

Faculty of Law, Economics and
Finance - University of Luxembourg

SUSTAINABLE INVESTMENT FUNDS IN THE AIFMD II: AN OUTLOOK

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Based on Zetzsche/Bodellini, Towards Sandbox Thinking in EU
Sustainable Finance Regulation (Working Paper, 6/22),
www.ssrn.com/abstract=4147295



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OVERVIEW

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- I. Subject Matter: AIFMR (April 2021 package) & AIFMD II
- II. AIFMDL2 (AIFMR) and UCITSD L2 changes
- III. AIFMD II (Modest) Changes
- IV. Legislation ↔ Challenges
- V. Solution(s)?

I. SUBJECT MATTER

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Sustainability-related provisions of:

a

- **Commission Delegated Regulation 2021/1255** amending AIFMR (April 2021 package) – applicable from 2 August 2022
- UCITS ManCOs in **Commission Delegated Regulation 2021/1270** amending Directive 2010/43/EU (UCITSD L2)

b

- **AIFMD II Review** (proposal of November 2021)

II. AIFMD & UCITSD L2 CHANGES

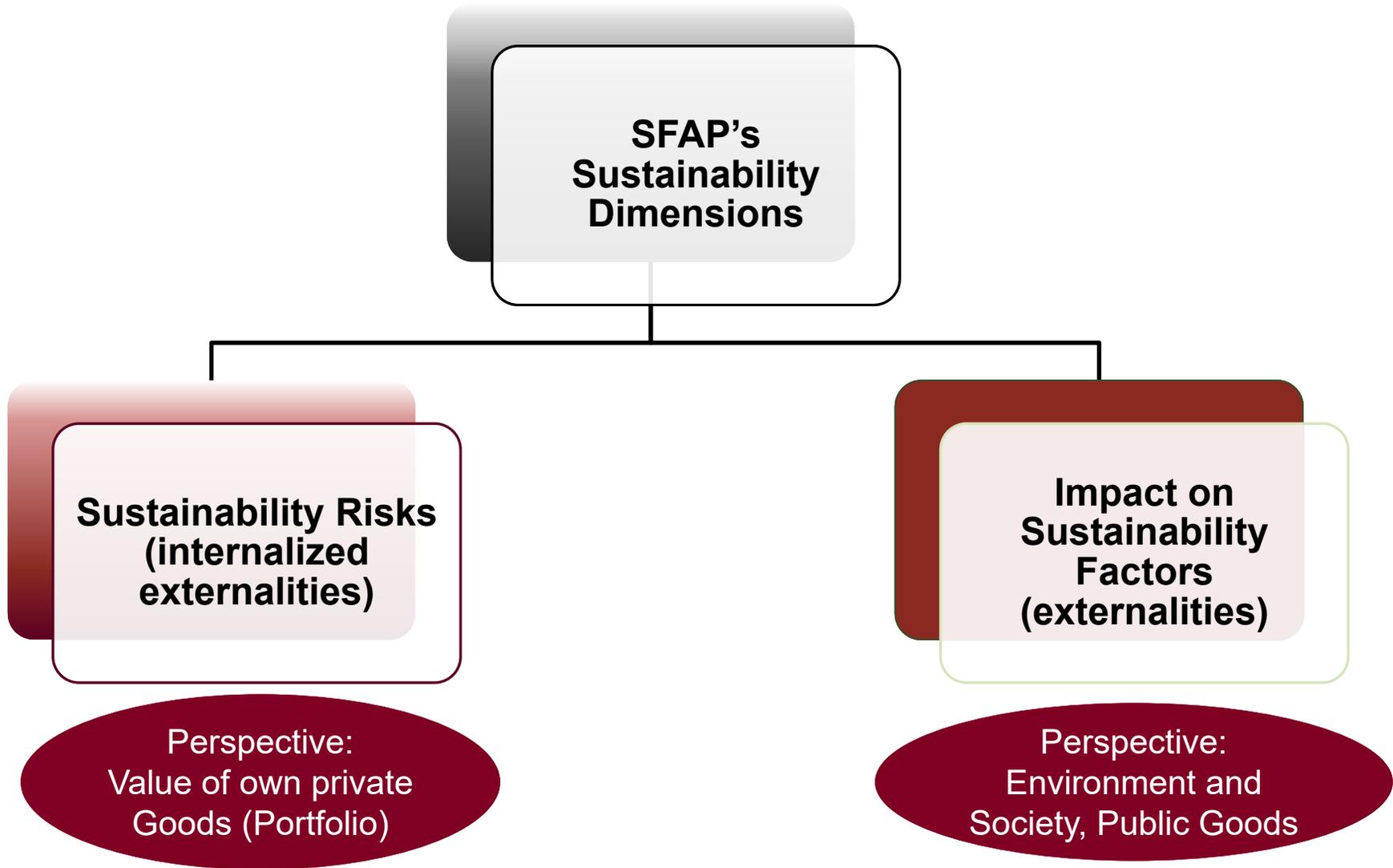
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AIFMD & UCITSD L2
specify ManCo's operating
conditions (e.g. due
diligence, conflicts of
interest, resources)

L2 amended to clarify how to
integrate sustainability risks and
sustainability factors in ManCo's
operating conditions

TERMINOLOGY: DOUBLE MATERIALITY



KEY CHANGES TO AIFMD & UCITSD L2

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1)

'sustainability risk' and 'sustainability factors' defined as in SFDR **(double materiality)**.

2)

ManCo's organization, processes, systems and internal controls to reflect sustainability risks; specific resources, technical capacity & knowledge needed.

3)

If ManCos consider PAIs on sustainability factors (Art. 4 SFDR): disclosure of how due diligence processes take PAIs into account.

4)

Conflicts of interest to include those from the integration of sustainability risks in the ManCo's organisation.

III. KEY PROVISIONS OF AIFMD II REVIEW PROPOSAL

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The **key provisions of the AIFMD II Review Proposal do not concern sustainability** and relate to:

1.

Delegation

2.

Liquidity management

3.

Loan origination (indirect references to sustainability)

A VIEW ON THE AIFMD II CONSULTATION OF OCTOBER 2020

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Full section on ESG/ sustainability (p. 77 et seq.)

- Question 91. Should **investment decision processes** of any AIFM **integrate the assessment of non-financial materiality**, i.e. potential principal adverse sustainability impacts?
- Question 92. Should the adverse impacts on sustainability factors be integrated in the **quantification of sustainability risks**?
- Question 93. Should AIFMs, when considering investment decisions, be required to take **account of sustainability-related impacts beyond what is currently required by the EU law** (such as environmental pollution and degradation, climate change, social impacts, human rights violations) alongside the interests and preferences of investors?

A VIEW ON THE AIFMD II CONSULTATION OF OCTOBER 2020

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Full section on ESG/ sustainability (p. 77 et seq.)

- Question 94. The EU Taxonomy Regulation 2020/852 provides a framework for identifying economic activities that are in fact sustainable in order to establish a common understanding for market participants and prevent green-washing. To qualify as sustainable, an activity needs to make a substantial contribution to one of six environmental objectives, do no significant harm to any of the other five, and meet certain social minimum standards. **In your view, should the EU Taxonomy play a role when AIFMs are making investment decisions, in particular regarding sustainability factors?**
- Question 95. Should other sustainability-related requirements or international principles beyond those laid down in Regulation (EU) 2020/852 be considered by AIFMs **when making investment decisions?**

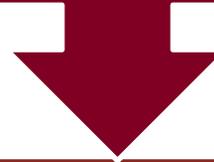
⇒ From nudging to mandatory?

MODEST APPROACH OF AIFMD II REVIEW PROPOSAL

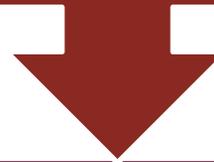
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Commission's plans in October 2020 ⇔ modest sustainability-related proposals in November 2021: Time for breathing?



Lack of evidence for additional steps prior to SFDR RTS' operational effectiveness?

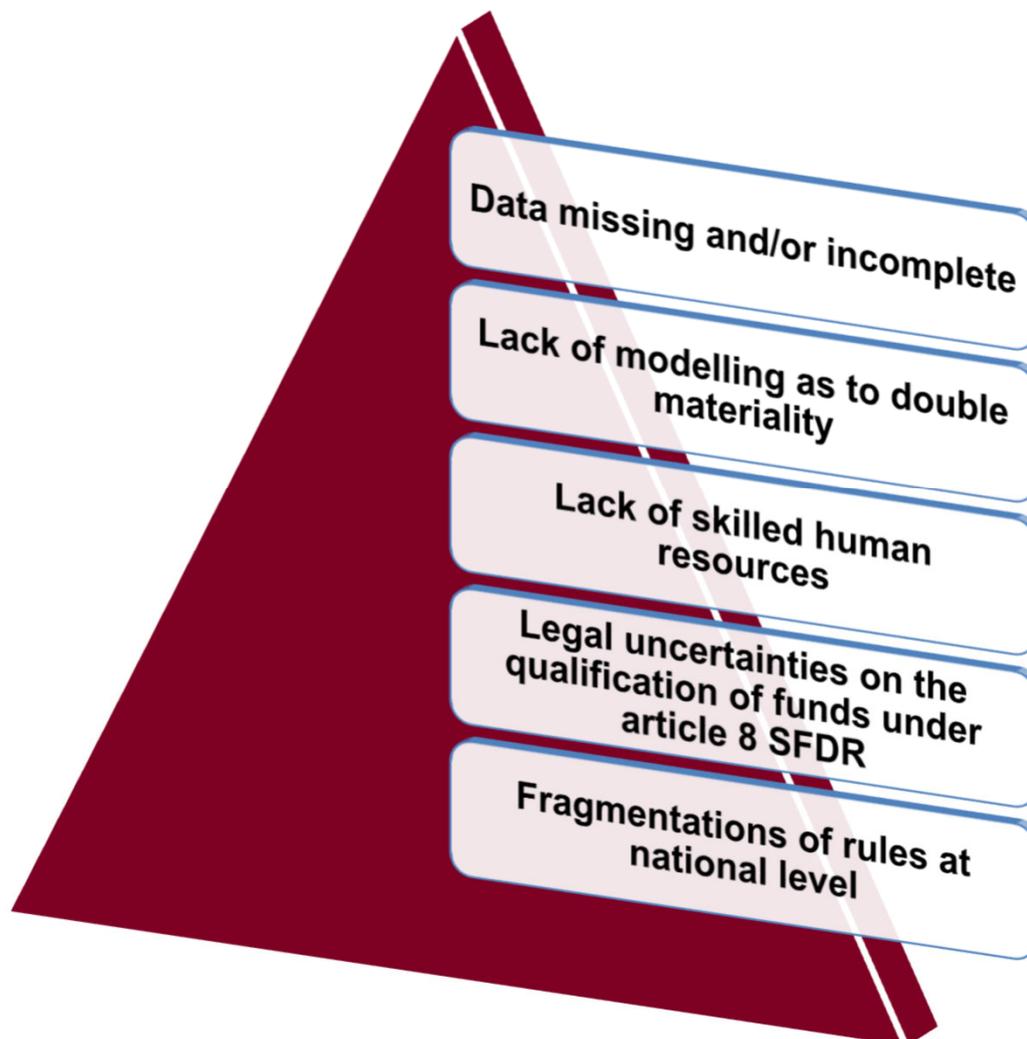


**Fund-specific application of the essence:
Extending obligations to all ManCos and funds may breach fiduciary duties**

IV. LEGISLATION VS CHALLENGES

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Key issues not addressed



V. SOLUTION?

„Sandbox Thinking“

- 1) Regulators & industry to **admit lack of knowledge, data, legal uncertainty, resources, tested models, implementing standards**
- 2) Acknowledge **phase-in period** until gaps are adressed
- 3) Enhanced reliance on **proportionality requirements** in financial legislation and EU treaties on all levels of EU financial regulation and supervision

Phase-in Period:
focus => gap filling by all public
& private actors

Robust
data-based
assessment

Final Period
focus: full compliance

V. SOLUTION?

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Policy approach during phase-in:

- Focus on mutual learning
- Enhanced coordination by ESMA to avoid cross-border fragmentation
- Leniency and transparency on remaining divergence of rules and standards
- Disclosure on *testing of* models, rather than application of (untested) models
- Acknowledge division of labour in delegation chains (PM vs RM)
- Accept estimates if due process (+) (e.g. Official estimates by ministries, Statec etc.)
- Build-up of sustainability data in Single EU Access Point

Thank you!

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For details, see
Zetsche/Bodellini, *Towards Sandbox Thinking in EU Sustainable Finance Regulation*, www.ssrn.com/abstract=4147295



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