Response Form
for the
Consultation Paper on the development of the CFA Institute ESG Disclosure Standards for Investment Products

CFA Institute is developing a voluntary, global industry standard, the CFA Institute ESG Disclosure Standards for Investment Products (the "Standard"), to establish disclosure requirements for investment products with ESG-related features. The purpose of the Standard is to provide greater transparency and comparability for investors by enabling asset managers to clearly communicate the ESG-related features of their investment products. The goal for this Consultation Paper is to elicit feedback on the proposed scope, structure, and design principles of the Standard. **All comments must be received by 19 October 2020 in order to be considered.**

Providing Feedback

Public commentary on this Consultation Paper will help shape an Exposure Draft, the initial version of the Standard, which is expected to be issued in May 2021. Comments should be provided in this response form. You may address as few or as many of the Consultation Paper's questions as you wish. Unless otherwise requested, all comments will be posted on the CFA Institute website.

<u>Guidelines for submission</u>

Comments are most useful when they:

- directly address a specific issue or question,
- provide a rationale and support for the opinions expressed, and
- suggest alternative solutions in the event of disagreement.

There is a section for general comments at the end of this response form.

Positive comments in support of a proposal are equally as helpful as those that provide constructive suggestions for improvement.

<u>Requirements for submission</u>

For comments to be considered, please adhere to the following requirements:

- Insert responses to numbered questions in the designated areas of the response form. Please do not remove tags of the type <QUESTION_XX>. Your response to each question must be framed by the two tags corresponding to the question. If you do not wish to respond to a given question, please do not delete it but simply leave the text "ENTER RESPONSE HERE" between the tags.
- Provide all comments in English.
- Assign a unique file name to your response form.
- Submit the response form as a Microsoft Word document.
- Submit the response form to standards@cfainstitute.org by 5:00 PM E.T. on 19 October 2020.

General Information (required)

Respondent: *(Please enter your full name if you are submitting as an individual or the name of the organization if you are submitting on behalf of an organization.)*	Eduardo Rodriguez Jr. on behalf of FlatStone Capital Advisors Inc.
Stakeholder Group: *(Please select the stakeholder group with which you most closely identify.)*	Asset Manager
Region: *(If you are submitting as an individual, please select the region in which you live. If you are submitting on behalf of an organization and the organization has a significant presence in multiple regions, please select "Global". Otherwise, please select the region in which the organization has its main office.)*	North America
Country: *(If you are submitting as an individual, please enter the country in which you live. If you are submitting on behalf of an organization, please enter the country in which the organization has its main office.)*	Canada
Confidentiality Preference: *(Please select your preference for whether your response is published on the CFA Institute website.)*	yes, my response may be published

Consultation Paper Questions

Market Needs

Question 1: Do you agree that a standard is needed to help investors better understand and compare investment products with ESG-related features?

<QUESTION_01>

Yes

<QUESTION_01>

Terminology

Question 2: Are any of the defined terms ambiguous? If so, how could they be clarified?

<QUESTION_02>

Some of the terms defined appear ambiguous and confusing to facilitate the investors understanding, the following terms could be clarified:

1. The term **ESG Related Factor** should read **(GIPS) ESG Standard Factor** denoting the minimum global standard requirements for an investment product to qualify under the GIPS ESG Standard for compliance and reporting
2. The term **ESG Related Feature** should read **(GIPS) ESG Standard Feature** denoting the minimum global standard component or capability, intentionally incorporated into the design of an investment product to provide a benefit for the investor, that relies on **(GIPS) ESG Standard Factors** qualify under the **(GIPS) ESG Standard for compliance and reporting**

<QUESTION_02>

Purpose and Scope

Question 3: In addition to the examples listed in Table 1, which regulations and standards, either in existence or in development, should be considered during the development of the Standard to avoid duplication or conflict and to ensure alignment and referencing if and when applicable?

<QUESTION_03>

As per the regulations and standards, we identify the following ones:

- **Specifications for investment product disclosures**:
  a. The CFA Institute ESG Disclosure Standards for Investment Products,
- **Specifications for measurement or reporting**:
  a. Principles for Responsible Investment (PRI) Reporting Framework
- **Specifications for issuer disclosures:**
  a. Sustainability Accounting Standards Board (SASB) Standards
  b. Global Reporting Initiative (GRI) Standards
  c. European Securities Market Authority, Securities and Markets Stakeholder Group (SMSG) advice to the ESA's Joint Consultation Paper on ESG Disclosures (ESMA22-106-2858)

- **Specifications for the cryptographic representation of ESG Compliant Assets**
- International Token Standard Association (ITSA) representation of ESG Security Tokens (Proposal being drafted by FCA for consideration and development under working group at ITSA)

<QUESTION_03>

Question 4: Do you agree that a disclosure-based approach would be more helpful to achieve the Standard's goals of transparency and comparability than a prescriptive-based approach?

<QUESTION_04>

No. FCA believes prescriptive based approach setting and describing minimum standards ESG factors and features an investment product must incorporate to meet the standard. The approach should clearly outline which features should be included and how they interact, function, or affect performance in a quantifiable way to achieve a minimum level of benefits that would qualify the investment product to become ESG. Ideally, the prescriptive approach should provide a point qualification formula that a) confirms compliance to the standard via qualitative + quantitative factors and b) Quantifies the net effect in risk mitigation/reduction/transfer reflected on c) The corresponding investment product enhancement in terms of benefits (tax credits/investment return/interest payable WACC

<QUESTION_04>

Question 5: Do you agree that the Standard should focus only on product-level disclosures and not firm-level disclosures?

<QUESTION_05>

FCA believes the standard without assurance of the firm-level disclosure, provides zero value, as the product level disclosure requires provenance as a condition to ensure compliance and disclosure based on trusted origination (provenance and data integrity).

<QUESTION_05>

Question 6: Do you agree that an asset manager should be permitted to choose the investment products to which they apply the Standard rather than be required to apply the Standard to all their investment products with ESG-related features?

<QUESTION_06>

No, allowing the asset managers to selectively apply the standard to only some of their investment products with ESG-related features would place the organization in conflict with ethical and other professional codes such as the CFA The Code of Ethics and Standards of Professional Conduct.

<QUESTION_06>

Design Principles

Question 7: Do you agree with the design principles for definitions of ESG-related terms?

<QUESTION_07>

FCA agrees with four of the five design principles, with some reservations on the Alignment. Linking terms used in the Standard with terms used by other organizations seems to pose a significant challenge given the current lack of universally accepted definitions across organizations.

<QUESTION_07>

Question 8: Do you agree with the design principles for disclosure requirements?

<QUESTION_08>

FCA believes the design principles for disclosure framework require more robust compliance and reporting methodology which includes quantifiable data and minimum standards enabling comparability across different investment products.

We believe the scope falls short to establish principles to ensure the disclosure requirements meet the purpose of the Standard. We propose the following changes to the design principles:

1. Disclosure requirements should focus on relevant, useful information that can ensure compliance to the standard(s). Disclosures must provide information that will help investors to better understand investment products, make comparisons, and choose among alternatives based on quantitative and qualitative data which can be measured vs minimum standard(s) across ESG Factors.

2. Disclosure requirements should focus on automating the process for "quantifiable" ESG-related features. Because the goal of the Standard is to enable greater transparency and comparability of investment products with ESG-related features, the Standard's disclosure requirements should focus on hard data (quantitative) and unique features (qualitative) which can be documented, verified and traced to the Asset Manager making the disclosure. By focusing on automating the compliance and disclosure requirements using enterprise technologies we can both ensure compliance and avoid unnecessary burdens to an asset manager's investment allocation process.

3. Disclosure requirements should provide asset managers with clear specific information to make the required disclosure in the most consistent possible manner given the nature of the product. Disclosure requirements can easily be formulated to establish requirements to claim compliance to the standard is met. The core elements could be established by structuring the criteria for meeting the standard in a clear consistent response for the sake of comparison by investors.

4. The disclosure requirements should aim to elicit a “specific” level of detail. An investment product’s disclosures should accurately and adequately represent the policies and procedures that govern the design and implementation of the investment product. The Standard’s disclosure requirements should be structured between a due diligence conversation and an audit for compliance. The disclosures should provide specific detail which is standardized and presented during a formal diligence process but less than an audit.

5. The disclosure requirements should prioritize format (quality) over content (quantity) of data. The disclosure requirements should focus on which information is disclosed rather than how much is disclosed. The Standard will provide a certain degree of flexibility in the format for information presentation. Providing clarity in the format is intended to reduce an asset manager’s disclosure burden and allow for harmonization with disclosures required by regulatory bodies and other standards.

6. Disclosure requirements should be categorized as feature-specific”. The Standard will have feature-specific disclosure requirements. General disclosure requirements can’t be applied to all investment products that don’t comply with the Standard. Feature-specific disclosure requirements will

apply only to investment products that have specific ESG-related features making them “meet the standard(s)”

7. The Standard should include disclosure methodologies in addition to requirements. We anticipate that in addition to the Standard's required disclosures, the Standard will have recommended disclosures as well. Required disclosures represent the minimum information that must be disclosed to comply with the Standard. Methodology disclosures provide standardized formatted data supporting investor's decision making. Methodology disclosures should be mandatory.

<QUESTION_08>

Question 9: Should the Standard require that all disclosures be made in a single document? If disclosures were spread across multiple documents, would that pose a challenge for investors to understand and compare investment products?

<QUESTION_09>

Yes, all disclosures should be made in one single document. Spreading the disclosures across multiple documents would not only pose a challenge for investors to understand the investment products but also increase the potential for mistakes in the process of compliance and reporting.

<QUESTION_09>

Question 10: Do you agree with the design principle for independent examination?

<QUESTION_10>

Yes. However, we suggest the independent examination seems appropriate to automate the process of compliance and disclosure using the enterprise technologies available from XBRL to blockchain

<QUESTION_10>

Question 11: Should independent examination be required, or should it be recommended as best practice but ultimately left to the discretion of the asset manager?

<QUESTION_11>

As per the above, the independent examination should be a mandatory process to claim adherence to the investment product to the ESG designation or standards.

<QUESTION_11>

Question 12: Should the independent examiner (i) examine the disclosures relative to only the design of the investment product, or (ii) examine the disclosures relative to both the design and implementation of the investment product?

<QUESTION_12>

The independent examiner should be required to complete a mandatory review relative to both the design and implementation methodology of the investment product in order to confirm compliance with the requirements of the standard.

<QUESTION_12>

Proposal for General Disclosure Requirements

Question 13: Do you agree with the scope of the general disclosure requirements? Are there topics that should be added, deleted, or modified?

<QUESTION_13>

Yes

<QUESTION_13>

Question 14: Should the disclosure requirements address an investment product's intention to align with policy goals, such as the UN Sustainable Development Goals (SDGs), and if so, should these requirements be part of general disclosure requirements or feature-specific disclosure requirements?

<QUESTION_14>

No.

<QUESTION_14>

Question 15: Should the disclosure requirements include an explanation of whether, and if so how, an investment product considers principal adverse impacts on sustainability factors and where to find additional information, as required by Article 7 of Regulation EU 2019/2088 Sustainable Finance Disclosure Regulation?

<QUESTION_15>

No

<QUESTION_15>

Proposal for ESG-Related Features and feature-specific Disclosure Requirements

Question 16: Do you believe that "ESG Integration" is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

<QUESTION_16>

No, we believe the term ESG Integration is too vague and ambiguous. The term should be replaced for ESG Compliance Matrix seeking to automate and streamline the disclosure and compliance process of meeting the standard via the inclusion of specific ESG Related Factors and/or ESG Features.

<QUESTION_16>

Question 17: If an investment product had Feature (A), and only Feature (A), as defined above, would it be consistent with the CFA institute policy paper "Positions on Environmental, Social, and Governance Integration"? In other words, would it be clear that material ESG-related factors are considered alongside traditional financial factors solely to seek to improve risk-adjusted returns? If not, please suggest how that could be made clearer.

<QUESTION_17>

No. If this is the case it should be called "ESG Alpha Enhancement" <QUESTION_17>

Question 18: Is Feature (A) clearly defined? If not, please explain how the definition could be made clearer or more precise.

<QUESTION_18>

No. In general, the six features are too vague as per previous comments.

<QUESTION_18>

Question 19: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (A)? Are there issues that should be added, deleted, or modified?

<QUESTION_19>

No, the Functions should establish the minimum ESG Related Factors and/ or Features which alone or in combination with other ESG- related factors and/or ESG features satisfy the conditions required to meet the standard or segmented levels of the standard. i.e. Leed Certification <QUESTION_19>

Question 20: Do you believe that "ESG-related Exclusions" is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

<QUESTION_20>

No. Combining both the exclusions under a single item on "security selection," is confusing combined in as these are subjective factors included on IPS exclusion frameworks. Hence this could be deal with by clearly stating the exclusions via business strategic approach or financial disclosure line items i.e., "Our fund excludes firms which are focused, and/or have core operations, business units, revenues from involvement in the manufacturer of tobacco and weapons, etc." in addition to " those scoring in the lowest quintile of peers according to our IPS, proprietary ratings methodology, which considers corporate impacts on a wide range of stakeholders. We also overweight, relative to the benchmark, those issuers which represent and intention to implement an ESG transition relative to best industry leader peer group' standards "CFA ESG Standards" <QUESTION_20>

Question 21: Are "negative screening" and "norms-based screening" similar enough, particularly in the types of issues to be addressed by disclosure requirements, that they can both be covered by Feature (B) ESG-Related Exclusions? If you prefer that they be two separate features, please explain the key differences in function, benefits, and disclosure requirements.

<QUESTION_21>

Please refer to 20

<QUESTION_21>

Question 22: Is Feature (B) clearly defined? If not, please suggest how the definition could be made clearer or more precise.

<QUESTION_22>

It seems to represent a value judgment whereas exclusions aren't about moral issues, we would argue some as religious beliefs relate to exogenous factors instead not risk selection <QUESTION_22>

Question 23: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (B)? Are there issues that should be added, deleted, or modified?

<QUESTION_23>

Yes

<QUESTION_23>

Question 24: Do you believe that "Best-in-Class" is a clear and appropriate name for this feature? If not, is "Positive ESG Performance Profile" a better name? If you dislike both of these names, please suggest an alternative and explain why it would be a better choice.

<QUESTION_24>

Yes

<QUESTION_24>

Question 25: Do you agree that Feature (C) is distinct enough, particularly in the types of issues to be addressed by disclosure requirements, that it should be separate from other features? If not, please suggest the feature with which it should be combined.

<QUESTION_25>

Please refer to above

<QUESTION_25>

Question 26: Is Feature (C) clearly defined? If not, please explain how the definition could be made clearer or more precise.

<QUESTION_26>

Please refer to above

<QUESTION_26>

Question 27: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (C)? Are there issues that should be added, deleted, or modified?

<QUESTION_27>

Yes, but it would take time to reach consensus for standardization and adoption unless mandatory to qualify under a new gold standard i.e. CFA ESG Standard.

<QUESTION_27>

Question 28: Do you believe that "ESG-related Thematic Focus" is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

<QUESTION_28>

No, we think this would need to have a separate qualifier(s), to eliminate ambiguity as today is hard to distinguish "ESG-Enhanced Focused Alpha" the investors and asset owners require transparency and simplicity to select among the multiple themes.

<QUESTION_28>

Question 29: Do you agree Feature (D) is distinct enough, particularly in the types of issues to be addressed by disclosure requirements, that it should be separate from other features? If not, please suggest the feature with which it should be combined.

<QUESTION_29>

No please refer to the next answers below

<QUESTION_29>

Question 30: Is Feature (D) clearly defined? If not, please explain how the definition could be made clearer or more precise.

<QUESTION_30>

No, thematic focus is an ambiguous term the Benefits have to be quantifiable in reference to the benchmark to become eligible ESG Investment Product

<QUESTION_30>

Question 31: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (D)? Are there issues that should be added, deleted, or modified?

<QUESTION_31>

No, and yes TBD

<QUESTION_31>

Question 32: Do you believe that "Impact Objective" is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

<QUESTION_32>

No, once more the "impact objective" like the previous terms are is hard to define even harder to quantify, the goals and objectives are usually described in the general fund objective without including them as part of the ESG framework.

<QUESTION_32>

Question 33: Is Feature (E) clearly defined? If not, please explain how the definition could be made clearer or more precise.

<QUESTION_33>

Refer to 32

<QUESTION_33>

Question 34: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (E)? Are there issues that should be added, deleted, or modified?

<QUESTION_34>

The expectation for asset managers to integrate such a robust and demanding process into their routine is simply unrealistic. There is no time for quantification, measurement, ranking, and so on. Hence the focus should be placed on decisive quantifiable factors that can be monitored and tracked using commercially viable technologies today.

<QUESTION_34>

Question 35: Do you believe that "Proxy Voting, Engagement, and Stewardship" is a clear and appropriate name for this feature? If not, please suggest an alternative and explain why it would be a better choice.

<QUESTION_35>

Not a bad designation, however—as per the comments below—the proposed framework demands the allocation of a disproportionate amount of time on portfolio construction relative to holdings, when in fact the investors have a binary option to either support (buy) or disapprove an asset (sell) effecting alignment to their views on ESG: using dollars to vote instead through proxy voting, dialogue, shareholder resolutions. All these usually happens at the asset management level instead of the fund management level

<QUESTION_35>

Question 36: Do you agree that "Proxy Voting, Engagement, and Stewardship" should be a distinct feature? If not, would you prefer that the types of issues to be addressed by disclosure requirements be redistributed to other features or to general disclosures?

<QUESTION_36>

Please refer to comments below as per weight and importance in factor to security selection
<QUESTION_36>

Question 37: Is Feature (F) clearly defined? If not, please explain how the definition could be made clearer or more precise.

<QUESTION_37>

The definition places too much emphasis on the materiality of the risk and returns, typically defined in a short time horizon and related to individual security selection, when in fact engagement by long-term owners holding the market, should place focus on systemic correlation risks analysis. The proxy voting focus suggests a short-term focus when engagement typically aims at long term Asset Liability Management (ALM) caused by sensitivity to ESG factors. We should also question the alignment and reliance on proxy advisors when there is evidence of proxy vote lending practices validating the asymmetric flow of short-term arbitrage opportunities vs ALM factors aligned with ESG

<QUESTION_37>

Question 38: Do you agree with the issues to be addressed by the disclosure requirements specific to Feature (F)? Are there issues that should be added, deleted, or modified?

<QUESTION_38>

Please refer to below

<QUESTION_38>

Question 39: Do the six features described fully cover the spectrum of ESG-related features currently offered in the marketplace?

<QUESTION_39>

Please refer to below

<QUESTION_39>

Proposal for Classification of ESG-Related Features According to ESG-Related Needs

Question 40: Does this list of ESG-related needs represent the spectrum of investors' ESG-related needs?

<QUESTION_40>

Yes

<QUESTION_40>

Question 41: Are these five ESG-related needs clearly differentiated and mutually exclusive?

<QUESTION_41>

No

<QUESTION_41>

Question 42: Do you agree with the classification of ESG-related features according to ESG-related needs, as shown in Table 3? If not, how might it be improved?

<QUESTION_42>

Yes—it appears to be a need to link features to needs to standardize the ESG designation. Most ESG investors want their investments to generate Alpha; some expect alignment with their moral positions; others may also seek to contribute to what they perceive as positive changes in society.

<QUESTION_42>

Users and Benefits

Question 43: Do you agree with the description of user benefits? Are there any benefits that should be added or deleted?

<QUESTION_43>

Yes

<QUESTION_43>

Question 44: Do you agree with the terms used to define the users of the Standard? Are there any terms we should include, or avoid using?

<QUESTION_44>

Good as starting point

<QUESTION_44>

General Comments: Please enter the general comments below.

<GENERAL_COMMENTS>

FlatStone Capital Advisors Inc. (FlatStone or FCA) agrees with the CFA Institute poll related to the need for a standard that would address the evident market integrity issues which pose a challenge for all stakeholders. As a Canadian Asset Manager with a significant focus on the energy and resource sectors we feel is a requirement to empower market professionals unable to exercise their fiduciary duty with an ever-expanding shelf of investment products claiming a multitude of ESG-related features which lack consistency and universal meaning.

As a signatory to the CFA Institute Asset Manager Code, FCA welcomes the development of a new global standard enabling greater transparency and comparability for investors enabling asset managers to clearly communicate the ESG-related features of their investment products among investment products.

FlatStone vision for an ESG Global standard would facilitate the compliance and report under a GIPS ESG Standard methodology by leveraging enterprise blockchain technology enabling traceability (provenance), enhancing transparency, and establishing trust by ensuring market integrity.

The CFA should focus on developing numerical models and formulas capable of measuring and capturing the effects of ESG ALPHA

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<GENERAL_COMMENTS>