About

The 2° Investing Initiative (2DII) is an international, non-profit think tank working to align financial markets and regulations with the Paris Agreement goals.

Working globally with offices in Paris and New York, 2DII coordinates some of the world's largest research projects on climate metrics in financial markets. In order to ensure our independence and the intellectual integrity of our work, we have a multi-stakeholder governance and funding structure, with representatives from a diverse array of financial institutions, regulators, policymakers, universities and NGOs.

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Annex 2: Financial product eligibility for recommendation

Financial product recommendation

(1) Following the identification of client sustainability preferences and wider sustainability motivations, investment firms can proceed to Step 3: Financial product recommendation.

(2) The Questionnaire accommodates three scenarios here:

- **Short assessment**: The client does not have any interest in sustainability. Only financial preferences are taken into account for the product recommendation.
- **Medium assessment**: The client expresses interest in sustainability or a need for further information. One or more sustainability goals and one or more sustainability preferences as defined by the client are taken into account for the product recommendation. No further details on values and sustainability priorities such as specific environmental or social sustainability objectives are assessed at this stage (except for those related to the different categories of MIFID II sustainability preferences such as principal adverse impacts).
- **Long assessment**: The client wants to provide more information on specific values or priorities for his or her investment. After the determination of the sustainability goals and sustainability preferences, more details on specific motivations related to positive or negative screenings are taken into account for the product recommendation.

(3) The information below can support investment firms form a view on which financial products can be recommended to satisfy different client sustainability preferences and wider sustainability motivations. It articulates a methodology for how investment firms should proceed together with features of financial products which correlate to minimum requirements for satisfying client sustainability preferences and wider sustainability motivations.

(4) However, investment firms should bear in mind that sustainability features of financial products are constantly evolving. In addition, the content below represents a starting point for determining whether a financial product satisfies sustainability preferences and wider sustainability motivations. **Investment firms must independently satisfy themselves that any financial product they recommend does in fact satisfy the specific sustainability preferences expressed by the client in that case.**

The need to consider wider information than categories of sustainability preferences

(5) The regulatory concept of client sustainability preferences is articulated as a client's preference for one or more of three MiFID II sustainability preference categories (A, B, C) of financial product. As explained in Section 4, for some clients, investing in a financial product which falls under one of these three categories may not be sufficient to satisfy all sustainability motivations associated with their investments.

(6) The following sustainability features are compulsory for financial products to be suitable to one or more sustainability preference categories:

Table 1: Draft matching table between Categories A, B, C and compulsory product features

MIFID II category of sustainability preference	Compulsory features
A	• Taxonomy Alignment • Exclusion Do No Significant Harm (according to Taxonomy) • Minimum Safeguards (UN Global Compact) exclusion
B	• Impact alignment • Exclusion Do No Significant Harm Exclusion (according to SFDR)
C	• Principle Adverse Impact consideration

(7) While sustainability preference categories of MiFID II Delegated Act are built around the concepts of greenness and sustainability, investor broader sustainability motivations are about impact, personal values and ESG integration, leading to many potential mismatches between what product features clients actual want and features of recommended products.[1] This is most clearly illustrated in the case of impact-motivated investors who want to cause additional positive environmental or social outcomes with their savings. However, an impact-oriented financial product is not defined under sustainability preference category A, B or C, although it would be the most suitable for impact-motivated clients. Investment firms need to raise questions which capture sustainable investment approaches beyond MiFID II Delegated Act to capture the actual motivations of retail clients and reduce the risk of mis-selling.

(8) Therefore, the Questionnaire and the Guidance integrates the concept of wider sustainability motivations (see Annex I) to denote other additional product features (not addressed by the regulatory concept of sustainability preferences) which are relevant to implement better practice for a comprehensive assessment of all sustainability related aspects associated with client investments and to increase the suitability of the recommended product.

(9) Better practice implies that financial products are recommended to satisfy different client sustainability preferences and wider sustainability motivations by matching a maximum of financial product features with client's expressed sustainability preferences as well as wider sustainability motivations (defined by sustainability goals, values and priorities).

(10) This additional information can be used as a further filter to narrow down the product universe to the most suitable products which best match the client's financial objectives and preferences, sustainability preferences and wider sustainability motivations.

(11) The Questionnaire and the Guidance include wider sustainability motivations to include the following:

a) **Sustainability goals** which are assessed in the Medium Assessment and relate to the main reasons why clients want to invest sustainably. These sustainability goals can be grouped in three principal categories: *Impact, Value Alignment* and *ESG integration*;

[1] To better understand the difference between "impact aligned" and "impact generating" products see Bush et al. (2021): Impact investments: a call for (re)orientation or Eurosif (2022): Classification Scheme for Sustainable Investments.

b) **Values and priorities** which are assessed in the long assessment and relate to specific priorities for investments such as focussing on one or more of the Sustainable Development Goals or avoiding financing certain economic sectors or violations of international standards.

(12) The Questionnaire and the Guidance include the following three core sustainability goals of clients when they want to invest sustainably*:*

Impact: A client wants to have an impact on the processes or outcome of a company. For instance, the client wants to improve labour relations in the value chains or increase the production of renewable energies.
Value alignment: A client wants to support or avoid activities to align an investment with her/his values. For instance, a client wants to support the companies with the relatively highest positive impact on climate change or exclude all companies with revenues coming from weapons, genetically modified organisms, or palm oil.
ESG integration: A client wants to use sustainability factors to increase the financial returns or decrease the financial risk of his/her investment. For instance, the client wants to focus on specific sustainable sectors or on the companies which manage best their ESG risks[2].

(13) The Questionnaire and the Guidance include the following set of value and priorities which can be used for sustainable finance products:

(14) Environmental objectives as defined by the Sustainable Development Goals (SDGs)
- **Clean water and sanitation**
- **Affordable and clean energy**
- **Sustainable cities and communities**
- **Responsible consumption and production**
- **Climate action**
- **Water quality and fish stocks**
- **Nature conservation and biodiversity**

(15) Social sustainability objectives as defined by the Sustainable Development Goals
- **No poverty**
- **Zero hunger**
- **Good health and well-being**
- **Quality education**
- **Gender equality**
- **Decent work and economic growth**
- **Sustainable industry, infrastructure and innovation**
- **Reduce inequalities**
- **Peace, justice and strong institutions**
- **All environment, social & governance matters**

(16) Environment exclusions
- **Pesticides**
- **Animal testing**
- **Genetic engineering**

[2] A significant part of investors thinks integrating ESG risks and opportunities leads to increased risk adjusted return. Currently not all financial products integrate ESG risks and opportunities. Therefore, investment firms should identify clients who want to integrate ESG risks and opportunities in their investment to recommend suitable products. This goal could become irrelevant if all financial products would integrate ESG risk and opportunities.

- **Palm oil**
- **Coal**
- **Oil**
- **Nuclear energy**
- **Gas**
- **Fur**
- **Factory farming**

(17) Social & ethics exclusions
- **Weapons and/or armament**
- **Tobacco products**
- **Alcohol**
- **Gambling**
- **Pornography**
- **Research on human embryos**

(18) Violations of International norms exclusions:
- **Violation of the principles of the UN Global Compact**
- **Violation of OECD guidelines for multinational enterprises**
- **Violation of International Labour Organisation rules**

(19) Sovereigns' exclusions
- **Nuclear weapons**
- **Non-proliferation treaty of nuclear weapons**
- **Democracy**
- **Corruption**
- **Death sentence**
- **War**
- **Non-ratification of Paris-Agreement**

Considering information on sustainability preferences and wider sustainability motivations in the product recommendation

(20) All information required for the medium and long assessment should be retrieved from an ESG data template[3] which is used between product manufactures and product distributors or if data points are missing in the template from additional data sources provided by the product manufactures.

Medium assessment

(21) In the medium assessment, the client's sustainability goals, and sustainability preferences are determined. At this stage, no further details on specific sustainability values or priorities are defined by the client due to low interest of the client to define more specific sustainability motivations. At this stage the client will however already indicate if he/she has specific interest for taxonomy aligned products (category A), or wider environmental and social considerations (category B). Although the client does not specify priorities, she/he still needs to define a minimum proportion of sustainable investing under

[3] See for instance Findatex templates

category A and B. In case the client expresses preferences for the category C, he/she will be asked to express which principal adverse indicators should be considered and how this should be implemented (e.g. through exclusion or engagement).

(22) When sustainability goals and sustainability preferences are determined by the client, they need to be translated into tangible data points for the product matching process.

(23) Specific sustainability features are linked to each category of MIFID II sustainability preference (see paragraph 6). In a first step, all sustainability features under the respective A, B, C categories are compulsory if one or more sustainability preference categories are selected by the client.

(24) The prioritization between the categories will help to recommend a product which is most suitable if a client has more than one sustainability preference and not all sustainability preferences can be met, and the client agrees to amend her or his sustainability preferences (see also step 3 in the Guidance: Financial product recommendation).

(25) The available product universe should be first filtered by the compulsory sustainability features related to the sustainability preferences without taking further notice of more detailed sustainability values or priorities. Since no further information on sustainability priorities are provided, financial products need to match at least one environmental sustainability objective as defined by the taxonomy (see category A) or at least one environmental or social sustainability objective (see category B) or at least consider all selected adverse sustainability indicators (see category C).

(26) In a second step, sustainability strategies related to one or more sustainability goals selected by the client are used as optional additional filters. The sustainability strategies under the respective sustainability goals are not compulsory (see table 1 below). However, implementing relevant sustainability strategies in the matching process reduces the risk of mismatch between product recommendation and the actual sustainability goals of the client.

(27) The matching of sustainability strategies with sustainability goals is helpful for clients to match the most suitable strategies to reach their sustainability goals.[4] See table 2 below:

[4] This approach is also recommended for instance by the Swiss Asset Management Association and SSF: https://www.sustainablefinance.ch/upload/cms/user/RecommendationsforSustainableInvestmentProducts_AMAS_SSF.pdf

Table 2: Draft matching between sustainability strategies and sustainability goals[5]

Product features		Sustainability goals (non-exclusive)		
		Impact	Value Alignment	ESG integration
Optional additional sustainability strategy	ESG integration			x
	Stewardship	x	x	
	Exclusion		x	
	Best-in-class		x	
	Thematic screening		x	
	Impact investing	x		
	Income-sharing	x		

X = to a great extent suitable sustainability strategy for the sustainability goal

(28) In case the client has more than one sustainability goal, the client needs to make a prioritization. As before, the prioritization will help to recommend a product which is most suitable if not all sustainability goals can be met, and the client agrees to amend her or his sustainability goals. The sustainability goal with the highest priority will be first used as an additional filter, followed by the second and potentially third goal and their additional filters (see also step 3 in the Guidance: Financial product recommendation).

(29) Table 3 below provides a matching between sustainability strategies and sustainability preferences as well as sustainability goals below:

[5] See similar approach in Swiss Asset Management Association/Swiss Sustainable Finance (2022): Recommendations on transparency and minimum requirements for sustainable investment approaches and products.

Table 3: Draft matching table between compulsory and optional additional product features and sustainability goals:

MIFID 2 sustainability preferences (non-exclusive)	Product features		Sustainability goals (non-exclusive)		
			Impact	Value Alignment	ESG integration
A	Compulsory sustainability approaches for A (irrespective of the wider sustainability motivations expressed by the client)		Taxonomy alignment Exclusion DNSH (Taxonomy) Minimum safeguards (UN GC exclusion)		
A	Optional additional sustainability strategy	ESG integration			x
A		Stewardship	x	x	
A		Exclusion		x	
A		Best-in-class		x	
A		Thematic screening		x	
A		Impact investing	x		
A		Income-sharing	x		
B	Compulsory features for B (irrespective of the wider sustainability motivations expressed by the client)		Impact alignment Exclusion DNSH (SFDR)		
B	Optional additional sustainability strategy	ESG integration			x
B		Stewardship	x	x	
B		Exclusion		x	
B		Best-in-class		x	
B		Thematic screening		x	
B		Impact investing	x		
B		Income-sharing	x		
C	Compulsory features for C (irrespective of the wider sustainability motivations expressed by the client)		PAI consideration		
C	Optional additional sustainability strategy	ESG integration			x
C		Stewardship	x	x	
C		Exclusion		x	
C		Best-in-class		x	
C		Thematic screening		x	
C		Impact investing	x		
C		Income-sharing	x		

X = to a great extent suitable sustainability strategy for the sustainability goal

(30) If a financial product is matching one or more sustainability strategies related to sustainability goals and the financial product is recommended to the client, then the investment firm should explain why the sustainability strategies of the financial product are suitable for the sustainability goal(s) of the client. The investment firm should provide concrete details about how the product applies the strategy in practice (criteria used, thresholds, voting reports, etc.).

(31) Find below a simplified example to illustrate the filter process of the medium assessment:

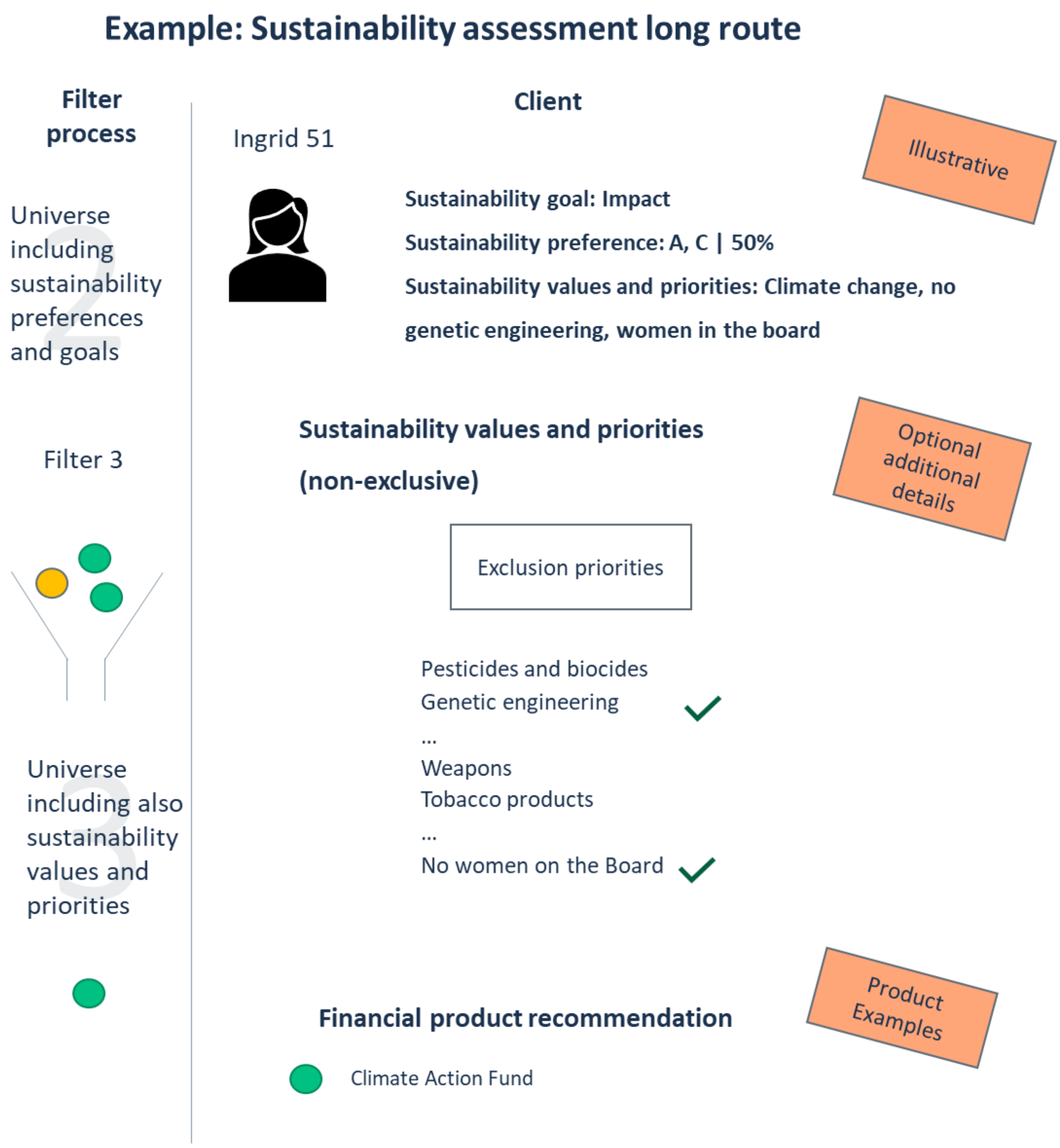
Example: Sustainability assessment medium route

Long assessment

(32) In the long assessment, the client's preferences for specific sustainability values and sustainability priorities are determined. At this stage, the client can specify environmental and social sustainability objectives and exclusion topics.

(33) In a third step the specific values and priorities can then be used in as additional filters to narrow down the product universe and to increase the suitability of the financial products recommended to the client.

(34) Find below a simplified example to illustrate the filter process of the long assessment:



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The Finance ClimAct project contributes to the implementation of France's National Low Carbon Strategy and the European Union's Sustainable Finance Action Plan. It aims to develop tools, methods and new knowledge that will enable (1) savers to integrate environmental objectives into their investment choices, and (2) financial institutions and their supervisors to integrate climate issues into their decision-making processes and align financial flows with energy and climate objectives.

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