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Definition of a sustainable investment
Sienna IM – Private Credit

The European Commission proposes, in Article 2 (17) of the EU Regulation 2019/2088, a definition of a sustainable investment within the meaning of the SFDR regulation.

"*sustainable investment: an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance.*“

It is up to asset managers to apply this definition to determine the proportion of their investments that are sustainable.

The definition is broad and leaves room for interpretation. It does, however, specify that sustainable investments must:

- Contribute to an environmental or social objective, as measured by indicators
- Do not significantly harm ("DNSH") other sustainable objectives
- Follow good governance practices

Sienna's Private Credit expertise approach to evaluating each of the three areas is detailed in the three sections below.

1. Contribution to a sustainable goal

Sienna IM – Private Credit structures the assessment of its contribution to a sustainable goal based on the Sustainable Development Goals (SDGs) and corresponding targets: each "sustainable investment" as defined by Sienna's Private Credit expertise pursues one of the 17 SDGs, further divided into 169 targets.

Sienna IM – Private Credit considers, as recommended by the European Commission, that a company's contribution to a Sustainable Development Goal (SDG) can be achieved in three ways:

- The company is active in a sector that directly contributes to an SDG (for example, a renewable energy producer or an organization promoting professional integration)
- The company has implemented practices that enable it to contribute to an SDG (for example, a factory modernizing its equipment to reduce its carbon footprint, a concrete action plan to reduce the gender pay gap)
- Companies that have made commitments through initiatives, certifications or labels and have an improvement plan (for example, companies that have signed a GHG reduction plan validated by SBTi, FSC, B Corp, ISO 14001)

For each asset, the contribution to an SDG is analysed at the time of the investment and on an annual basis.

2. Do Not Significantly Harm analysis procedure

Sienna IM - Private Credit considers PAIs (Principal Adverse Impacts) in its investment opportunity analysis. The "DNSH" approach takes into account 7 PAI indicators that it considers the most important. These indicators are detailed below. Companies that have provided the response indicated below to any of the PAIs 1, 4, 7, 8, 9, 11, 14 are considered to have a negative impact on sustainable objectives and are not eligible for "sustainable investment":

- **Greenhouse gas emissions (GHG) intensity (scope 1 and 2, PAI #3)**: the company has a carbon intensity (tonnes of CO_2 equivalent/million euros of turnover) above the threshold of **255 t CO_2 eq/million euros of turnover** and has not implemented any measures to reduce emissions in line with the 1.5°C trajectory (subject to validation by a third party).

  Sienna IM - Private Credit has adopted an approach based on sector benchmarks to set a carbon intensity ceiling based on the MSCI Europe index, which covers a wide range of European companies. The five sectors with the highest GHG emissions have been identified within this index, based on GHG emissions (scope 1 and 2). The representative baseline has been determined based on the median carbon intensity of these sectors. This threshold will serve as the maximum acceptable value for the evaluation of the financed companies and is updated annually (based on the scope covered by Sustanalytics). Any company with a higher carbon intensity will be subject to an in-depth analysis to assess its decarbonization trajectory and its commitments to reduce emissions.

  Note: Sienna IM - Private Credit may use parametric models provided by third parties to measure borrowers' carbon intensity where borrowers are not equipped to do so (most of the borrowers involved in Sienna IM - Private Credit's financing are not required to do so at this time).

- **Activity related to the fossil fuel sector (PAI #4):** Yes
- **Controversial Weapons Exposed Activity (PAI #14):** Yes
- **Pollutant waste emissions (PAI #9):** if manufacturing activity, and emissions > 1 tonne/year, and the organization has not implemented a waste reduction policy, resulting in measurable and significant results
- **Emissions to water (PAI #8)**: if manufacturing activity, and emissions > 1 tonne/year, and the organization does not have a water emission reduction policy in place to gradually reduce pollutant emissions to water to 0
- **Biodiversity impact (PAI #7)**: activity of the organization affecting biodiversity-sensitive areas
- **Violations of the Global Compact and the OECD Guidelines for Multinational Enterprises (PAI #10)**: Yes

The DNSH analysis is completed by an analysis of the controversies to which the beneficiary organization is or may have been exposed. The analysis of controversies is part of the systematic ESG analysis of the beneficiary organizations.

3. Governance practices assessment policy

Our policy of assessing good governance practices focuses on the organizations that receive funding.

The policy of assessing good governance practices is systematic for all transactions carried out within the framework of funds that promote environmental and social characteristics, as long as the issuer of the **debt securities is an organization with more than 50 employees**, organized in corporate form (SAS, SA, SARL or European equivalent).

It covers, as recommended in Article 28 of the technical standards published in the Delegated Act (EU) 2022/1288, the following elements:

- **Sound management structures:** Sienna IM - Private Credit ensures that the issuer has governance bodies (board of directors, executive board, management committee, etc.) or an organization consistent with its size and jurisdiction. Sienna IM - Private Credit encourages the integration of independent members in governance bodies. For companies with no independent members at the time of investment, a review of the need to strengthen governance may be carried out depending on the size and maturity of the company.
- **Employee relations:** Sienna IM - Private Credit assesses the quality of employee relations by analysing controversies to identify potential social tensions (such as strikes).
- **Employee compensation:** Sienna IM - Private Credit assesses the quality of the issuer's employee compensation practices, focusing in particular on the existence of a compensation policy, a profit-sharing agreement, the signing of at least one NAO agreement in the last three years (French issuers) and the existence of an employee share ownership mechanism. In the absence of all these elements, the issuer's practices in terms of employee compensation are considered weak.
- **Tax liabilities:** Sienna IM - Private Credit is aware of any pending tax disputes involving the beneficiary company. In the event that tax disputes are pending, an assessment of the materiality of the disputes is performed.