Revised Towards Sustainability Quality Standard
Final criteria

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Introduction

This document presents the criteria of the revised Towards Sustainability Quality Standard (QS).

The priorities for this revision were determined by the CLA Board of Directors:

1. Alignment and complementarity of the Towards Sustainability Quality Standard with (upcoming) EU legislation and future initiatives on sustainable finance (such as EU Taxonomy, Sustainable Finance Disclosure Regulation, Climate Benchmark Regulation, EU Ecolabel, etc.)
2. ESG assessment of financial institutions
3. ESG assessments of the energy and electricity utilities sector
4. Increased transparency requirements
5. Other technical issues and need for clarifications

The revised criteria were developed by the CLA Eligibility Commission in line with the CLA Board of Directors’ priorities and taking into account the recommendations of the CLA’s Advisory Commission. Information on the CLA governance structure and the composition of the commissions can be found on the CLA website: [https://www.towardssustainability.be/en/central-labelling-agency-cla](https://www.towardssustainability.be/en/central-labelling-agency-cla)

The revised criteria integrate the results of the multiple external checks that were performed concerning feasibility, verifiability, data availability and regulatory compliance.

Technical version of the revised criteria

This document contains the criteria of the revised QS in a technical format.

Requirements in the current QS that are not updated by the new revised criteria, will stay in place.

A consolidated and translated version of the revised QS will be published on the CLA website at a later stage.

Timing

The revised criteria will come into effect in January 2022.
1. Sustainability strategies

1.1 Number of ESG strategies

Criteria
A sustainable financial product shall make use of the following (4) strategies:

1. ESG integration (see 1.2)
2. Normative screening (see 1.3)
3. Exclusion (see 2.1 and 3)
4. At least 1 additional strategy

The first 3 strategies ensure the products does not finance activities that pose significant harm to sustainability factors. The additional strategy or strategies support the positive ESG impact the product wants to realize.

The additional strategies can have varying degrees of selectivity or focus:

a) Best-in-class/universe selection (see 1.4)
b) Sustainability themed investing (see 1.5)
c) Impact investing (see 1.6)
d) Over/underweighting of exposures to individual positions relative to higher/lower ESG scores
e) Objective to do better than a benchmark on one or more ESG indicators
f) Other strategy, recognized by the CLA, that results in favouring more sustainable issuers in the selection process

The manager shall disclose the selection methodology and/or portfolio-level ESG characteristics and/or objectives.

Next to the 4 strategies, the manager shall put in place appropriate corporate engagement or shareholder action (see 1.7) regarding the fossil fuel sector. It is also encouraged for other sectors with elevated risks for principal adverse impacts.

All sustainability strategies that are applied will be mentioned on the Sustainability ID. Investors will be able to filter products based on the types of additional strategies.

The manager shall calculate reduction rate (by number of issuers) resulting from the application of all sustainability strategies. The reduction rate will be published on the Sustainability ID, presented in brackets (E.g. 0-10%, 10-25%, +25%). For thematic and impact funds, the reduction rate is defaulted to the highest bracket.
Sustainability strategies – universe reduction

0 - Total universe
• Initial demarcation of investments by region, sector, size, type, ...
  • E.g. EU Equity, Emerging markets debt, US Energy, Japan small-caps, ...

1 - Investable universe
• ESG integration: ESG due diligence (principle adverse impacts on sustainability factors)
• Normative screening
• Sector policies

2 - ESG Negatively screened universe
• Best-in-class/universe selection
• Sustainability themed investing
• Impact investing
• Over/underweighting
• Better than benchmark
• Other

3 - ESG Positively screened universe
• ESG integration: Sustainability risk assessment
• Financial evaluation (risk-return)

4 - Product portfolio
• Corporate engagement/shareholder action

Figure 1
1.2 ESG integration

Criteria

The manager shall have formal and credible policies and procedures in place to assess:

a) the likely impacts of sustainability risks on the return of the product
b) the risk of principal adverse impacts on sustainability factors (E+S+G) of each investment.

The manager shall consider, where appropriate:

- the OECD Guidelines for Multinational Enterprises: Responsible Business Conduct for Institutional Investors
- the UN Principles for Responsible Investing (UN PRI)

For a) and b) the manager can use information obtained directly from the issuer, data sourced from ESG data providers or rating agencies and public available data.

For each position in the portfolio (except technical assets) an ESG due diligence result shall be present.

The depth and focus of the ESG due diligence process shall take into account the likelihood and size of the potential negative impact (= materiality) on sustainability factors of each investment.

A controversy screening (e.g. based on UN Global Compact violations) is not considered sufficient as ESG integration.

The practical implementation of ESG integration will be a focus of the on-site audit.

See also the section on ESG due diligence and analysis in the current QS.
1.3 Normative screening

Criteria

The manager shall have in place procedures to monitor the alignment of investee companies with:

- The UN Global compact
- The UN Guiding Principles on Business and Human Rights (UNGPs)
- The OECD Guidelines for Multinational Enterprises (as far as relevant)
- The ILO Conventions

This means that managers shall at least verify, based on available information, whether investee companies are not involved in (structural, repetitive and severe) controversies or violations of these frameworks.

Additionally, their shall be no clear indications of companies’ involvement in manufacturing doubt about the principal adverse impacts on sustainability factors of their activities (e.g. actively spreading misinformation). This shall be part of a controversy screening.

For requirements for sovereign issuers (States) see 2.1
1.4 Best-in-class/universe selection

Criteria

A best-in-class or best-in-universe strategy shall select from the ‘ESG negatively screened universe’ ('investable universe' after mandatory exclusions and normative screening), only the issuers with the highest ESG ratings, evaluated per industry/sector/region (best-in-class) or evaluated on the level of the universe as a whole (best-in-universe).

The ESG ratings can be based on a quantitative or qualitative ESG rating scale.

The issuers selection threshold can be relative (top percentile) or absolute (minimum rating).

The manager shall disclose the calculated average selectivity (in % of issuers in/excluded) of the best-in-class/universe selection strategy.

The manager shall describe the source of the ESG ratings, the ESG rating scale, the selection threshold and methodology used.
1.5 Sustainability themed investing

Criteria

A sustainability themed investing strategy shall select investments using one or more well-defined themes based on relevant frameworks, recognized by the CLA, to measure contribution to sustainability factors (EU Taxonomy, SDGs, EU Green Bond Standard, ICMA Social Bond Principles, etc).

Additionally, it shall comply with at least 1 of the following:

a) At least 70% of the assets in the portfolio (measured by company or by AUM) are related to the theme(s). An investee company is considered related to a theme if at least 50% of its revenue is related to the theme.

b) At least 50% of the total portfolio (by AUM) is invested in economic activities contributing to the theme.

c) The product uses a best-in-universe strategy (see 1.4) selecting the top 25% highest rated issuers (‘leaders’) based on an ESG rating appropriate to the theme.

d) The product classifies as an SFDR art. 9 product and has sustainability themed investing as a strategy.

If the product has the EU Ecolabel then the requirements for a sustainability themed investing strategy are considered fulfilled.

The manager shall disclose the selection of the theme(s) and the implementation in the portfolio.
1.6 Impact investing

Criteria
An impact investing strategy shall select investments using one or more well-defined themes based on relevant frameworks, recognized by the CLA, to measure contribution to sustainability factors (EU Taxonomy, SDGs, EU Green Bond Standard, ICMA Social Bond Principles, etc).

Additionally, it shall comply with at least 1 of the following:
   a) At least 70% of the assets in the portfolio (measured by company or by AUM) are related to the theme(s). An investee company is considered related to a theme if at least 90% of its revenue is related to the theme.
   b) The product classifies as an SFDR art. 9 product and has impact investing as a strategy.

The manager shall disclose the selection of the theme(s) and the implementation in the portfolio.

The manager shall publish an annual impact report.
1.7 Corporate engagement or shareholder action

Criteria

The manager shall put in place an appropriate corporate engagement or shareholder action process regarding the fossil fuel sector. Corporate engagement or shareholder action is encouraged for other sectors with elevated risks for principal adverse impacts.

The manager shall clarify its engagement approach, e.g.:

- **a)** Engagement policy which describes:
  - Objectives
  - Strategy
  - Methods
  - Monitoring and reporting of outcome
- **b)** Policy regarding exercising of voting rights and reporting about voting
- **c)** Dialogue with investee companies

The product manager shall actively and regularly engage at management level with companies in the fossil fuel sector. These companies shall be selected from amongst those with the most material risk for adverse impact.

Engagement shall at least interrogate issuers about their alignment with the objectives of the Paris agreement, including about intermediatory targets for 2030.

If appropriate, the manager shall publish an annual engagement and/or voting report. This will include detailed information on the degree of engagement towards companies in fossil fuel sector.

The use of specific portfolio management techniques shall not preclude engagement when chosen as a strategy or when required by the QS.

Corporate engagement or shareholder action does not count to reach the required minimal number of sustainability strategies (see 1.1).
1.8 Solidarity/Charity

Criteria

The use of a solidarity or charity component by the manager can be taken into account (as a strategy) and mentioned on the Sustainability ID when the manager has in place monitors and reports about the impact to the charity.

The manager shall disclosure:

- the details of the solidarity approach and the beneficiaries of the charity
- the % (of fees) that go to selected charities, if applicable

However, this strategy does not count to reach the required minimal number of sustainability strategies (see 1.1).
2. Specific asset classes, investment techniques and product types

2.1 Sovereign bonds

Criteria

A sustainable financial product shall not finance (e.g. via sovereign issued instruments):

- States that have not ratified or have not implemented in equivalent national legislation:
  - the eight fundamental conventions identified in the International Labour Organisation’s declaration on Fundamental Rights and Principles at Work
  - at least half of the 18 core International Human Rights Treaties
- States which are not party to:
  - the Paris Agreement
  - the UN Convention on Biological Diversity
  - the Nuclear Non-Proliferation Treaty
- States with particularly high military budgets (>4% GDP)
- States considered ‘Jurisdictions with strategic AML/CFT deficiencies’ by the FATF
- States with less than 40/100 on the Transparency International Corruption Perception Index
- States qualified as ‘Not free’ by the Freedom House ‘Freedom in the World’ survey

Products can invest for reasons of diversification or (currency risk) hedging, in public debt instruments issued by core reserve (non-EURO) currency issuers\(^1\) that do not comply with the above requirements, to a maximum of 30% (in total) of the portfolio. This threshold may temporary be exceeded in the event of extraordinary market conditions. In any case, this will be indicated on the Sustainability ID.

Products classified as an SFDR art. 9 product and with an emerging markets focus can invest in public debt instruments issued by States that do not comply with the above requirements. In any case, this will be indicated on the Sustainability ID.

Use-of-proceeds instruments issued by States can be eligible. See 4.3 e)

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\(^1\) I.e. the US, Japan and the UK
2.2 Securities lending

Criteria
The use of securities lending shall not preclude engagement when chosen as a sustainability strategy or when required by the QS. This means that the lender should get back control over the securities to exercise his voting rights as beneficial owner. Borrowing securities with the purpose of using them to exercise voting rights as borrower is not accepted. Thus, the lenders should have the ability to recall and/or restrict securities for a certain period during the lending programme.

The lender shall have a dialogue with the custodian about the possible integration of sustainability considerations in the securities lending criteria.

The lender shall, on a best effort basis, ensure and monitor that the securities are not used contrary to its own ESG policies and the principles of the QS. The lender shall have credible procedures in place to handle potential conflicts.
2.3 Unsegregated portfolios

Criteria
Sustainable financial products of which the assets are not legally separated (ring-fenced), can determine a virtually separated asset pool within the larger unsegregated asset pool in such a way as to ensure that the assets underlying the sustainable financial products are traceable and correspond with the money invested in them.

As for the composition of the virtually separated asset pool:
- The assets in the virtual pool shall be QS compliant
- The size of the virtual pool shall be equal or greater than the total value of all sustainable financial products that make use of it
- The percentage of corporate-issued securities in the virtual pool shall, as far as technically possible, be at least as high as the percentage of corporate-issued securities in the total unsegregated asset pool

As for the auditability of the virtually separated asset pool:
- QS compliant assets shall be clearly earmarked
- The compliance of the virtual pool’s composition shall be independently attested

In addition, the product manager shall be transparent and report about:
- The asset allocation of the unsegregated asset pool
- The ESG relevant evolution of the unsegregated asset pool
- The % of unsegregated asset pool that is QS compliant
2.4 Saving deposit products

Criteria
A saving deposit product of which the assets are not legally separated (ring-fenced) on the balance sheet, shall determine a virtually separated asset pool within the larger unsegregated asset pool in such a way as to ensure that the assets underlying the sustainable financial products are traceable and correspond with the money invested in them (See 2.3).
2.5 Branch21 insurance products

Criteria
A branch21 insurance product of which the assets are not legally separated (ring-fenced), shall determine a virtually separated asset pool within the larger unsegregated asset pool in such a way as to ensure that the assets underlying the sustainable financial products are traceable and correspond with the money invested in them (See 2.3).

Grandfathering
- If a fixed income position, that is part of the guarantee providing structure, was QS compliant when the position was bought but is not QS compliant anymore, the position can be held for a maximum of 5 years.
- The grandfathered fixed income positions cannot be increased and can in total not represent more than 10% of a virtually separated asset pool.
- These fixed income positions can only serve to cover existing guarantees, not to cover new guarantees for new clients. Fixed income positions covering guarantees for new clients shall be QS compliant.
- As soon as possible, without negative effects for the guarantee, the fixed income positions shall be sold.
2.6 Structured products

Criteria

A structured product is QS compliant when all composing parts are QS compliant, i.e.:

1. For the funding component (asset basket or fixed income instrument), one of the below:
   - The issuers of the assets in the asset basket or of the fixed income instrument are QS compliant.
   - The asset basket is a QS compliant virtually separated asset pool (see 2.3)
   - The issuer of the fixed income instrument is a financial institution with headquarter in a OECD country and compliant with the QS criteria for financial institutions (see 3.8).

2. For the index component (of which the performance is swapped)
   - The index composition methodology is QS compliant.

3. For the derivative component: a swap is considered a purely technical instrument and thus ESG neutral

Note the general rule that the Towards Sustainability label is awarded for 1 year and then expires. Products with longer maturity that want to keep using the label after the first year need to reapply and will be reassessed for QS compliance.
2.7 Fund of funds

Criteria

For a fund of funds to be QS compliant, at least 75% of underlying portfolios (measured by AUM) must have the Towards Sustainability label or another ESG label recognized by the CLA\(^2\).

Alternatively, the fund of funds manager can request a formal commitment of the managers of (external) underlying portfolios to be compliant with the QS. The fund of funds manager remains however, fully accountable and responsible for the fund of funds’ compliance with the QS.

Underlying index-based products can be evaluated on QS compliance using a look-through approach, if based on a solid regular monitoring and audit system. The look-through approach shall ensure that the composition of the indices is compliant with the exclusionary requirements of the QS.

The remainder (max. 25% measured by AUM) of underlying portfolios must be:

- Products that promote ESG characteristics and also partially have sustainable investments\(^3\), or
- Products that promote ESG characteristics and also consider principal adverse impacts on sustainability factors, or
- Products that have sustainable investment as an objective (SFDR art. 9).

The Sustainability ID will mention the % of underlying funds (by AUM) that does not have the Towards Sustainability label or another recognized label.

Other assets (except for purely technical reasons) in the fund of funds’ portfolio must be QS compliant.

**Grandfathering**

- Until end 2022 a look-through approach is also allowed for not index-based products, if based on a solid regular monitoring and audit system.
- Until end 2023, a fund of fund can also contain up to 50% index-based products that were awarded the Towards sustainability label in the past and are SFDR art. 8 or 9 products.

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\(^2\) Currently no other ESG labels are recognized

\(^3\) As defined in Article 2, point (17), of the SFDR
3. Sector policies (Corporate-level criteria)

3.1 General approach

Criteria

a) Scope

- Companies involved in harmful activities (see Annex) that could lead to adverse impacts on sustainability factors, or companies providing dedicated equipment or services to enable these activities.
  - Value chain to be taken into account:
    i. Companies with direct involvement in the execution of harmful activities
    ii. On a best effort basis, companies with more than 50% of their revenues derived from products/services dedicated to the execution of harmful activities. Products/services aimed at mitigating or reducing negative effects of these activities should not be included.
    iii. On a best effort basis, companies with more than 50% of their revenues derived from companies in i. or ii.
  - Parent-Subsidiary relationships
    i. The eligibility of a parent company takes into account eligibility of subsidiary companies.
    ii. The eligibility of subsidiary companies is not dependent on the eligibility of the parent company.
- Indicative sector/industry classifications (see Annex) are provided for illustrative purposes and do not limit the scope of the QS criteria.
- Companies involved in multiple harmful activities will need to comply with all relevant QS requirements.

b) Governance criteria

- Companies shall have a strategy to reduce the adverse impact of their activities and to increase their contributing activities, if applicable.

c) Business criteria

Companies shall comply with a selection of quantitative criteria appropriate to their activities.

Indicators to measure avoidance of harm:

- Absolute production of harmful products or absolute capacity for harmful activities
- Revenue/turnover derived from harmful activities
- Capital expenditures (CapEx) dedicated to harmful activities
- Other sector-relevant indicators

Indicators to measure transition:

- Ambitious measurable & auditable commitment to reduce principle adverse impacts within strict timelines
- Capital expenditures (CapEx) dedicated to contributing activities (see Annex)
- Other sector-relevant indicators

Indicators can be understood as annual average over the previous 3 years, if available.
When the QS allows for a choice between indicators, this choice can be made on a company by company basis.

Where information relating to any of the indicators used is not readily available, the manager shall provide details of the best efforts used to obtain the information either directly from investee companies, or by carrying out additional research, cooperating with third party data providers or external experts or making reasonable assumptions. Such assessments and estimates should only compensate for limited and specific parts of the desired data elements, and produce a prudent outcome.

d) **Phase-out margin**

Some companies are currently not yet aligned with the business criteria in c) but are nevertheless within the best of their peer group in transitioning their business model. A sustainable financial product can finance these companies selectively and to a limited extent. However:

- The total portfolio exposure to non-compliant companies (only concerning eligible activities⁴) is < 5%. This margin will decrease by 1pp (percentage point) per year as of 1/1/2023.
- Additionally, companies in this margin shall be subject to a best-in-class selection that selects from the 25% highest ESG-rated companies (leaders), with special attention to sustainable energy transition.
- Companies in this margin shall still meet the governance criteria b).

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⁴ Eligible activities are conventional oil & gas (3.6) and power generation (3.7)
3.2 Tobacco

Criteria

a) Scope
   • Companies involved in the production or wholesale trading of tobacco products or providing dedicated equipment or services therefor (see also 3.1 a).
   • Indicative sector/industry and activity classifications (See Annex)

b) Governance criteria
   • See 3.1 b)

c) Business criteria
   • The company shall derive less than 5% of its revenues from the production of tobacco, products that contain tobacco or the wholesale trading of these products.

d) Phase-out margin
   • Companies not compliant with these criteria are not eligible for the phase-out margin.
3.3 Weapons

Criteria

a) **Scope**
   - Companies involved in weapons-related activities or providing dedicated equipment or services therefor (see also 3.1 a).
   - Indicative sector/industry and activity classifications (See Annex)

b) **Governance criteria**
   - See 3.1 b)

c) **Business criteria**
   - The company shall have no activity of manufacturing or of manufacturing tailor-made components, using, repairing, putting up for sale, selling, distributing, importing or exporting, storing or transporting controversial or indiscriminate weapons such as: anti-personnel mines, submunitions, inert ammunition and armour containing depleted uranium or any other industrial uranium, weapons containing white phosphorus, biological, chemical or nuclear weapons.
   - The company shall derive less than 5% of its revenues from the production of (other) weapons or tailor-made components thereof.

d) **Phase-out margin**
   - Companies not compliant with these criteria are not eligible for the phase-out margin.
3.4 Coal Criteria

a) **Scope**
   - Companies involved in the exploration, mining, extraction, transportation, distribution or refining of thermal coal or providing dedicated equipment or services therefor (see also 3.1 a).
   - Indicative sector/industry and activity classifications (See Annex)

b) **Governance criteria**
   - See 3.1 b)

c) **Business criteria**
   - The company’s absolute production of or capacity for thermal coal-related products/services shall not be increasing.
   - The company shall meet at least one of the following criteria:
     - Have a SBTi\(^5\) target set at well-below 2°C or 1.5°C, or have a SBTi ‘Business Ambition for 1.5°C’ commitment
     - Derive less than 5% of its revenues from thermal coal-related activities
     - Have less than 10% of CapEx dedicated to thermal coal-related activities and not with the objective of increasing revenue
     - Have more than 50% of CapEx dedicated to contributing activities

d) **Phase-out margin**
   - Companies not compliant with these criteria are not eligible for the phase-out margin.

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\(^5\) See [https://sciencebasedtargets.org/companies-taking-action#table](https://sciencebasedtargets.org/companies-taking-action#table)
3.5 Unconventional oil & gas

Criteria

a) **Scope**
   - Companies involved in the exploration or extraction of unconventional oil and gas or providing dedicated equipment or services therefor (see also 3.1 a).
     This includes: the extraction of tar/oil sands, shale oil, shale gas and Arctic drilling.
   - Indicative sector/industry and activity classifications (See Annex)

b) **Governance criteria**
   - See 3.1 b)

c) **Business criteria**
   - The company’s absolute production of or capacity for unconventional oil and gas-related products/services shall not be increasing.
   - The company shall meet at least one of the following criteria:
     - Have a SBTi target set at well-below 2°C or 1.5°C, or have a SBTi ‘Business Ambition for 1.5°C’ commitment
     - Derive less than 5% of its revenues from unconventional oil and gas-related activities
     - Have more than 50% of CapEx dedicated to contributing activities

d) **Phase-out margin**
   - Companies not compliant with these criteria are not eligible for the phase-out margin.
3.6 Conventional oil & gas

Criteria

a) Scope
   • Companies involved in the exploration, extraction, refining and transportation of oil and gas, or providing dedicated equipment or services thereof (see also 3.1 a).
   • Indicative sector/industry and activity classifications (See Annex)

b) Governance criteria
   • See 3.1 b)

c) Business criteria
   • The company shall meet at least one of the following criteria:
     o Have a SBTi target set at well-below 2°C or 1.5°C, or have a SBTi ‘Business Ambition for 1.5°C’ commitment
     o Derive less than 5% of its revenues from oil and gas-related activities
     o Have less than 15% of CapEx dedicated to oil and gas-related activities and not with the objective of increasing revenue
     o Have more than 15% of CapEx dedicated to contributing activities

d) Phase-out margin
   • Companies not compliant with the business criteria are eligible for the phase-out margin.
3.7 Power generation

Criteria

a) **Scope**
   - Companies involved in the generation of power/heat from non-renewable energy sources, or providing dedicated equipment or services therefor (see also 3.1 a).
   - Indicative sector/industry and activity classifications (see Annex).

b) **Governance criteria**
   - See 3.1 b).

c) **Business criteria**
   - The company’s absolute production of or capacity for coal-based or nuclear-based energy-related products/services shall not be structurally increasing.
   - The company’s absolute production of or capacity for contributing products/services shall be increasing.
   - The company shall meet at least one of the following criteria:
     - Have a SBTi target set at well-below 2°C or 1.5°C, or have a SBTi ‘Business Ambition for 1.5°C’ commitment
     - Derive more than 50% of its revenues from contributing activities
     - Have more than 50% of CapEx dedicated to contributing activities

d) **Phase-out margin**
   - Companies not compliant with the business criteria are eligible for the phase-out margin.

**Grandfathering**
- Until 2025, electricity utilities with a carbon intensity lower than the annual thresholds below and that are not structurally increasing coal- or nuclear-based power generation capacity, are eligible:

<table>
<thead>
<tr>
<th>Year</th>
<th>Max. gCO₂/kWh</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>429</td>
</tr>
<tr>
<td>2020</td>
<td>408</td>
</tr>
<tr>
<td>2021</td>
<td>393</td>
</tr>
<tr>
<td>2022</td>
<td>374</td>
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<td>354</td>
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<tr>
<td>2024</td>
<td>335</td>
</tr>
<tr>
<td>2025</td>
<td>345</td>
</tr>
</tbody>
</table>
3.8 Financials

Criteria

Scope
- Financial institutions (FIs) when acting as issuer of a fixed income instrument funding a QS compliant structured product (2.6 1 3rd bullet) and that is not a use-of-proceeds instrument (see 4.3).

Governance criteria & Business criteria
- The financial institution shall meet a number of cumulative normative, comply or explain, and disclosure expectations based on:
  1. External ESG ratings
  2. Current operations
  3. ESG due diligence process and financing policies
  4. Strategies on ESG themes
  5. Adherence to (international) frameworks and standards, involvement in sectoral initiatives
  6. Disclosures and reporting

Note that many of the requirements overlap and will be fulfilled simultaneously.

<table>
<thead>
<tr>
<th>Restrictive criteria</th>
<th>Strategy &amp; Policies</th>
<th>Disclosure &amp; reporting</th>
</tr>
</thead>
<tbody>
<tr>
<td>- ESG rating in top 50% (2 sources)</td>
<td>- ESG risk &amp; sector policies</td>
<td>- Sustainable finance activities</td>
</tr>
<tr>
<td>- No new loans/underwriting to coal sector &gt; 2030 maturity</td>
<td>- Climate alignment strategy</td>
<td>- Share renewables in energy credit/loan portfolio</td>
</tr>
<tr>
<td>Comply or Explain (mandatory +500 empl.)</td>
<td></td>
<td>- Amount loans/underwriting to fossil fuel sector (except use of proceeds)</td>
</tr>
<tr>
<td>- UN PRB/PRI/PSI signatory</td>
<td></td>
<td>- Own GHG emissions (scope 1, 2, (3))</td>
</tr>
<tr>
<td>- OECD Guidelines financial sector</td>
<td></td>
<td>- Portfolio GHG intensity (credit/investment portfolio)</td>
</tr>
<tr>
<td>- TCFD recommendations</td>
<td></td>
<td>- CSR report</td>
</tr>
<tr>
<td>- NFRD Climate reporting</td>
<td></td>
<td>- NFRD, SFDR and Taxonomy mandatory disclosures</td>
</tr>
</tbody>
</table>

1. External ESG ratings
   a. The overall ESG rating of the FI, as calculated by 2 rating agencies, recognized by the CLA, rank in the top 50th percentile of its sector. FIs without external ratings or with less than 500 employees can provide the CLA with an equivalent assessment.
   b. The name of the rating agencies, the actual percentiles and the dates^6 of calculation shall be disclosed.

^6 Max. 1 year old
2. Current operations
   a. The FI shall report on its sustainable finance activities7:
      - ‘Environmental’ finance: Financing8 of activities contributing to the EU environmental objectives9. The FI shall disclose how and to what extent its activities are associated with economic activities that qualify as ‘environmentally sustainable’10
      - ‘Social’ finance: Financing of healthcare, education and other activities contributing to social objectives
      - ‘Sustainable’ products (savings, investment, insurance) distributed + the share of these products in the total
   b. The FI shall not grant (new) general unqualified corporate loans to companies, and not underwrite (new) unqualified general bonds from companies in the ‘coal sector’11 that are not QS compliant (see 3.4), with a maturity later than 2030 for European and OECD countries and 2040 for non-OECD countries. Dedicated ‘green’ loans12 and ‘green’ use-of-proceeds bonds are allowed.
   c. The FI shall disclose the share of its total credit/loan portfolio that consists of general corporate loans to companies, and underwritten general bonds from companies in the ‘fossil energy sector’13.
   d. The FI shall disclose the share of its total energy credit/loan portfolio financing renewable energy.
   e. The FI shall disclose scope 1 and scope 2 greenhouse gas emissions of its operations. Disclosure of scope 3 greenhouse gas emissions on a best effort basis is encouraged.

3. ESG due diligence process and financing policies14
   a. The FI shall implement the OECD Guidelines for Multinational Enterprises - Responsible business conduct in the financial sector15, as far as applicable. Mandatory if +500 employees else, if not, the FI shall explain why.
      - Due Diligence for Responsible Corporate Lending and Securities Underwriting16
      - The Responsible Business Conduct for Institutional Investors17
   b. The FI shall formalise and publish policies on how it considers and monitors the following in its financing decisions:
      - Human rights

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7 In million EUR + annual growth
8 E.g. via loans (corporate and mortgages), bonds, project finance, insurance
9 See Taxonomy Regulation art. 9: (a) climate change mitigation; (b) climate change adaptation; (c) the sustainable use and protection of water and marine resources; (d) the transition to a circular economy; (e) pollution prevention and control; (f) the protection and restoration of biodiversity and ecosystems.
10 See Taxonomy Regulation art. 8 §1
11 ISIC (Rev. 4)/NACE (Rev. 2) codes 05, 06, 09.1 and 19; GICS 1010 + Companies listed on the Global Coal Exit List (https://coalexit.org/).
12 See LMA Green Loan Principles https://www.lma.eu.com/sustainable-lending
13 See definition ‘fossil fuel sectors’ in SFDR Final RTS art 1 (2): sectors of the economy which produce, process, store or use fossil fuels as defined in Article 2(62) of Regulation (EU) 2018/1999 = ‘fossil fuel’ means non-renewable carbon-based energy sources such as solid fuels, natural gas and oil.
14 See also SFDR Final draft RTS Annex I - Principal adverse sustainability impacts statement
• Labour rights  
• Biodiversity  
• Water  
• Waste  
• Corruption  
• Taxation  
• Diversity and equality (gender and other)  
• Fair and sustainable remuneration  

3. The FI shall formalise and publish policies on financing companies active in the following sectors:
• Weapons industry  
• Tobacco industry  
• Coal industry  
• Oil & gas energy industry  
• Power generation industry

4. Strategies on ESG themes
   a. The FI shall formalise and publish a strategy about its role in tackling climate change. This strategy will include actions aimed at avoiding significant harm to as well as significantly contributing to the objectives of climate change mitigation and climate change adaptation.

5. Adherence to (international) frameworks and standards, involvement in sectoral initiatives
   a. The FI shall be a signatory of the UNEP FI Principles for Responsible Banking18 (for banks), UNEP FI Principles for Sustainable Insurance19 (for insurance companies) or UNEP FI Principles for Responsible Investing20 (for asset managers), as far as applicable. Mandatory if +500 employees else, if not, the FI shall explain why.
   b. The FI shall list other initiatives it is involved in and standards it follows21.

6. Disclosures and reporting
   a. The FI shall publish a CSR or integrated report, preferably using an accepted framework (e.g. GRI).
   b. The FI shall disclose if and to what degree it implements the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Mandatory if +500 employees else, if not, the FI shall explain why.

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18 https://www.unepfi.org/banking/bankingprinciples/
19 https://www.unepfi.org/psi/
20 https://www.unpri.org/
21 E.g. Equator Principles, IFC Performance standards, PACTA, PCAF, Collective Commitment to Climate Action, Climate Action 100+, Tobacco Free Portfolios, Tobacco-Free Finance Pledge, Wolfsberg Principles, Finance for Biodiversity Pledge, Febelfin Gender Diversity in Finance charter, etc.
c. The FI shall comply with the legal requirements of the Non-Financial Reporting Directive (2014/95/EU), as far as applicable.


e. The FI shall comply with the legal requirements of Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (‘Disclosure Regulation’), esp. the entity-level disclosures, as far as applicable.

f. The FI shall comply with the legal requirements of Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment (‘Taxonomy Regulation’), as far as applicable.

**Signatory**

Compliance with the above criteria, except for the ESG ratings criterium, is a condition for financial institutions to become Signatory to the Towards Sustainability Initiative.
4. Clarifications to existing QS requirements

4.1 Cash or cash equivalents, crypto currencies

Criteria
Cash positions do not have to be evaluated if their only purpose is technical or for the hedging of risks.
If held as a source of return, the depository bank shall comply with the QS criteria for financial institutions (see 3.8).

Crypto currencies (or assets) are not allowed unless within a recognized regulatory framework. Also, given the huge energy use of Proof of Work mining (e.g. Bitcoin, Ethereum), this is considered incompatible with a sustainable product.

4.2 Derivatives

Criteria
The use of derivatives cannot be at odds with the sustainable character of the product. This means that the potential (indirect) negative impact on sustainability factors of using/investing in derivatives shall be taken into account.

Derivatives that are solely used as a technical tool in the context of efficient portfolio management or for hedging purposes with regard to currency risk, duration risk, market risk or/and sensitivity to changes in interest rate structures can be excluded from ESG evaluation.

If used as a source of return, the issuer of the underlying assets shall be evaluated. When the underlying of the derivative is an index, the index shall be QS compliant (see 4.7).
However, derivatives on the product’s reference (sub)benchmark (or an equivalent broad market benchmark) are temporary allowed to a maximum of 10% of the portfolio.
Replacing a direct investment risk with a derivative investment in that risk does not take away the need for ESG due diligence of the direct investment.

The product manager is encouraged to perform ESG due diligence on the counterparties.

Derivatives on agricultural commodities for speculative reasons are not allowed.

The manager shall describe the nature of the derivatives used, the average proportion of the portfolio concerned, the ESG analysis made of the underlying and counterparties (when applicable), the strategy (market hedging, liquidity management, additional performance, etc.) and whether the derivative has an effect on the ESG performance of the portfolio.

4.3 Use-of-Proceeds instruments

Criteria
Use-of-proceeds instruments shall meet the following criteria:

a) Use-of-proceeds instruments shall comply with an appropriate framework (e.g. ICMA/CBI/EU GBS/LMA) and be subject to independent external review. For some specific issuers, supranational institutions and agencies, this might not be possible. In that case, elaborate on equivalence (see c.).
b) Issuers and beneficiaries of use-of-proceeds instruments shall be subject to the ESG due diligence process of the product manager. The environmental, social and governance aspects of the
financed programs/projects shall be taken into account when investing in use-of-proceeds instruments.

c) The evaluation of use-of-proceeds instruments issued by financial institutions, governments and supra-nationals is left to the discretion of the product manager.

Use-of-proceeds instruments issued by companies that fail the business criteria (c) of 3.4-3.7, can be eligible.

While all types of bonds issued by QS compliant issuers are in any case eligible, if the product manager promotes investments in use-of-proceeds bonds as a strategy, all use-of-proceeds instruments in the portfolio shall comply with the above criteria.

4.4 Short selling
Criteria
The QS, as a principle, does not a priory exclude the use of specific investment or portfolio management techniques, as long as the use of the technique is not contrary to the ESG characteristics or objectives of the product and does not benefit unsustainable issuers.

- Short positions shall be used with the objective to trade on ESG concerns over e.g. corporate governance, environmental issues, or alleged human rights abuses, and aimed at exposing failings of issuers and bolstering market transparency for investors.
- The decision to go short should also be driven by ESG considerations and not solely with the aim to generate additional performance.
- The product manager shall be transparent about the objectives and motives of short selling and have in place a monitoring system to detect potential negative impacts of using this technique on the ESG quality of the product.

The use of short selling will be indicated on the Sustainability ID.

4.5 Real Estate products
Criteria
Real estate products shall have in place an appropriate ESG due diligence and evaluate their real estate investments using an appropriate framework that determines contribution to ESG objectives and avoidance of negative ESG impact.

This framework shall at least take into account:
- Energy efficiency
- Water use
- Material use, recycling, waste and circular economy
- Location, e.g. mobility score

Real estate and infrastructure investments shall not be linked to the business activities of issuers that are not compliant with the QS. Next to environmental factors, also social and governance factors should be taken into account where relevant.
4.6 Index-based products

Criteria

Index-based products (e.g. ETFs) are compliant with the QS when the underlying index is QS compliant.

Investing in index-based products based on broad market indices for technical reasons (hedging) is considered ESG neutral to a maximum of 10% of the portfolio.

4.7 Indices

Criteria

To be considered QS compliant, the construction of the index shall comply with one of the following:

- The index construction rules integrate the QS requirements on sustainability strategies (see 1.1), except for corporate engagement.
- The index is an EU Paris-Aligned Benchmark

If rebalancing is required to have an index become compliant with the QS, the rebalancing shall at the latest be effective 3 months after the approval.

Applications for the labelling of indices shall be made by the index provider/manufacturer (and not only by the manager of a product that uses the index).

Applications for the approval of indices (without labelling at the index level) for use by a product, can be requested by the product manager.

4.8 Prospectus or equivalent

Criteria

A product applying for the Towards Sustainability label must either be a product promoting environmental or social characteristics (in the sense of SFDR art. 8) or a product with sustainable investment objectives (in the sense of SFDR art. 9), or analogous if the product is not in scope of the SFDR. This information will be mentioned on the Sustainability ID.

The description of the ESG characteristics and/or objectives of the product in pre-contractual disclosures shall be compliant with the requirements of the SFDR, or analogous if the product is not in scope of the SFDR.

The prospectus shall specify that all dimensions of ESG, i.e. environmental, social and governance, are taken into account in the investment strategy.

Adapting official documents and approval by regulators can take considerable time. To apply for the label, the intention to modify these documents and a concrete timing can suffice.

A prospectus that is still in the process of regulatory approval is not considered a blocking issue for awarding the label. However, the final draft prospectus must be compliant and available for verification.

4.9 Disclosure of policies

Criteria

Mandatory issues

The product manager or distributor shall publish on its website, preferably on a dedicated webpage:
a) A detailed description of the implementation of the sustainability strategies used by the product (See 1.1)
b) A statement about how climate change and Paris alignment is taken into account
c) Policies about sectors for which the QS has specific requirements (See 3):
   1. Tobacco
   2. Weapons
   3. Coal
   4. Unconventional oil & gas
   5. Conventional oil & gas
   6. Power generation, incl. nuclear energy
d) Policies about other key ESG issues:
   7. Biodiversity (e.g. deforestation, palm oil)
   8. Water use
   9. Pollution & waste (e.g. plastics)
   10. Gender & diversity
   11. Taxation
   12. Oppressive regimes (State and company level)
   13. Death penalty
   14. Forward contracts on agricultural commodities
e) When not already covered in a) to d), policies about other issues of principle adverse impact about which disclosure is required by the SFDR RTS (Annex I table 1)
f) Policies about other ESG issues that are material to the product.

When issues under b), c), d) or e) are not relevant to a product, this shall be formally stated and explained.

When the investment policy of a product explicitly excludes investing in a sector listed in c), a policy on that sector is not required.

Optional issues
The product manager or distributor is invited to publish on its website, preferably on a dedicated webpage:

   a) When not already covered, policies about other issues of principle adverse impact about which disclosure is encouraged by the SFDR RTS (Annex I tables 2 & 3)
   b) Policies about other issues commonly addressed in values-based investing:
      15. Alcohol
      16. Gambling
      17. Adult entertainment
      18. Cannabis
      19. Animal testing
      20. Genetically modified organisms (GMOs)
      21. etc.

Scope of policies
The policies shall at least be applicable to the labelled product. The manager can also refer to policies applicable on the level of a range of products or on the level of the product manager.
**Format of policies**

The detail of the policies should be relative to the materiality of the issues for the product.

Policies about issues for which the QS sets detailed requirements or expectations, shall clearly reflect these requirements or expectations. For other key ESG issues, a policy could range from a very restrictive approach to a statement that an issue is currently not part of the ESG analysis.

A policy document shall describe the policy on the issue and by which processes and criteria the issue is evaluated, e.g.: a description of the metrics, thresholds, exemptions and the sources used in the evaluation. Reference can be made to the general ESG due diligence process, but a useful level of detail on the specific issue should be provided.

The different issues can be covered in separate policy documents or can be bundled in one or more documents.

**4.10 Disclosure of indicators**

**Criteria**
The product manager shall provide to the CLA, on the product/portfolio level:

- GHG emissions (absolute GHG)
- Carbon footprint (GHG per million EUR invested)
- GHG intensity of investee companies (GHG per million EUR revenue) and of sovereigns (GHG per million EUR GDP)
- Fossil fuel sector exposure, split in (fossil) energy sector exposure and (fossil) electricity utilities sector exposure
- SFDR portfolio info:
  - proportion of ‘sustainable investments’ as defined in Article 2, point (17)
  - proportion of the investments of the financial product used to attain the environmental or social characteristics promoted
  - remaining proportion of investments
- Taxonomy info: proportion invested in in environmentally sustainable investments as defined in Article 2, point (1)
- Portfolio reduction rate (see 1.1)
- % of underlying funds (by AUM) that does not have the Towards Sustainability label or another recognized label (see 2.7)
- % of States (by number and AUM) invested in by the product (via sovereign debt), that are not compliant with 2.1

As of 30/12/2022, the product manager is encouraged to provide disclosure on all other product-level principle adverse impact indicators listed in the SFDR.

The CLA will integrate the indicators in the Sustainability ID.
Annex: Harmful and contributing activities

Harmful activities and related sectors/industries

Sector/industry classifications are provided for illustrative purposes and do no limit the scope of the QS criteria.

Harmful activities about which the QS requires specific sector policies (see 3.):

- **Tobacco**: GICS 30203010; ICB 451030; TRBC 54102030; NACE 01.15, 12, 46.35
- **Aerospace & Defence / Weapons**: GICS 201010; ICB 502010; TRBC 521010; NACE 25.4, 30.4
- **Energy**: GICS 101010, 101020; ICB 601010; TRBC 5010; NACE 06, 09.1, 19, 35.21
  - Coal: GICS 10102050; ICB 60101040; TRBC 501010; NACE 05, 19
  - Unconventional oil & gas: TRBC 5010202015, 5010301015
- **Utilities (Power generation)**: GICS 551010, 551020, 551030, 55105010; ICB 651010; TRBC 5910101012, 5910101013, 5910102011, 5910102013, 59102010; NACE 35.1
  - Nuclear: TRBC 5210204016, 5220102022, 5910101013, 5910102013; NACE 24.46

This list does not limit other material harmful activities to be considered in the ESG due diligence process.

Contributing activities

- **Economic activities included in the EU Taxonomy**
- **Other economic activities (not yet in the EU Taxonomy)** that contribute to environmental or social objectives.
  - The activities shall clearly and concretely contribute to any of the EU environmental objectives or the Sustainable Development Goals (SDGs).
  - The product manager shall disclose the sectors/activities it considers as contributing and describe how these contribute to the selected objectives or goals.