



ACRONYMS TO ACTION

DEMYSTIFYING SUSTAINABLE FINANCE JARGON

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1. INTRODUCTION

The climate crisis is the existential challenge to economic and social sustainability of our time. Key regulatory initiatives are driving forward climate sensitive investing faster than ever and understanding how your fund is impacted by these developments is a pre-requisite to meeting your fiduciary and regulatory objectives.

Minerva has been helping investors navigate environmental, social and governance (ESG), and sustainability reporting for over 20 years. We realise that sustainable investing can be a bewildering task, with an alphabet soup of acronyms and terms clouding the way forward for your organisation as a fiduciary.

For those who are just starting their journey in sustainable finance, this Minerva Briefing will answer the questions: What is sustainable finance? Why is it important? What are the key terms, organisations, and initiatives you should be aware of as an investor? And how can you feed the resources available into an action plan for your organisation?

Key Summary

- Sustainable finance is the process of taking environmental, social and governance (ESG) considerations into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects.
- Sustainable finance has evolved significantly over recent years, with a long list of regulatory bodies and frameworks now in place to guide investors toward detailed sustainability reporting.
- Sustainable investing is here to stay no matter the acronyms and frameworks that surround it. Minerva can help you translate your climate policy into a fully-fledged investment framework using climate indices and sustainability ratings

2. WHAT IS SUSTAINABLE FINANCE?

The European Commission defines sustainable finance as “the process of taking environmental, social and governance (ESG) considerations into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects.”ⁱ This does not mean there is a trade-off between sustainable investment and strong returns, as its inherent long-term approach may protect against social and environmental risks.

2.1 THE EVOLUTION OF SUSTAINABLE FINANCE

1700s	<p>Socially Responsible Investing (SRI)</p> <p>The first major concept to lead toward modern sustainable finance is Socially Responsible Investing (SRI). This usually refers to the exclusionary approach that many investors take to portfolio management, removing exposure to specific sectors such as alcohol or gambling. This method is also known as “negative screening”. SRI or ethical investing has its roots in religious movements on both sides of the Atlantic dating back to as early as the mid-1700s, with Quakers and Methodists arguing against the slave trade and then later involvement in so-called ‘sin stocks’ of alcohol and tobacco.</p>
2004	<p>ESG Investing</p> <p>As concepts of socially responsible investing developed, the scope began to widen to consider ESG issues. The term “ESG” was first coined by the World Bank report ‘Who Cares Wins’ in 2004.ⁱⁱ It represented a departure from the narrow applications of social outcomes-based investment. ESG investing encourages an inclusionary approach to investing, seeking out companies with strong environmental, social, and governance practices that may provide a source of long-term value not captured by traditional financial analysis.ⁱⁱⁱ This approach is also referred to as “positive screening”, and although it is seen as a hallmark of ESG investing, many ESG-aware investors still rely heavily on negative screening.</p> <p>Over time, ESG investing has become synonymous with the term ‘responsible investing’, a term that pre-dates ESG investing as a distinction from solely socially focused investing. The responsible investment movement grew at a rapid pace throughout the early 2000s and culminated in the founding of the Principles for Responsible Investment, an independent organisation supported by the United Nations.</p>
2007	<p>Impact Investing</p> <p>Impact Investing is a growing area interest for investors that expands beyond the usual confines of ESG investing. Impact investments are made with the explicit intention to generate positive ESG outcomes whilst also closely measuring and disclosing the degree of impact being made.^{iv} There is no standard way of performing this measurement. One example of impact investing is the establishment of “green bonds” that dedicate their proceeds to combatting climate issues.</p>
2015	<p>Sustainable Investing</p> <p>Sustainability is the concept that social, economic, and cultural development can meet the needs of the present without preventing the ability of future generations to meet their own needs.^v Originally established in 1987 by the Brundtland Report^{vi}, it was popularised in 2015 by the 17 Sustainable Development Goals (SDGs) established as the centrepiece for the UN’s Agenda 2030.</p> <p>Based on the UN definition of sustainable development, sustainable investing came to be defined by its recognition of ESG factors as economic factors, especially in the long term. The Bridges Spectrum of Capital in 2015 outlined the difference between responsible and sustainable investment, saying responsible investment sought to “mitigate risky ESG practices in order to protect value”, while sustainable investment aimed to “adopt progressive ESG practices that may enhance value.”^{vii} Similarly, to the original emergence of ESG, the conversation continues to revolve around the shift from negative screening, toward positive screening.</p>

2.2 REGULATORY BODIES & FRAMEWORKS (A-Z)

The many years of developments in sustainable finance has shaped today's sustainability reporting landscape. Sustainability reporting is defined as "an organisation's practice of reporting publicly on its most significant economic, environmental and social impacts", and hence its contributions – positive or negative – toward the goal of sustainable development.^{viii} Starting from the now-outdated concept of socially responsible investing, sustainability reporting today considers a range of ESG and sustainable development issues.

The process of sustainability reporting is governed by a long list of regulatory bodies and frameworks that guide investors. As global concern around the climate crisis has increased, many of these frameworks have particularly focused on climate reporting and environmental impact.

CDP

[CDP](#) (formerly the Carbon Disclosure Project) is a UK-based not-for-profit charity that runs a global disclosure system for investors, companies, cities, states, and regions to manage their environmental impacts.^{ix} They are widely recognised as providing gold standard environmental reporting with a rich and comprehensive dataset on corporate and city action. To date they work with over 590 investors managing over US\$110 trillion in assets, and disclosing through CDP on issues like climate change, water security and deforestation.

CDSB

The [Climate Disclosure Standards Board](#) (CDSB) is a non-profit, international consortium of business and environmental NGOs. They aim to advance and align the global mainstream corporate reporting model to equate natural capital with financial capital. Investors may benefit from the work of the CDSB by making informed and robust capital allocation decisions based on improved climate disclosure by companies. Importantly, the CDSB produces a Framework for reporting environmental and climate change information.^x

SFDR

The Sustainable Financial Disclosure Regulation (SFDR) was adopted by the European Commission in 2019 and came into force in March 2021. It requires all financial market participants, including asset managers, institutional investors, financial advisers involved in investment products, and all entities offering financial products where they manage clients' money to publicly disclose their adverse impacts on sustainability.^{xi} The regulation is particularly significant as it obliges investors to not only consider the material impact of ESG factors on their investments, but to also consider the negative material effects their investment decisions have on the environment and society, known as 'double materiality'.

EU Taxonomy

The [EU Taxonomy](#) Regulation was published in the Official Journal of the European Union on 22 June 2020 and entered into force on 12 July 2020. It is a classification system, establishing a list of environmentally sustainable economic activities.^{xii} The EU taxonomy is an important enabler to scale up sustainable investment and to implement the European Green Deal. Notably, by providing appropriate definitions to companies, investors, and policymakers on which economic activities can be considered environmentally sustainable, it is expected to create security for investors, protect private investors from greenwashing, help companies to plan the transition, mitigate market fragmentation and eventually help shift investments where they are most needed.

GRI

The [Global Reporting Initiative \(GRI\)](#), formed in 1997, provides widely used, freely available standards for companies to report on their sustainability – the GRI Standards. The organisation was originally convened by the non-profit organisations CERES and the Tellus Institute (with involvement of the UN Environment Programme).^{xiii}

Taskforce on Climate-related Financial Disclosure

The Financial Stability Board established the [Taskforce on Climate-related Financial Disclosure \(TCFD\)](#) to develop recommendations for more effective climate-related disclosures that could promote more informed investment, credit, and insurance underwriting decisions and, in turn, enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks.^{xiv} The Task Force consists of 31 members from across the G20, representing both preparers and users of financial disclosures. The TCFD is chaired by Michael R. Bloomberg, founder of Bloomberg L.P.

In 2017, the TCFD released climate-related financial disclosure recommendations designed to help companies provide better information to support informed capital allocation. Their disclosure recommendations are structured around four thematic areas that represent core elements of how organisations operate: governance, strategy, risk management, and metrics and targets.

The Values Reporting Foundation

As a merging of the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB), the [Value Reporting Foundation \(VRF\)](#) helps investors develop a common language about the financial impacts of sustainability.^{xv} Despite the new name developed for the merger, the VRF still produces 'SASB Standards' that guide the disclosure of financially material sustainability information by companies to their investors. Available for 77 industries, the Standards identify the subset of ESG issues most relevant to financial performance in each industry.

Transition Pathways Initiative

The Transition Pathway Initiative (TPI) is a global, asset-owner led tool that assesses companies' preparedness for the transition to a low carbon economy.^{xvi} The TPI was established in 2017 as a joint initiative between the Church of England National Investing Bodies and the Environment Agency Pension Fund. The TPI is governed by the TPI Steering Group and consists of representatives from asset owners who are significant sponsors of the initiative.

TPI assesses companies on two dimensions: Management Quality and Carbon Performance. FTSE Russell, a TPI partner, provides the climate change and corporate governance related data that underpins the first dimension, the initiative's Management Quality framework. Following the release of the TCFD recommendations, FTSE Russell aligned their methodologies and criteria, accordingly, allowing investors to now use the TPI as a tool to assess TCFD compliance.

UK Taxonomy

The Green Technical Advisory Group, an expert group chaired by the Green Finance Institute and composed of key financial market stakeholders, has been commissioned by the UK government to produce a taxonomy of its own.^{xvii} Announced in November 2020, the UK government claims the taxonomy will be science-based and comprised of technical screening criteria that focus on net-zero in the UK context. When the taxonomy will be formally legislated is unknown, but a strong precedent has been set by the EU taxonomy, and the government spokespeople are confident the UK Taxonomy will be an excellent opportunity to become a global leader in green finance.

“A UK green taxonomy will provide better data on the environmental impact of firms, supporting investors, businesses and consumers to make green financial decisions and accelerating the transition to net zero.”.

John Glen MP, Economic Secretary to the Treasury, 2020

UN SDGs

The [United Nations Sustainable Development Goals](#) is a collection of 17 goals adopted by the UN member states in 2015 to achieve the 2030 Agenda for Sustainable Development.^{xviii} The SDGs provide a blueprint for countries to achieve a more sustainable future, including ending poverty and hunger, improving health and education, combating climate change, and protecting oceans and forests. While the SDGs were created for UN member states, the UN Global Compact and GRI have joined forces to help businesses report on the SDGs. Ensuring your own investing behaviours are SDG-aligned is an important step for getting ahead of the game as sustainable finance becomes the new normal.

Principles for Responsible Investment

The United Nations in 2005 supported the launch of the [Principles for Responsible Investment \(PRI\)](#), an independent organisation that helps investors incorporate ESG factors into their investment and ownership decisions.^{xix} The international network of investor signatories has grown from 100 to over 2,300, representing over \$80 trillion in assets under management. The six principles are a set of voluntary investment principles, supported by 35 possible actions, that investors can use to integrate ESG into investment practice. The PRI has specifically aligned its work with the UN SDGs and has also made TCFD-based reporting mandatory for its signatories in 2020.

For more information on the wider lexicon of sustainable finance, including terms such as impact investing, natural capital, and net zero, Minerva recommends the resources made available by the [Stockholm Sustainable Finance Centre](#).

3. UNDERSTANDING SUSTAINABLE FINANCE

Sustainable finance has become a key component of any investor's considerations. Not only have reporting standards around social and governance issues become far more mainstream in recent years, but the environment has also rushed to the forefront of regulatory developments. Governments are rapidly developing stringent and compulsory sustainability disclosure rules for companies and investors alike, many of which revolve around the climate crisis.

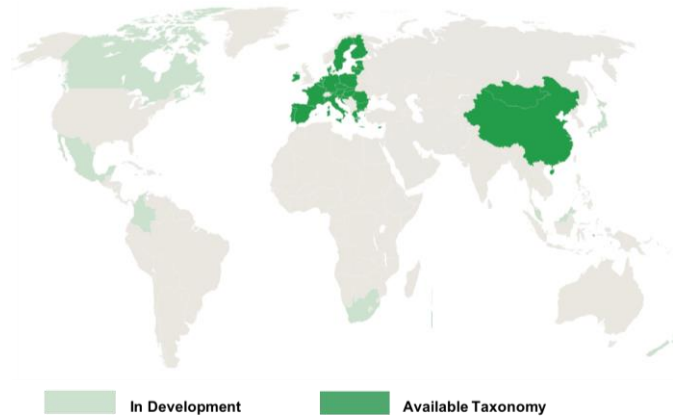


Figure 1 - Global green taxonomy development^{xx}

Transitioning to a low carbon economy poses significant risks and opportunities for investors' portfolios. The market-wide migration from carbon-intensive activities to a low or zero-carbon economy requires a dynamic and adaptable response from investors to mitigate their climate risk; manage their carbon price risk, understand the feasibility of business models amidst ever-stricter climate regulations, and of course protect against the possibility of stranded assets.

Low-carbon and zero-carbon companies, and companies that are well-positioned for transition are highly likely to become a more attractive investment option due to demand for their products and services increasing and their low exposure to transition risks. Minerva's philosophy is to understand the governance of sustainability by issuers, with emphasis on their disclosure of sustainability risks, management, and accountability.

Beyond the fiduciary duty of investors to protect their portfolios from climate risk, the financial sector has a key role to play in reaching the SDGs. It can:

1. shift investments toward more sustainable technologies and businesses;
2. finance economic growth in a sustainable manner over the long-term;
3. help create a low-carbon, climate resilient and circular economy.^{xxi}

“Fair, transparent and consistent reporting on climate-related risks and opportunities is key to collectively delivering on the Paris Agreement”.

Financial Conduct Authority

4. NEXT STEPS

Sustainable investing is here to stay no matter the acronyms and frameworks that surround it. We hope that demystifying deciphering some of the confusing terminology has helped start the conversation in your own organisation.

Once the conversation has started, climate aware and sustainable investment policies and governance structures are the starting point. Resources from the many organisations and frameworks detailed within this document will help you to achieve these first steps but translating policy into a fully-fledged investment framework requires climate indices and sustainability ratings for your portfolio that are compliant with the international climate frameworks including the TCFD, the TPI, the SDGs, and the EU Taxonomy.

The sustainable finance landscape is continuously evolving, and although this briefing helps to demystify the confusing mess of acronyms and frameworks, there are encouraging moves toward standardised sustainability reporting. The TCFD is gaining ground as a common set of principles-based guidelines for sustainable investment. Likewise, the new Sustainability Standards Board set to be launched at COP26 by the International Financial Reporting Standards Foundation may produce internationally viable sustainability standards in due time.

Minerva, together with our strategic shareholder, [Solactive](#), is ready to help investor managers integrate climate and sustainability into their strategy. Our services are aligned with many of the frameworks and regulatory bodies outlined in this briefing, including the SDGs, the TCFD, the GRI, and TPI.

To find out more, say hello@minerva.info.

About Minerva

Minerva helps investors and other stakeholders to overcome data disclosure complexity with robust, objective research and voting policy tools. Users can quickly and easily identify departures from good practice based on their own individual preferences, local market requirements or apply a universal good practice standard across all markets.

For more information, please email hello@minerva.info or call + 44 (0)1376 503500

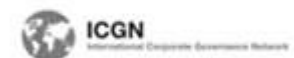
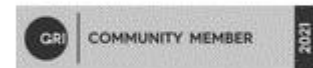
Other Briefings Available

- Board Evaluation in Europe
- Board Gender Diversity in Europe
- Board Independence – A Global Review
- Chair Independence
- Cybersecurity
- Employee Board Representation in Europe
- Global Research and Voting Policy Guidelines 2019
- Investment Association Remuneration Guidelines
- Shareholder Rights Directive II
- Sustainability and Remuneration
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- Regulatory Round-up
- Voting Trends



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ENDNOTES

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