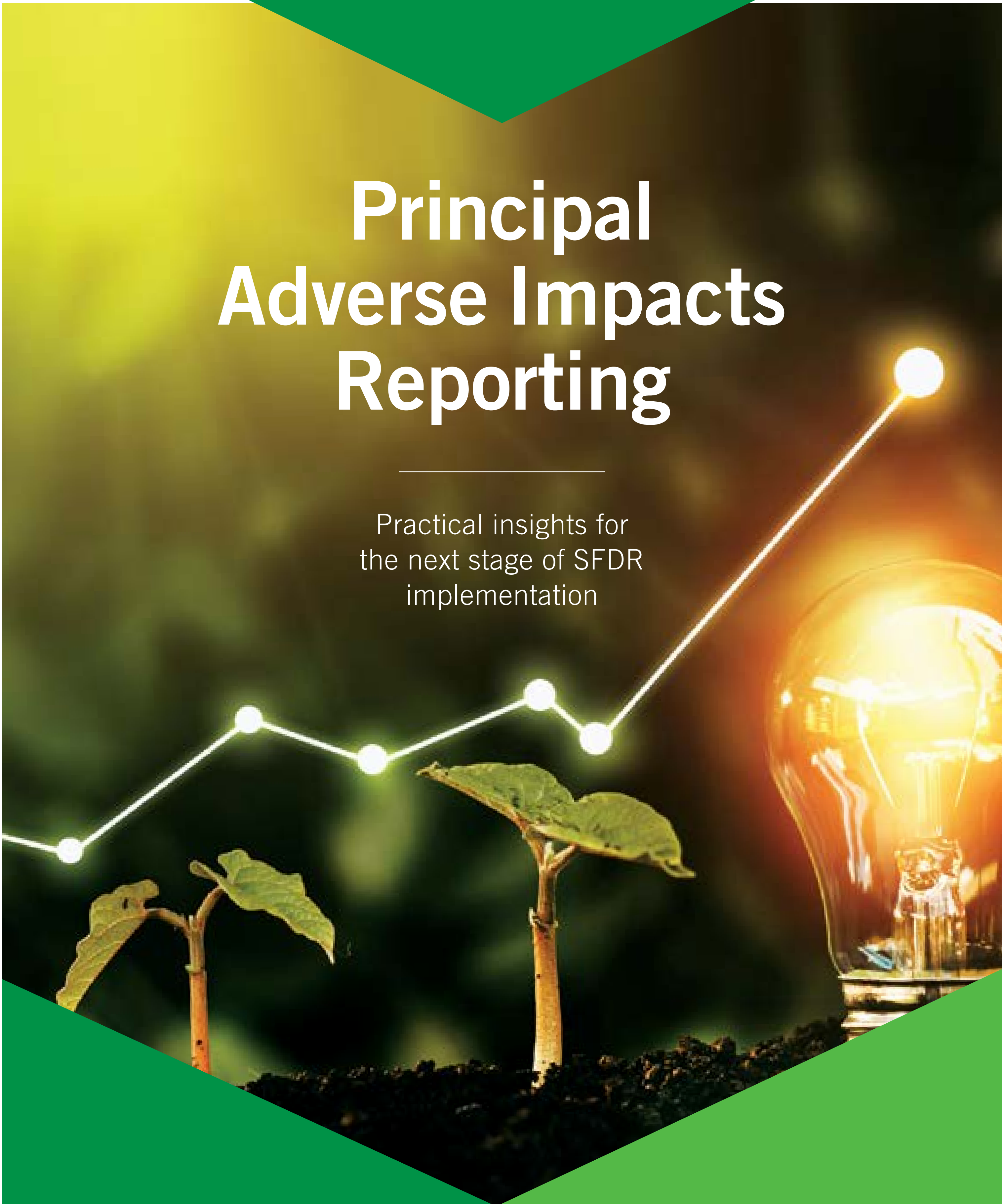
Principal Adverse Impacts Reporting

Practical insights for the next stage of SFDR implementation



irish funds

The EU Sustainable Finance Disclosure Regulation (**SFDR**) has applied on a "Level 1" or high-level principles basis since 10 March 2021. The next significant milestone in the implementation of the SFDR is the application of the detailed "Level 2" measures or Regulatory Technical Standards (**RTS**) which, according to a recent communication for the European Commission, will now apply from 1 July 2022[1], rather than the anticipated 1 January 2022 application date. The delay is intended to facilitate the finalisation and orderly implementation of the consolidated RTS. Notwithstanding this six-month delay, much remains to be done in order to prepare for the reporting of ESG metrics. As well as setting out prescriptive obligations relating to prospectus, periodic and website disclosures applicable to ESG products, the RTS specify the detailed requirements which must be complied with when reporting on the principal adverse impacts (PAI) of investment decisions on sustainability factors. The draft RTS set out the mandatory PAI indicators, as well as optional PAI indicators which may be used for such reporting purposes. This paper focuses on the preparation needed for the reporting of these.

UCITS management companies and AIFMs (**Managers)** that are required (or have opted in) to undertake PAI reporting will need to focus on establishing a framework to report against all relevant PAI indicators. The work involved in this undertaking should not be underestimated. In order to assist Managers in their preparations, this paper provides a Q&A on implementing PAI reporting. Irish Funds has also conducted a survey of ESG data vendors (**Data Vendors)** in order to provide some clarity for Managers on the reality of preparing for PAI reporting. The results of the survey are presented in this paper (see "ESG Data Vendor Survey and Analysis" below).

Through comparing the data provided by the Data Vendors for sample PAI indicators, we assessed the current preparedness of Data Vendors to provide relevant and accurate ESG data required for PAI reporting. Through this exercise we have been able to determine which PAI mandatory reporting indicators are hardest to obtain data for and how comparable reports from different Data Vendors on the same set of securities are. We have also identified some practical considerations Managers should bear in mind when preparing for PAI reporting.

Our findings reveal patchy coverage on several ESG data points and a wide range of variance in the reported data with low levels of comparability.

It is important to note that the data provided by Data Vendors in response to this survey related to relevant ESG data available as of May 2021. This paper does not reflect any changes to Data Vendors' SFDR data offerings following this date and is purely a "point in time" analysis of the availability of data required to provide PAI reporting as at that date.

The findings reveal patchy coverage on several ESG data points and a wide range of variance in the reported data with low levels of comparability. The findings underscore the importance of engaging with Data Vendors and investee companies/issuers now, as well as the evident need to employ a best-efforts approach as a consequence of the challenges arising during the phasing-in of this reporting. It is expected that the quality and availability of PAI reporting will improve over time, as investee companies and Data Vendors adjust, and further regulatory developments aimed at standardisation materialise.

It should be noted that this paper has been prepared on the basis of the draft RTS contained in the ESA Final Report published on 4 February 2021[2] which have not yet been adopted by the European Commission. As noted in this paper, we also await further clarification from the European Commission on the application date of PAI reporting obligations relating to "reference periods". Consequently, the information contained herein may be subject to further change depending on the content of the RTS finally adopted by the European Commission.

[1] Letter from European Commission DG FISMA Director General, John Berrigan, to the Economic and Monetary Affairs Committee of the European Parliament and the Econfin Council, dated 8 July 2021.

[2] ESA Final Report on draft Regulatory Technical Standards Article 2a(3), Article 4(6) and (7), Article 8(3), Article 9(5), Article 10(2) and Article 11(4) of Regulation (EU) 2019/2088, dated 2 February 2021.

The SFDR aims to increase transparency in the investments sector in relation to sustainability. It lays down a new set of disclosure requirements applicable to financial market participants, financial advisors, and financial products. The SFDR takes a broad approach and Managers, as "financial market participants", whether active in the environmental, social and governance (ESG) space or not, are required to comply with certain disclosure requirements relating to the integration of sustainability risks into (i) the investment decision making process at both entity and fund level and (ii) into the remuneration arrangements of the Manager.

Additional disclosure requirements apply in respect of ESG products.

ESG products – Light Green and Dark Green

LIGHT GREEN FUNDS

Funds falling in scope of Article 8 of the SFDR (**Light Green Funds**) are products that promote, among other characteristics, environmental or social characteristics, or a combination of those characteristics. Examples can include:

- Sustainability-themed
- Best in class
- Positive tilt
- Exclusions of particular securities

DARK GREEN FUNDS

Funds falling in scope of Article 9 of the SFDR (**Dark Green Funds**) are products that pursue 'sustainable investment' as their investment objective or which have reduction in carbon emissions as their objective. Sustainable investment is defined as an investment in an economic activity that contributes to an environmental and/or social objective provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices.

Managers categorising their funds as either Light Green Funds or Dark Green Funds will be subject to enhanced disclosure requirements to increase transparency and inform end investors about the sustainability-related performance of those funds relative to the environmental/ social characteristics promoted or the sustainability objectives pursued. Managers of Light Green and Dark Green Funds which are not required due to their size to report on PAIs may choose to do so in order to provide investors with information on the impact that their investment decisions have on sustainability factors.

Dark Green and Light Green Funds in Ireland

To enhance our understanding of the current product categorisation of Irish domiciled funds under the SFDR, we surveyed law firms in the Irish market with respect to the filings made under the SFDR product categories for the 10 March 2021 filing deadline. According to the survey there were:

- 1,023 Ireland-domiciled ESG funds in total, i.e. Light and Dark Green Funds (representing approximately 17% of all Ireland-domiciled funds)
- 896 Light Green Funds (representing approximately 15% of all Ireland-domiciled Funds)
- 127 Dark Green Funds (representing approximately 2% of all Ireland-domiciled Funds)
- 5,159 funds falling under Article 6 representing approximately 83% of all Ireland-domiciled funds

For a detailed overview of the SFDR read our previous publication "SFDR – preparing for compliance".

1 What are principal adverse impacts?

The concept of 'principal adverse impacts' or PAI is intended to capture the impact of investment decisions (and advice) that results in negative effects on sustainability factors. PAI is therefore concerned with how the activities of underlying investee companies impact on sustainability factors, as captured by various adverse impact indicators.

Sustainability factors are defined as 'environmental, social or employee matters, respect for human rights, anticorruption and anti-bribery matters.' PAI and 'sustainability risk' are therefore differing (although interrelated) concepts, the latter being concerned with how sustainability factors could impact on the value of an investment and the former with how the investment itself impacts on sustainability factors.

2 What must be disclosed, by whom and by when?

Under Article 4 of the SFDR, which has applied since 10 March 2021, financial market participants (including Managers) must publish and maintain certain information on their websites relating to the adverse impacts of their investment decision-making process on sustainability factors. This website disclosure obligation is imposed on Managers rather than on individual funds. It applies on a "comply or explain" basis although Managers with an average number of more than 500 employees are required to report on the PAI of their investment decisions on sustainability factors using the template PAI Statement contained in the RTS (PAI Statement). All other Managers can choose to publish a PAI Statement or alternatively explain why they do not do so on their website. Managers complying with the requirement to publish a PAI Statement will need to aggregate the PAI scores at fund level in order to make the PAI Statement at entity level.

The detailed disclosure obligations set out in the RTS, which supplement Article 4 of the SFDR, are now expected to apply from 1 July 2022. These include some qualitative disclosures set out below at question 12. The ESAs had previously clarified in their Final Report on the draft RTS that the information to be reported in respect of a "reference period" (effectively reporting against the relevant PAI indicators) must be published for the first time on or before 30 June 2023, which would cover a reference period running from 1 January 2022 to 31 December 2022. This approach to the phasing in of the PAI reporting was subsequently confirmed in a Supervisory Statement published in February 2021[3]. However, it remains to be seen whether or not this timeframe will be adjusted in light of the European Commission's deferral of the application of the RTS as a whole to 1 July 2022.

3 Are there any prospectus disclosure obligations relating to the principal adverse impacts of investment decisions on sustainability factors?

Under Article 7 of the SFDR, the prospectus of each fund must disclose whether the Manager complies with the reporting obligation imposed under Article 4 of the SFDR and consequently whether it considers principal adverse impacts of investment decisions on sustainability factors in managing the assets of that fund.

Where a Manager does not comply with the PAI reporting requirement introduced under Article 4 of the SFDR, the prospectus of that fund must include a statement that the Manager does not consider adverse impacts on sustainability factors and must provide the reasons for taking this approach. This prospectus disclosure obligation has applied since 10 March 2021.

However, where a Manager does comply with the PAI reporting requirement introduced under Article 4 of the SFDR and takes principal adverse impacts on sustainability factors into account in its investment decision-making, the prospectus of the relevant fund should disclose this fact and should disclose how such impacts are taken into account. This prospectus disclosure obligation does not apply until 30 December 2022.

It is worth noting that the PAI Statement template required to be used for the website disclosures (as described below) does not appear to apply to the prospectus disclosure requirements arising at product level under Article 7 of the SFDR. Instead, it would seem that Managers can tailor the disclosure to the specifics of a particular fund and the PAI indicators used to measure the PAI of that fund on sustainability factors.

[3] Joint ESA Supervisory Statement on the application of the Sustainable Finance Disclosure Regulation, 25 February 2021.

4 What does the PAI Statement contain?

Under the RTS, the PAI Statement will comprise of the following sections:

i. summary;

ii. description of PAI, using PAI indicators;

iii. description of policies used to identify and prioritise PAI;

iv. engagement policies; and

v. adherence to responsible business conduct codes and international standards for due diligence.

Going forward, the PAI Statement must also include historical comparisons covering up to five reference periods against the current reference period in order to ensure adequate comparability of the PAI reports published by the Manager over time.

5 How does a Manager describe the principal adverse impacts of its decision-making on sustainability factors as required under (ii) above?

Each Manager must use PAI indicators to report on the impact that their investment decisions have on sustainability factors in respect of the relevant reference period.

6 What type of PAI indicators must be used?

Mandatory Indicators

Managers are required to report against all "mandatory" indicators laid down in Table 1 of Annex I to the RTS, which capture both climate and environmental-related adverse impacts as well as adverse impacts relating to social and employee matters, respect for human rights, anti-corruption and anti-bribery matters.

These mandatory indicators are further divided into separate indicators which should be used to assess impacts from different types of investments, namely:

i. investments in investee companies (14 mandatory indicators)

ii. sovereigns (and supranationals) (2 mandatory indicators); and

iii. real estate assets (2 mandatory indicators).

The requirement to report against mandatory indicators set out in the RTS is intended to ensure the comparability of PAI disclosures produced by all Managers.

A full list of the mandatory indicators specified by the RTS is included at Appendix A.

Optional indicators

Managers must report against at least one additional "**environmental**" indicator (as set out in Table 2 of Annex I of the RTS) and at least one additional "**social**" indicator (as set out in Table 3 of Annex I of the draft RTS contained in the ESA Final Report).

When identifying additional indicators, the scope and severity of the effects of the adverse impacts should be borne in mind, such as the number of individuals that could be affected or the extent of environmental damage which would result if the adverse impact actually materialised. The likelihood of an adverse impact materialising and whether such an impact, if materialised, could lead to irreparable environmental or social harm should also be considered when selecting optional indicators.

Renewed Strategy on Sustainable Finance

In the Renewed Strategy on Sustainable Finance[4] published by the European Commission in July 2021, the Commission notes that it intends to engage with the ESAs before December 2022 to review the RTS to clarify indicators for both climate and environment-related adverse impacts and principal adverse impacts in the field of social and employee matters, respect for human rights, anti-corruption, and anti-bribery matters. The possibility therefore exists that the indicators set out in the RTS may be revisited or further clarifications in relation to these provided before the end of 2022.

7 Can we use additional indicators not set out in the RTS?

Yes, this has been confirmed in the RTS which provide that a Manager can report against indicators other than those set out in the RTS, which the Manager uses to identify and assess the principal adverse impacts of investment decisions on sustainability factors.

[4] Commission Communication on a "Strategy for Financing the Transition to a Sustainable Economy", 6 July 2021.

8 What is meant by "reference period"?

In order to ensure comparability of the information published in the PAI statement of each Manager, the same reference period must be used by all Managers (and other financial market participants publishing PAI Statements) when reporting on the principal adverse impacts of investment decisions on sustainability factors. Under the draft RTS, the reference period runs from 1 January to 31 December of the preceding year.

9 Does this mean that a Manager only needs to report against the PAI indicators as at 31 December in each year?

No. Under the draft RTS, the assessment must be based on at least the average of four calculations made on 31 March, 30 June, 30 September, and 31 December during the reference period, with the reference period defined as 1 January to 31 December of the preceding year.

10 What type of information must be provided when describing the policies that are used to identify and prioritise the principal adverse sustainability impacts?

Each Manager must provide a description of its policies on the assessment process used to identify and prioritise PAI on sustainability factors and describe how these policies are maintained and applied.

This should include the following:

- the date on which the policies have been approved by the board of directors of the Manager;
- a description of how responsibility for the implementation of the policies within the organisational structure and procedures of the Manager have been allocated;
- a description of the methodologies to select the indicators (see Article 6 of the draft RTS), identify and assess the PAI and how those methodologies take into account the probability of occurrence and severity of adverse impact, including their potentially irremediable character;
- an explanation of the margin of error within the methodologies above; and
- a description of the data sources used in the above calculations.

Importantly, where this data is not readily available, then details need to be given regarding the best efforts used to obtain this information, such as engagement with companies, or any assumptions made owing to lack of data.

11 What type of information must be provided relating to the international standards adhered to by the Manager?

The SFDR requires that the PAI Statement includes a description of the adherence of the Manager to responsible business codes and internationally recognised standards for due diligence and reporting. Where relevant, the degree of the Manager's alignment with the objectives of the Paris Agreement should also be disclosed.

The specifications for adherence to this requirement set out in the RTS are:

- The adverse indicators used in the assessment of the PAI referred to in the description above to measure adherence or alignment (as per Article 6 of the RTS).
- The methodology and data used to measure that adherence or alignment, including a description of the scope of the coverage, data sources and how the methodology forecasts the future performance of investee companies.
- Where a forward-looking climate scenario is used, an identification of that scenario, including the name and provider of the scenario and when it was designed.
- Where a forward-looking climate scenario is not used, an explanation of why forward-looking climate scenarios are not considered to be relevant by the Manager.

12 What changes need to be made to existing PAI Statements by 1 July 2022?

Managers have been required to disclose their approach to the consideration of PAI of investment decisions on sustainability factors on their websites since 10 March 2021.

For those Managers who either (i) voluntarily choose to comply or (ii) are required due to their size (>500 employees) to comply with the detailed disclosure obligations relating to how they consider the principal adverse impacts of their investment decisions on sustainability factors, the PAI Statement will need to be updated from 1 July 2022 to incorporate the additional disclosure obligations prescribed by the RTS.

By way of example only, these include (i) providing a 2-page summary of the PAI Statement, (ii) providing investors with information on the allocation of responsibility for the implementation of the due diligence policies within the organisational strategies and procedures of the management company, (iii) providing a description of the methodologies used to select the indicators which will be used to monitor PAI and (iv) providing a description of data sources used. More detailed information about the engagement policies implemented by the Manager and its adherence to responsible business conduct codes and internationally recognised standards for due diligence must also be provided.

As noted previously, the ESAs had indicated in a Supervisory Statement published in February 2021 that the disclosure obligations under the RTS which relate to a “reference period” will not need to be incorporated into the PAI Statement until 30 June 2023 (in respect of the reference period running from 1 January 2022 until 31 December 2022). This meant that the first PAI Statement which reports against the PAI indicators in respect of a reference period would need to be published by Managers by 30 June 2023.

It remains to be seen whether the European Commission will, in light of the deferral of the application date of the RTS until 1 July 2022, defer the application date of reporting information relating to a “reference period” for the first time by a year until 30 June 2024 (covering a reference period running from 1 January 2023 to 31 December 2023) in the finalised RTS adopted by it. Such an approach would be consistent with the current RTS in specifying that the reporting on PAI contained in the PAI Statement must be based on the average of the results for the four quarters of the preceding year. This is also consistent with the Commission’s stated intent under the Renewed Sustainable Finance Strategy to engage with the ESAs and clarify the PAI indicators before December 2022.

In light of the recent deferral of the SFDR RTS application date to 1 July 2022, clarification on the phasing in of the PAI reporting is needed as soon as possible so that Managers can plan and prepare for PAI reporting accordingly.

In-scope Managers will need to implement a framework from the beginning of the first reference period in order to capture the required data needed to report on PAI in the statement published in the June of the following calendar year due to the obligation to use the average of four calculations made on 31 March, 30 June, 30 September and 31 December.

If, for example, it was the case that the European Commission clarified that Managers must report information in respect of a reference period for the first time in the PAI Statement published in June 2024, then a framework would need to be put in place from the beginning of 2023 in order to capture the required data needed to perform the necessary calculations on 31 March 2023, 30 June 2023, 30 September 2023 and 31 December 2023. It is also possible that the Commission may clarify a reference period for PAI reporting commencing on 1 July 2022.

Clarification from the European Commission on the phasing in of the PAI reporting is needed as soon as possible in order to plan and prepare for PAI reporting accordingly.

13 Is there a template PAI Statement to be followed?

Yes, under the RTS a template PAI Statement must be followed. This template is provided in Table 1 of Annex 1 to the RTS. As noted above, the section of the template entitled "Description of Principal Adverse Sustainability Impacts" will not need to be included in the PAI Statement published by the relevant Manager on 1 July 2022.

14 Does the PAI Statement need to be translated if a fund under management is marketed in another Member State?

Under the RTS, the two-page summary which must be included at the beginning of the PAI Statement must be translated into one of the official languages of any host Member State in which any fund under management is marketed.

15 It is proving difficult to obtain the data I will require from investee companies in order to report against the PAI indicators included in the RTS. Will the regulatory authorities provide some form of "regulatory forbearance" in cases where data is not easily obtainable?

Recital 8 to the RTS sets quite a high bar on obtaining data. It provides that the PAI on sustainability factors should be identified "through all reasonable means available". It then goes on to list a number of different data sources including:

- **i.** internal financial analysts and specialists in the area of sustainable investments;
- **ii.** external market research providers;
- **iii.** undertaking specifically commissioned studies;
- **iv.** use of publicly available data, or data available from "peer networks or collaborative initiatives"; or
- **v.** direct engagement with the issuers which may be "particularly necessary" in situations where there is an insufficient level of data available.

The reference to "all reasonable means available" in Recital 7 of the RTS arguably provides some scope for interpretation taking into account the nature, scale and complexity of the Manager and the types of funds under management.

Article 7 of the RTS directly addresses the issue of lack of available data and provides that where information relating to any of the indicators used is not readily available, the Manager should disclose in its PAI Statement information on the "best efforts" used to obtain the relevant data directly from investee companies, by carrying out additional research or cooperating with third party data providers or making reasonable assumptions. The reference to "reasonable assumptions" indicates that there may be some leeway for use of assumptions or modelled data when reporting on PAI on sustainability factors.

The results of our survey of ESG Data Vendors set out below underscores the need to employ a best-efforts approach as a consequence of the challenges arising in sourcing data, particularly in the earlier stages of PAI reporting.

16 What disclosure obligations arise if a management company, due to its size, chooses to "explain" rather than comply with the PAI reporting?

Such management companies have been required under the SFDR since 10 March 2021 to include a statement on their website providing clear reasons for why they do not consider adverse impacts of investment decisions on sustainability factors, including, where relevant, information as to whether and when they intend to consider such adverse impacts.

Under the draft RTS, this statement must be included in a separate section of the website entitled "No consideration of sustainability adverse impacts". Where this statement indicates that such adverse impacts may be considered in the future, this should make reference to at least the mandatory indicators set down in the RTS.

In assessing the availability of data for reporting against the mandatory PAI indicators laid down in the draft RTS, we provided a number of data vendors with a sample of seven securities issued by investee companies and two sovereign bonds (together known as the "Sample Portfolio"). Real estate assets were not included in the Sample Portfolio. We analysed the data and provided a Red Amber Green (RAG) rating on an overall basis for coverage including range, comparability and suitability of the data provided by the Data Vendors for the sample portfolio in fulfilling the mandatory PAI indicators required under the template PAI Statement. Nine Data Vendors responded to the research request covering a range of Data Vendors in both the traditional and alternatives spaces. The response from the Data Vendors indicates that data is generally available for only eight of the fourteen mandatory PAI relating to investee companies, and that data can vary considerably between Data Vendors. It is important to note that the data analysed refers to vendor data available up to May 2021. The analysis performed in this paper only reflects the data available from the Data Vendors up to this date.

Coverage

Overall, there is patchy coverage across the Data Vendors for all mandatory PAI indicators relating to investee companies as shown in Table 1. From some of these indicators there is good coverage, however, for a number of other indicators there is currently little or no data provided by the underlying companies, or captured by the Data Vendors.

The responses from the Data Vendors indicate that data is generally available for only eight of the fourteen mandatory PAI relating to investee companies, and that data can vary considerably between Data Vendors.

The key findings of the analysis are:

- Across all the Data Vendors there was good coverage on the Greenhouse Gas ("GHG") emissions, carbon footprint, carbon intensity and board diversity. However, across these indicators there was a wide variance in the data provided as shown in Table 2.
- For biodiversity, water emission, hazardous waste and gender pay gap, there was limited information reported. In some cases, only 3 companies in the sample portfolio were covered.
- For the indicators applicable to investments in sovereigns and supranationals there was data provided by 4 Data Vendors and the range of information varied across all Data Vendors.

Table 1 – Patchy coverage of mandatory PAI[5]

	Mandatory Principal Adverse Indicator (PAI)	Vendor 1	Vendor 2	Vendor 3	Vendor 4	Vendor 5	Vendor 6	Vendor 7	Vendor 8	Vendor 9	Overall
1	GHG emissions										
2	Carbon footprint										
3	GHG intensity of investee companies										
4	Exposure to companies active in the fossil fuel sector										
5	Share of non-renewable energy consumption and production										
6	Energy consumption intensity per high impact climate sector										
7	Activities negatively affecting biodiversity-sensitive areas										
8	Emissions to water										
9	Hazardous waste ratio										
10	Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises										
11	Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact principles and OECD Guidelines for Multinational Enterprises										
12	Unadjusted pay gap										
13	Board diversity										
14	Exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)										
15	GHG intensity										
16	Investee countries subject to social violations										

Key for Companies
(PAIs 1-14)

>70% range	45% < 70% range	<44% range

Key for Countries
(Sovereigns and Supranationals - PAIs 15 and 16)

100%	50%	0

[5] Data analysed relates to 7 sample investee companies and 2 sovereign issuers.

Data variance

For a number of the indicators there is wide variance amongst the data points provided by the Data Vendors being used to meet the specifications of the PAI indicators. This wide variance could impact on the creditability of the data reported. Table 2 below provides a summary of the range of data points for Scope 1 and 2 Greenhouse Gas emissions (GHG) and carbon intensity.

Analysis of the variance in the data points identified the following findings:

- For scope 1 GHG, the range of information across the Data Vendors was between 10% and 50% of a difference.
- For scope 2 GHG the range of information across the Data Vendors was greater than 50% of a difference.
- For GHG intensity the range of information across the Data Vendors was greater than 50% of a difference but GHG intensity is calculated at the portfolio level under SFDR and therefore what is reported by the Data Vendors seems to be their calculation of GHG intensity.

Table 2 - Widely varying climate data returned by the Data Vendors for the same sample companies[5]

Company	Scope 1	Scope 2	Carbon Intensity
Company 1	3,770,000 to 4,494,068	2,800,000 to 5,973,894	4.27 to 1,687.32
Company 2	49,041 to 61,187	159,788 to 288,902	4.692 to 66.86376
Company 3	3,291,303 to 3,349,632	2,000,000 to 3,206,495	60.47 to 917.9515
Company 4	4,069,000 to 5,067,000	8,733,000 to 10,998,000	0.13 to 483.098
Company 5	15,560,000 to 18.593,000	3,279,000 to 3,552,000	353.142 to 2,037
Company 6	15,000,000 to 18,300,000	9,066,000 to 11,431,000	154.503186 to 1,730.76
Company 7	613,000 to 1,208,000	733,000 to 960,000	6.05562759 to 1,730
Country 1			
Country 2			

Key

<10% range	10%<50% range	>50% range

[5] Data analysed relates to 7 sample investee companies and 2 sovereign issuers.

Comparability

In comparing the data provided by all Data Vendors, we found that some data differed in terms of value and some in terms of units of measurement. One key factor for value differences is the timeliness of the data provided for the sample portfolio. Some Data Vendors provided data for companies for 2019 and some for 2020. Depending on the Data Vendor that a Manager uses there could be a significant difference in the reporting of some of the indicators for funds with similar portfolios. The timeliness of data will be a challenge as in most cases the data will be based on the previous financial year.

For a number of indicators there are different measures used by the Data Vendors. Across the Data Vendors there were only some metrics that were comparable. Four companies had indicators that were comparable, mainly GHG emissions, board diversity and renewable energy. For the exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons, and biological weapons) most Data Vendors only provided a “yes” or “no” response. This is a challenging indicator to measure as companies may be involved in only a subset of the areas highlighted. To maximize this comparison, we analysed the PAI coverage of the Data Vendors based on their comparability and suitability across all 7 public companies of the portfolio.

Table 3 - Poor comparability and suitability of PAI data across the nine Data Vendors[6]

Company	Vendor 1	Vendor 2	Vendor 3	Vendor 4	Vendor 5	Vendor 6	Vendor 7	Vendor 8	Vendor 9	Overall
Company 1										
Company 2										
Company 3										
Company 4										
Company 5										
Company 6										
Company 7										
Country 1										
Country 2										

Key

>85%	45% < 84%	<44%

In order to fully understand how the data provided by the Data Vendors compares we have done a deep dive comparing two Data Vendors (Data Vendor 5 and Data Vendor 6) for two investee companies, highlighting the best- and worst-case scenario for coverage and comparability.

[6] Data analysed relates to 7 sample investee companies and 2 sovereign issuers.

Best case scenario – PAI analysis of two Data Vendors' results for one investee company

In this scenario, we have examined the data for the investee company that shows the most advanced disclosure policy based on PAI coverage across all Data Vendors. Thus, using this investee company helps best isolate the issues of comparability and suitability between Data Vendors.

The key findings are:

- The data differences shown in PAI 1, 3 and 13, suggest that data has been provided from two different reporting periods for the investee company. Given PAI 13 is likely to have improved over time, it is likely that Data Vendor 6 has reported more up to date information.
- The data for PAI 2 is not comparable. However, this is a portfolio-level value that Managers would calculate using i) the Total GHG as provided along with ii) the company's Enterprise Value, iii) the amount invested in the investee company, and iv) the total portfolio value. See SFDR Annex 1 point (7).
- Seven of the remaining PAI indicators are either not provided, or are provided but not in the measurement required, by Data Vendor 5. Three of these are listed as 'Not Disclosed' by Data Vendor 6.
- This leaves PAI 4 and 14 as the only two data points that Data Vendor 5 and Data Vendor 6 agree upon.

Table 4 - Best case scenario comparing results from Data Vendor 5 and 6 for sample companies

	COMPANY 1 (Security with Most Vendor Data Coverage and Comparability)					
	Indicator	**Measurement**	**Vendor 5 (worst equity PAI coverage)**	**Vendor 6 (best equity PAI coverage)**	**% Diff**	**Data Comparison**
1	GHG emissions – Scope 1	Actual	3,770,000	4,340,000	15.1%	10%-50% Difference
	Scope 2	Actual	3,800,000	2,800,000	-26.3%	10%-50% Difference
	Scope 3	Actual	447,420,740	368,936,120	-17.5%	10%-50% Difference
	Total GHG	Actual Sum	454,990,740	376,076,120	-17.3%	10%-50% Difference
2	Carbon footprint	Weighted average of portfolio	7,570,000	376,076,120	Incongruent	>50% Difference
3	GHG intensity of investee companies	Per million EUR	1,886.69	1,687.32	-10.6%	10%-50% Difference
4	Exposure to companies active in the fossil fuel sector	% of investments that are active in the fossil fuel sector by yes or no	No	No		OK
5	Share of non-renewable energy consumption and production	Percentage	Unclear from response	111.29		Missing x1
6	Energy consumption intensity per high impact climate sector	GWh per million EUR	NaN	21,590.00		Missing x1
7	Activities negatively affecting biodiversity-sensitive areas	% of investments by yes or no	NaN	Not disclosed		Missing x2
8	Emissions to water	Per million EUR	NaN	Not disclosed		Missing x2
9	Hazardous waste ratio	Per million EUR	NaN	213,535.00		Missing x1
10	Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises	% of investments by yes or no	Unclear from response	Yes		Missing x1
11	Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact principles and OECD Guidelines for Multinational Enterprises	% of investments by yes or no	NaN	No		Missing x1
12	Unadjusted pay gap	% of females	NaN	Not disclosed		Missing x2
13	Board diversity	% of females	25%	40%	60.0%	>50% Difference
14	Exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)	% of investments by yes or no	No	No		OK
15	GHG intensity (environmental)	Per million EUR	N/A	N/A		N/A
16	Investee countries subject to social violations	% of investments by yes or no	N/A	N/A		N/A

Worst case scenario – PAI analysis of two Data Vendors' results for one sample company

We examined the data for the investee company that shows the least advanced disclosure policy based on PAI coverage across all Data Vendors. Thus, using this investee company helps explore the lack of data disclosed and the poor comparability between Data Vendors.

The key findings are:

- Only PAI 1 and 14 match in results between Data Vendors.
- GHG does not compare well. Only Scope 1 GHG agree between the two datasets. Scope 2 shows a 16% difference, and Scope 3 differs by two orders of magnitude (note Scope 3 will not be in scope until 1 January 2023). GHG Intensity also compares poorly. However, Carbon Footprint fairs better with only a 10% difference.
- Nine of the PAI indicators (from 4-12) cannot be compared due to missing data.
- Board diversity also exhibits a difference, again it is likely that Data Vendor 6 is reporting more up to date values in this respect.

Table 5 - Worst case scenario comparing results from Data Vendors 5 and 6 for sample companies

COMPANY 7 (Security with Least Data Vendor Coverage and Comparability)

	Indicator	Measurement	Vendor 5 (worst equity PAI coverage)	Vendor 6 (best equity PAI coverage)	% Diff	Data Comparison
1	GHG emissions – Scope 1	Actual	613,000	613,000	0.0%	OK
	Scope 2	Actual	871,000	733,000	-15.8%	10%-50% Difference
	Scope 3	Actual	11,119,408	290,000	Incongruent	>50% Difference
	Total GHG	Actual Sum	12,603,408	1,636,000	Incongruent	>50% Difference
2	Carbon footprint	Weighted average of portfolio	1,484,000	1,636,000	10.2%	10%-50% Difference
3	GHG intensity of investee companies	Per million EUR	164.62	21.37	-87.0%	>50% Difference
4	Exposure to companies active in the fossil fuel sector	% of investments that are active in the fossil fuel sector by yes or no	0%	NaN		Missing x1
5	Share of non-renewable energy consumption and production	Percentage	100%	Not disclosed		Missing x1
6	Energy consumption intensity per high impact climate sector	GWh per million EUR	NaN	0.07		Missing x1
7	Activities negatively affecting biodiversity-sensitive areas	% of investments by yes or no	NaN	Not disclosed		Missing x2
8	Emissions to water	Per million EUR	NaN	Not disclosed		Missing x2
9	Hazardous waste ratio	Per million EUR	Unclear from response	Not disclosed		Missing x2
10	Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises	% of investments by yes or no	Unclear from response	Yes		Missing x1
11	Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact principles and OECD Guidelines for Multinational Enterprises	% of investments by yes or no	NaN	Yes		Missing x1
12	Unadjusted pay gap	% of females	NaN	Not disclosed		Missing x2
13	Board diversity	% of females	25%	44%	76.0%	>50% Difference
14	Exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)	% of investments by yes or no	Yes	Yes		OK
15	GHG intensity (environmental)	Per million EUR	N/A	N/A		N/A
16	Investee countries subject to social violations	% of investments by yes or no	N/A	N/A		N/A

Suitability

We assessed the suitability of the reported metrics, in other words the appropriateness or level of alignment of the data based on the requirements of the indicators in the RTS. Across the 14 indicators there was suitable data reported by the different Data Vendors for 4 investee companies across a number of the indicators mainly GHG and board diversity. In analysing the data, we found that some of the Data Vendors may be providing their existing data to try and meet the SFDR requirements rather than creating new data points to specifically meet the SFDR requirements.

For the indicators applicable to investments in sovereigns and supranationals, only four of the Data Vendors supplied the data for PAI 15-16 for the two Countries in the sample portfolio. One of these Data Vendors provided data that is not easily compared to the remaining three.

The analysis in Table 6 presents the widest difference in values from the remaining Data Vendors. A 27% difference exists between Data Vendor 8 and 9 on GHG intensity. The data for GHG intensity ranged from 137.00 to 173.39 carbon intensity score.

For investee countries subject to social violations indicators, three Data Vendors just provided a “No” response to this indicator whereas one Data Vendor provided additional detail on the types of violations, e.g. Civil liberties, political rights, human rights etc.

For the metrics where the Data Vendors have provided a yes or no response, it is likely that more data will be required to determine if a company is exposed to UN violations or controversial weapons.

Table 6 - Comparing Data Vendors 7 & 8 on PAI 15-16 for a sovereign issuer

	COUNTRY 2 (Security with Most Data Vendor Coverage)					
	Indicator	Measurement	Vendor 8 (poorest Sovereign PAI scores)	Vendor 7 (strongest Sovereign PAI scores)	Range as % Diff	Data Comparison
15	GHG intensity (environmental)	Per million EUR	137.00	173.39	26.6%	10%-50% Difference
16	Investee countries subject to social violations	% of investments by yes or no	No	No		OK

Other examples of different approaches for some of the indicators include:

	Indicators	Example metrics provided
4	Exposure to companies active in the fossil fuel sector	Per Million of Revenue / Yes / No
10	Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises	Yes / No / Breakdown by principles e.g. human rights
11	Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact principles and OECD Guidelines for Multinational Enterprises	Yes / No / Breakdown by principles e.g. human rights etc.
14	Exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)	Yes / No / Breakdown of individual criteria e.g. chemical, biological etc.

Key implications and next steps

The findings from the survey conducted by Irish Funds reveal patchy coverage on several of the PAI indicators and a wide range of variance in the reported data with low levels of comparability between data vendors.

The results of the survey illustrate that the lack of common sustainability reporting standards for companies hinders the comparability and creditability of the reported data. The proposal for a Corporate Sustainability Reporting Directive (CSRD) published in April 2021 extends the scope and content of sustainability-related reporting obligations of certain EU companies. Consequently, we expect the availability of data by such companies to improve over time.

The European Financial Reporting Advisory Group (EFRAG) is currently drafting the technical standards and the CSRD is expected to be in place for large, listed public companies and listed Small Medium Enterprises (SME) from 1 January 2023, with first reports containing this information to be published in 2024. The timeframe is ambitious both for companies (preparers) and for assurance providers and there may be challenges with collecting and evaluating this new data, but it is a step in the right direction in the harmonisation of sustainability reporting.

However, significant data challenges will remain for Managers investing in non-EU companies or EU companies that do not fall within the scope of the CSRD.

Furthermore, the timeframe for reporting against the PAI indicators for the first time is now unclear in light of the European Commission's deferral of the application date of the RTS as a whole until 1 July 2022. Early clarification from the European Commission on this critical point would be welcome in order to enable Managers to prepare accordingly.

In light of the significant data challenges that currently exist, Managers seeking to comply with the PAI reporting requirements will need to employ a best-efforts approach. The same challenges will also apply in relation to the implementation of reporting under the EU Taxonomy Regulation. Guidance from regulators on how to address these data gaps and on the use of "best efforts" until such time as sustainability reporting standards are in place under the CSRD would be welcomed. We would encourage Managers to start engaging with their Data Vendors to determine if they will be able to provide sufficient data to report on the PAI. This will not be an easy exercise and we suggest that to the extent not already underway, project plans addressing PAI reporting are put in place as soon as possible.

ESG Data Appendix A
– PAI Template for Mandatory Reporting Indicators

Adverse Sustainability Indicator		Metric	Impact [year n]	Impact [year n-1]	Explanation	Actions Taken
Climate and other Environmental-Related Indicators						
Greenhouse gas emissions	1. GHG emissions	Scope 1 GHG emissions				
		Scope 2 GHG emissions				
		Scope 3 GHG emissions (From 1 January 2023)				
		Total GHG emissions				
	2. Carbon footprint	Carbon footprint				
	3. GHG intensity of investee companies	GHG intensity of investee companies				
	4. Exposure to companies active in the fossil fuel sector	Share of investments in companies active in the fossil fuel sector				
	5. Share of non-renewable energy consumption and production	Share of non-renewable energy consumption and non-renewable energy production of investee companies from non-renewable energy sources compared to renewable energy sources, expressed as a percentage				
	6. Energy consumption intensity per high impact climate sector	Energy consumption in GWh per million EUR of revenue of investee companies, per high impact climate sector				
Biodiversity	7. Activities negatively affecting biodiversity-sensitive areas	Share of investments in investee companies with sites/operations located in or near to biodiversity-sensitive areas where activities of those investee companies negatively affect those areas				
Water	8. Emissions to water	Tonnes of emissions to water generated by investee companies per million EUR invested, expressed as a weighted average				
Waste	9. Hazardous waste ratio	Tonnes of hazardous waste generated by investee companies per million EUR invested, expressed as a weighted average				

ESG Data Appendix A
– PAI Template for Mandatory Reporting Indicators

Adverse Sustainability Indicator		Metric	Impact [year n]	Impact [year n-1]	Explanation	Actions Taken
Social and Employee, Respect for Human Rights, Anti-corruption and Anti-bribery matters						
Social and employee matters	10. Violations of UN Global Compact principles and Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises	Share of investments in investee companies that have been involved in violations of the UNGC principles or OECD Guidelines for Multinational Enterprises				
	11. Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact principles and OECD Guidelines for Multinational Enterprises	Share of investments in investee companies without policies to monitor compliance with the UNGC principles or OECD Guidelines for Multinational Enterprises or grievance /complaints handling mechanisms to address violations of the UNGC principles or OECD Guidelines for Multinational Enterprises				
	12. Unadjusted gender pay gap	Guidelines for Multinational Enterprises				
	13. Board gender diversity	Average ratio of female to male board members in investee companies				
	14. Exposure to controversial weapons (anti-personnel mines, cluster munitions, chemical weapons and biological weapons)	Share of investments in investee companies involved in the manufacture or selling of controversial weapons				
Indicators applicable to investments in sovereigns and supranationals						
Environmental	15. GHG intensity	GHG intensity of investee companies				
Social	16. Investee countries subject to social violations	Number of investee countries subject to social violations (absolute number and relative number divided by all investee countries), as referred to in international treaties and conventions, United Nations principles and, where applicable, national law				
Indicators applicable to investments in real estate assets						
Fossil fuels	17. Exposure to fossil fuels through real estate assets	Share of investments in real estate assets involved in the extraction, storage, transport or manufacture of fossil fuels				
Energy efficiency	18. Exposure to energy-inefficient real estate assets	Share of investments in energy-inefficient real estate assets				

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