless of materiality."
    - "Materiality does not turn on what is important to non-investors or to a select group of investors motivated by objectives unrelated to or only tangentially connected to their investment's profitability."

Regulation S-K – Proposed Rule Changes *(cont'd)*

- Allison Lee: "[T]he proposal is notable in what is does not do: make any attempt to address investors' need to standardize disclosure on climate risk."
- SEC Chair Clayton: "[A]s a standard setter, I should not be substituting my operational and capital allocation judgments for those of issuers and investors."

Green Bonds – What Are They?

- Green Bonds might be thought of as a form of socially responsible investing – aligning investor interest in environmentally-sound projects with their desire to invest in fixed income securities
- There is no uniform definition of a "Green Bond" but it is generally thought of as a debt security the proceeds of which have been earmarked for use in special projects that advance environmentally friendly objectives
  - Investments in renewable energy, energy efficiency, climate-friendly projects
- From a legal perspective, a "Use of Proceeds" Green Bond is a traditional (usually) senior debt obligation of the issuer that pays a coupon but it is distinguished by the specificity of the use of proceeds

Types of Green Bonds

- Use of Proceeds Bond – traditional debt security the proceeds of which are earmarked for use in advancing certain eligible investments
- Revenue Bond – non-recourse to the issuer; the credit exposure is to pledged cash flows of the revenue stream. Proceeds are ring-fenced or tacked by the issuer and tied to the issuer's investments in the project
- Project Bond – for single or multiple projects, where the investor has direct exposure to the project
- Asset-Backed Bond – collateralized by one or more specific projects

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