

August 11, 2020

New Common Terminology for ESG Investing Strategies

Funds' Use of Integration and Sustainable Investing Strategies: An Introduction

“We created this introduction to ESG investing strategies to encourage funds to use consistent terminology when describing ESG integration and sustainable investing strategies. ... The working group hopes the document will also help improve the public’s understanding of ESG investing and help inform ... about the many choices that funds provide.”

*ICI’s Environmental, Social, and Governance
Working Group (July 2020)*

ICI Board of Governors Unanimously Supports

“We strongly endorse the recommendations of the Working Group and urge all ICI members to take such actions as may be appropriate to implement the terminology recommended as soon as reasonably practicable.”

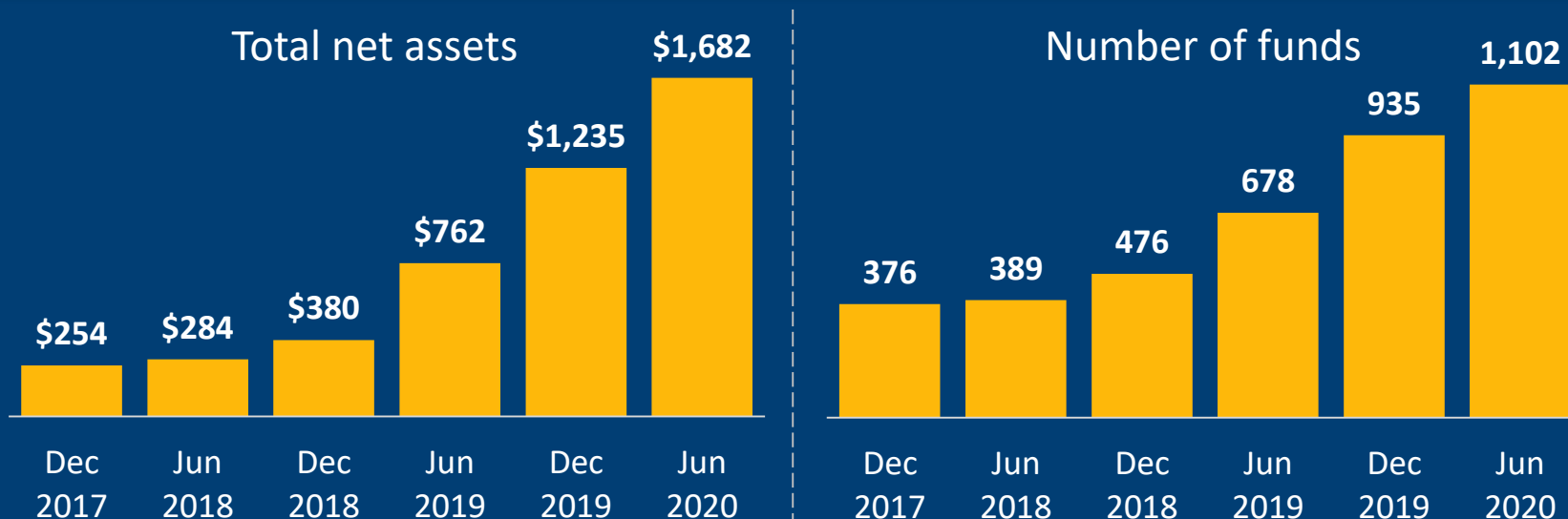
ICI Board of Governors (July 2020)

Panelists

- » Jane Carten, President, Director, and Portfolio Manager, Saturna Capital
- » Karla Rabusch, Independent Trustee, Board of Directors, Lord Abbett Funds
- » Jennifer Wu, Global Head of Sustainable Investing, J.P. Morgan Asset Management
- » Moderator: Dorothy M. Donohue, Deputy General Counsel, Securities Regulation, ICI

ESG Landscape: More ‘Socially Conscious’ Funds

Total net assets in billions of US dollars



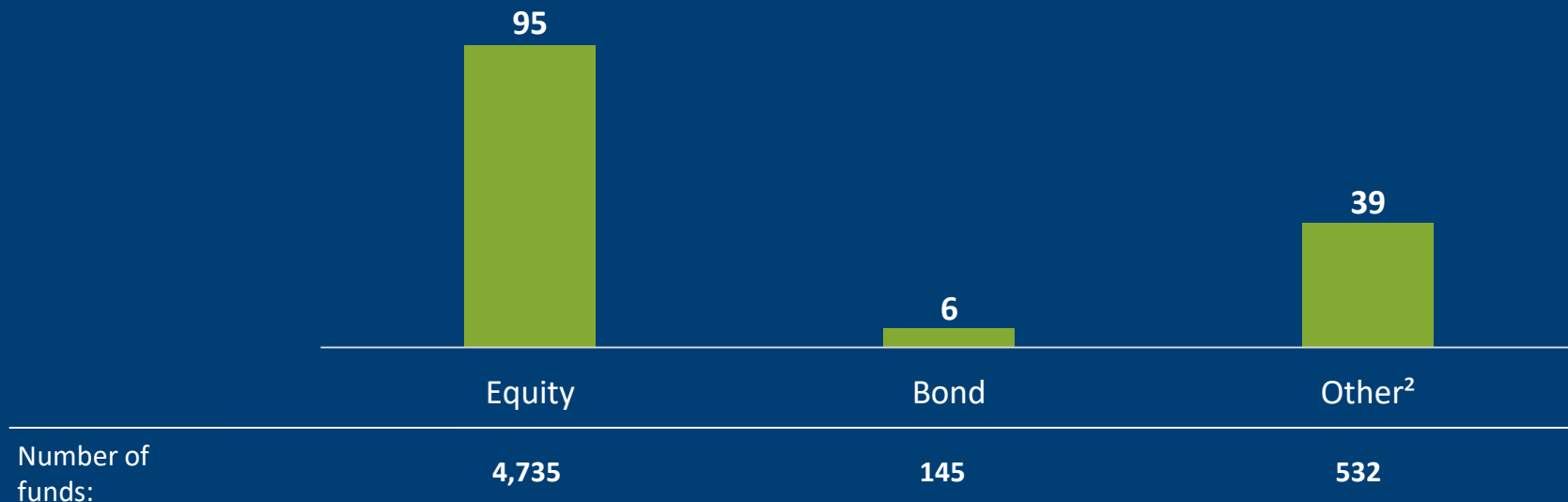
**Socially conscious* is defined as a fund that invests according to non-economic guidelines. This may include funds that invest based on environmental issues, but will also include funds with exclusionary clauses that prohibit the fund from investing in certain industries such as alcohol and tobacco.

Note: Data include exchange-traded funds but exclude funds that invest primarily in other funds.

Source: Morningstar

ESG Landscape: Equity Funds Predominate

Percentage of funds that have a Morningstar ESG Sustainability rating¹



¹ Data are those available in Morningstar Direct as of July 23, 2020.

² Other includes balanced funds, alternative funds, commodities, and a small number of funds without an assigned US category group.
Note: Data include mutual funds and ETFs but exclude money market funds. Data also exclude funds that invest primarily in other funds.
Source: Investment Company Institute tabulations of Morningstar Direct data

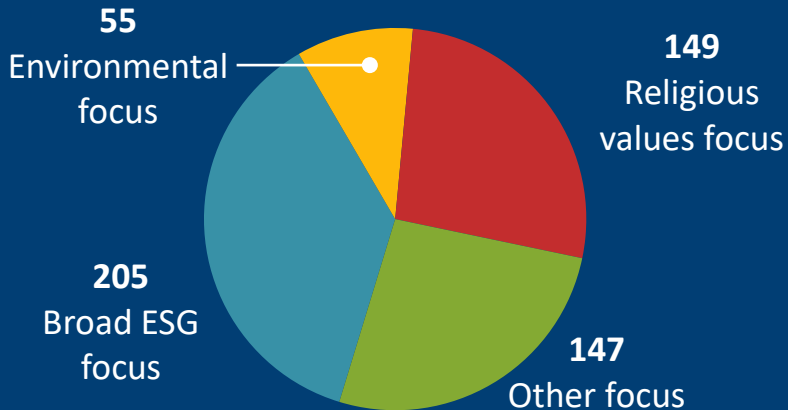
Scaling the US ESG Market: ICI Research

- » Categorize funds objectively by applying predetermined rules and definitions
- » Focus on fund prospectus language—‘Investment Objective’ and ‘Principal Investment Strategies’
- » Identify language indicating that a fund places an important and explicit emphasis on environmental, social, or governance criteria to achieve certain goals

Number, Assets of Funds that Invest by ESG Criteria

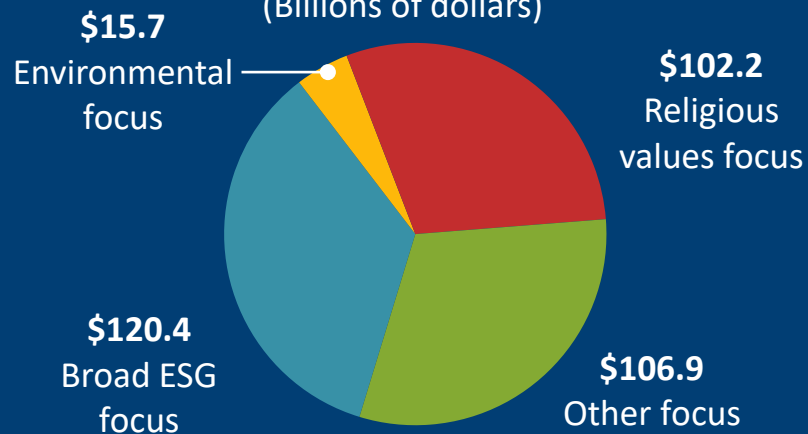
By focus, June 2020

Number of funds



Total number of funds: 556

Total net assets
(Billions of dollars)

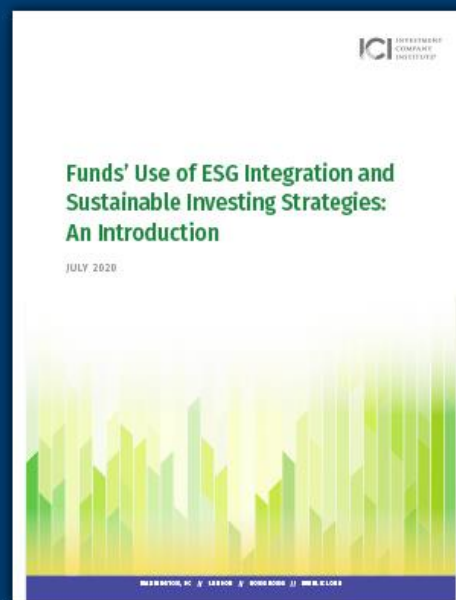


Total net assets: \$345.1 billion

Note: Data include mutual funds and ETFs. Data include mutual funds that invest primarily in other mutual funds and ETFs that invest primarily in other ETFs. For a small number of funds, Morningstar data is used for total net assets.

Sources: Investment Company Institute and Morningstar.

ICI Activity: Research and Terminology



A Broad Spectrum of ESG Investing

Integration

Inclusion

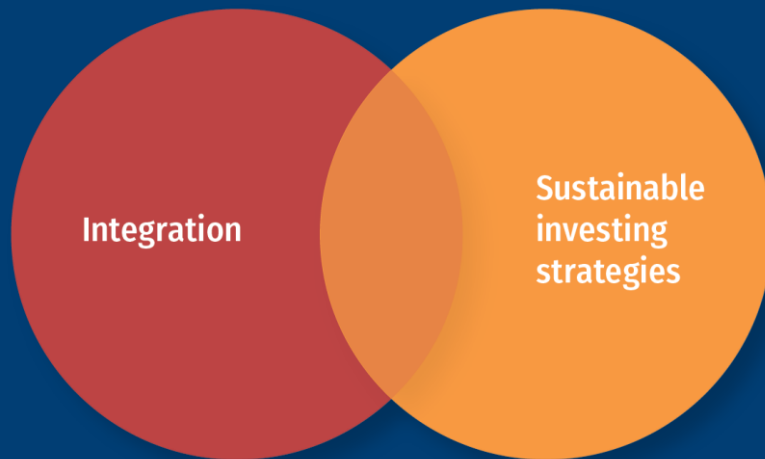
Impact

Note: Each of these investing strategies may also incorporate aspects of exclusionary investing.

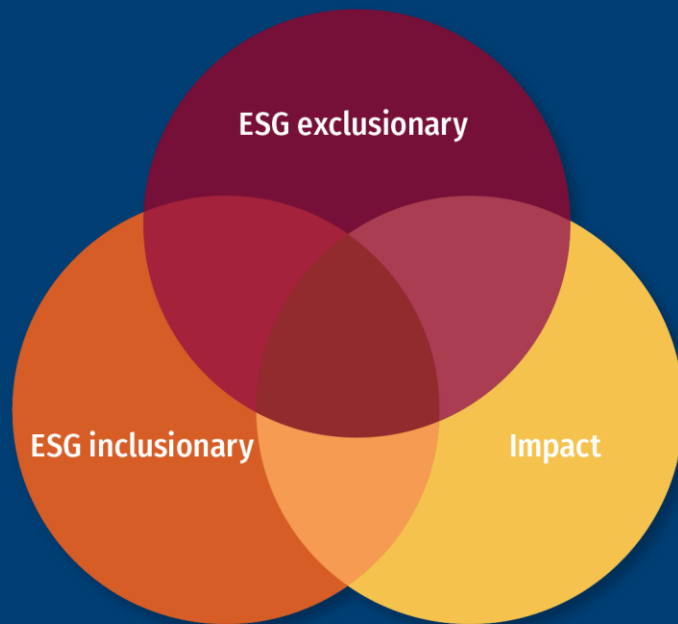
ESG Strategies Encompass Many Concepts

- » Integration
- » ESG Exclusionary: negative screening, optimization, socially responsible investing (SRI), and values driven
- » ESG Inclusionary: best in class, ESG tilted, positive screening, sustainable, and thematic
- » Impact: community investing, goal-based, sustainable, and thematic

Integration, Sustainable Investing Overlap ...



As Do Sustainable Investing Strategies



Questions Fund Directors Might Consider Asking

- » Does management support the ICI's common terminology and, if not, why not?
- » How do our funds' current disclosure align with, or differ from, the ICI's common terminology? What, if any, changes are being considered?
- » Which communications will need updating? How and when will this happen?

SEC Focus on ESG Funds

- » Review of ESG fund names and prospectus disclosure
 - » 'Green,' 'sustainable'
 - » Is name consistent with investment strategy?
- » OCIE exam request letter asks about:
 - » Proprietary or third-party ESG scoring systems
 - » ESG-related investment decisions
 - » Engagement with portfolio companies on ESG issues
 - » ESG-related marketing materials

Public Company Disclosure: A Spectrum of Views



Asset managers should have **access to critical information** related to climate risk and, more broadly, to ESG issues to meaningfully pursue their investment goals.



Disclosure of **material information includes financial and nonfinancial information** and should be evaluated from a reasonable investor's perspective.



I have serious reservations about **imposing prescriptive disclosure requirements on public companies** because this type of mandated disclosure is often fraught with personal views.



A new SEC disclosure framework for ESG information **seems unnecessary.**

SEC Views on Fund Manager Responsibilities

Lee

Are asset managers investing and voting in line with long-term client goals?

Lee and Roisman

Funds with ESG names need clearer parameters

Roisman

Fund investors who want 'green' or 'sustainable' products deserve more clarity.

Another risk for investors is "greenwashing,"

DOL Proposal on Retirement Plans and ESG Investing

“Private employer-sponsored retirement plans are not vehicles for furthering social goals or policy objectives that are not in the financial interest of the plan. Rather, ERISA plans should be managed with unwavering focus on a single, very important social goal: providing for the retirement security of American workers.”

*Eugene Scalia, Secretary of Labor
(June 2020)*

ICI's View on DOL Proposal

“We cannot support the Proposed Rule because we are deeply concerned that it will have significant unintended consequences. It is premised on an incorrect assumption that integrating ... ESG considerations into an investment strategy is, by its nature, ... inconsistent with ... the plan’s financial returns.”

*Paul Schott Stevens, President and CEO
Investment Company Institute
(July 2020)*

What's Next?

- » New Administration?
- » New Congress?
- » Fad or Here to Stay?

Appendix: Resources

- » “Environmental, Social, and Governance Investing,” *2020 Investment Company Fact Book*
 - » www.ici.org/pdf/2020_factbook.pdf at page 50.
- » ICI Comment Letter on SEC Request for Comment on Fund Names Rule (May 5, 2020)
 - » www.ici.org/pdf/20_ltr_fundnames.pdf
- » *Funds’ Use of Integration and Sustainable Investing Strategies: An Introduction* (July 2020)
 - » www.ici.org/esgprimer

Appendix: Resources

- » ICI Comment Letter on Financial Factors in Selecting Plan Investments (July 30, 2020)
 - » www.ici.org/pdf/20_ltr_dolesg2.pdf
- » ICI ESG Investing Resource Center
 - » www.ici.org/esg
- » “Public Companies, Disclosure of Environmental, Social and Governance Factors and Options to Enhance Them,” Government Accountability Office (July 2020)
 - » www.gao.gov/assets/710/707949.pdf