A&L Goodbody

ASSET MANAGEMENT &
INVESTMENT FUNDS

UCITS directive and AIFM regulation - *sustainable finance revisions*

Following on from the implementation of the Sustainable Finance Disclosures Regulation (**SFDR**) and the Taxonomy Regulation, on 21 April 2021 the European Commission adopted a delegated UCITS directive and delegated AIFM regulation on the sustainability risks and sustainability factors to be taken into account for UCITS management companies and AIFMs.

The changes are effective from 1 August 2022.

4 MIN READ

Which entities will be impacted by these changes?

The requirements apply to all UCITS management companies and AIFMs (referred to collectively here as management companies), regardless of whether or not they manage UCITS or AIFs with an ESG focus.

The requirements also apply to investment companies or ICAVs that do not have a designated management company, taking into account, where outlined below, the nature, scale and complexity of the relevant business. References herein to management companies should be taken to include these types of entities.

Where investment or portfolio management has been delegated by the management company, the requirements have an indirect impact on the delegate irrespective of whether the delegate is domiciled in the EU or not, for example, in relation to investment due diligence.

What are the main changes?

Under the amended regimes, management companies are required to look through a sustainability lens at risk management procedures and processes, investment decision making processes, organisational structure and resources, governance, oversight, reporting and conflicts of interest management. Boards of externally managed AIFs and UCITS will need to consider the extent of their responsibilities in relation to integration of sustainability risks and factors and those of the management company.

A "*sustainability risk*" is defined by SFDR as "*an environmental, social or governance event or condition that, if it occurs, could cause an actual or a potential material negative impact on the value of the investment.*"

"*Sustainability factors*" are defined by SFDR as "any environmental, social and employee matters, respect for human rights, anti-corruption and anti-bribery matters".

A summary of the key changes is set out below:

Senior management	Senior management of the management company is made responsible for integrating the consideration of sustainability risks into the management company's business.
Resources	The entity must retain the necessary resources and expertise for the effective integration of sustainability risks into its governance structure.
Organisation systems	Documented decision-making procedures, organisational structures, reporting lines and control mechanisms must provide that sustainability risks are taken into account.
Conflicts of interest	Processes, policies and registers around conflicts of interest must include conflicts that may arise as a result of the integration of sustainability risks such as conflicts arising from the risk of greenwashing, mis-selling or misrepresentation of investment strategies.
Due diligence	Due diligence processes must take account of sustainability risk. Management companies should ensure that they have access to information which enables them to consider sustainability risks as part of their investment due diligence processes.
Risk management	The risk management policy must consider exposures of UCITS and AIFs to sustainability risks, in addition to market, liquidity and counterparty risks and all other relevant risks, including operational risks.

What action should management companies take?

Organisational structure:

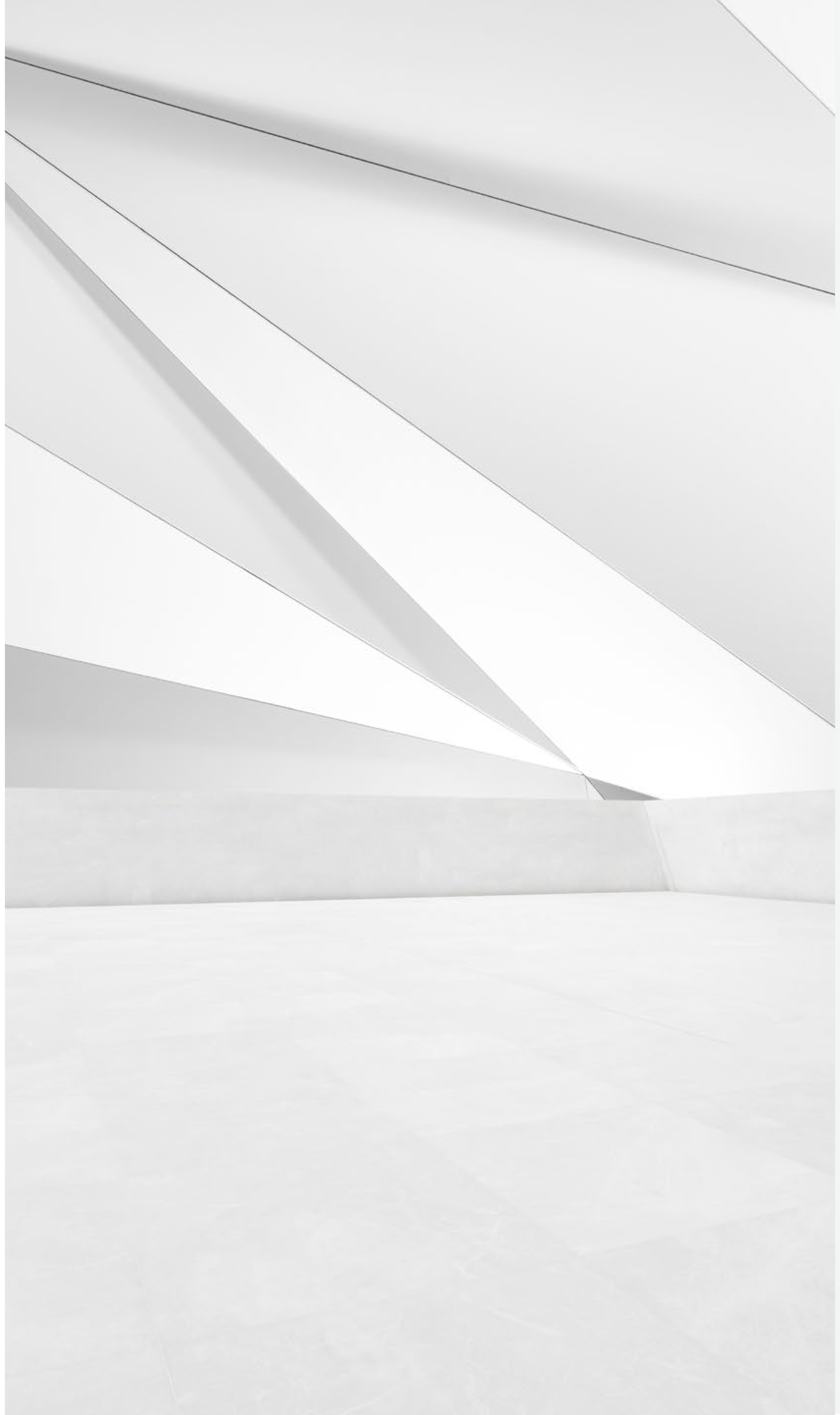
- Review the organisational structure to ensure it has the appropriate resources, expertise and governance to effectively integrate sustainability risks into its governance structure. An investment company or ICAV that has not designated a management company may take into account the nature, scale and complexity of their business when seeking to comply with this requirement.
- Ensure relevant employees understand sustainability risks and how they could apply to the business. Some entities may already have the requisite level of skill, others may upskill teams through training or by appointment of new personnel.
- Consider the designation of a sustainability officer within larger management companies. This would not be appropriate for all.
- Develop a policy in relation to how sustainability issues are applied by its senior management.

Policies, procedures and registers:

- Review and update all relevant policies and procedures, in particular conflict of interest and risk management procedures, to reflect how sustainability risks are integrated into the decision making-process.
- Integrate sustainability risks in the risk register.
- Review and update reporting processes to ensure sustainability risks are being taken into account.
- Review and update investment due diligence processes to take into account sustainability risks. Pursuant to SFDR, management companies that opt-in or that are obliged to consider principal adverse impacts of investment decisions on sustainability factors, must disclose how their due diligence policies take those principal adverse impacts into account.

Business plan / programme of activity:

- Review and update to reflect the resources in place and the allocation of responsibilities in respect of sustainability risks.



A&L Goodbody

Key contacts

Brian McDermott
Partner
+353 1 649 2307
bmcdermott@algoodbody.com

Michael Barr
Partner
+353 1 649 2327
mbarr@algoodbody.com

Stephen Carson
Partner
+44 20 7382 0820
scarson@algoodbody.com

Mary McKenna
Partner
+353 1 649 2344
mmckenna@algoodbody.com

Kerill O'Shaughnessy
Partner
+353 1 649 2422
koshaughnessy@algoodbody.com

Laura Butler
Partner
+353 1 649 2209
lbutler@algoodbody.com

Chris Bergin
Senior Associate
+353 1 649 6826
cbergin@algoodbody.com

For further information contact a member of the A&L Goodbody Asset Management & Investment Funds team.