SFDR APPLICATION

THE SFDR FRAMEWORK

The European Commission has established through the regulation (EU 2019/2088) called the Sustainable Finance Disclosure Regulation (SFDR), which entered into force on 10 March 2021, a regulatory framework clarifying the intentions in terms of sustainable development of funds.

The aim is to convey to future investors the fund's ESG dimension, through standardised and regulated communication in Europe.

Below is the overall framework induced by SFDR, and in particular the definitions in Articles 6, 8 and 9:

	ARTICLE 6	ARTICLE 8	ARTICLE 9

SFDR DEFINITION	- Funds that **do not promote environmental or social characteristics**
	- Funds that **do not have a sustainable investment objective**
		- Funds that **promote environmental or social characteristics** (or a combination of these characteristics)
		- Funds with **no sustainable investment objectives**
			- Funds with **a sustainable investment objective** : an economic activity that contributes to an environmental and/or social objective and whose :
			  - The investments **do not cause significant harm** to any other environmental and social objective
			  - The invested companies **practice good governance**

DEFINITION – REAL ESTATE SECTOR	- « Classic » financial product	- Without a **binding objective** - **Monitoring** of an indicator, **no need to manage it**	- To have a **positive impact** on external social and environmental factors - Committed objectives --> the fund's principal approach - **Monitoring** and **managing** indicators
ADDITIONAL TRANSPARENCY	**Transparency :** - On the **inclusion of sustainability risks** (Article 6)		
		Transparency : - On the promotion of environmental or social characteristics and sustainable investments on the **website** (Article 10) - Information on investments in the annexes to the **pre-contractual documents** - The promotion of environmental or social characteristics and sustainable investments in the **periodic reports** (Article 11)	

Source - Weefin

SFDR CONCEPTS

Principal Adverse Impacts

An **adverse impact** is an impact of an investment decision on sustainability factors.

The SFDR regulation defines the Principal Adverse Impacts (PAI) for the real estate sector as:

- Exposure to fossil fuels
- Exposure to non-energy-efficient real estate assets
- Additional indicators: Scope 1, 2 and 3 GHG emissions or Artificialisation of soils

Exposure to fossil fuels by real estate assets:

Primonial REIM's real estate investments focus on the following asset classes: health, office, residential, commercial, hospitality and logistics. None of Primonial REIM's real estate investments are directly involved in the extraction, storage or transportation of fossil energy.

It is worth emphasising that the exposure to fossil fuels to which the regulator refers does not concern the heating systems used (gas boiler type) at the asset level.

Exposure to non-energy-efficient real estate assets:

In the context of the integration of the principal adverse impacts at the level of products classified Articles 8 and 9 (Article 7) as defined in Regulation (EU) 2019/2088 SFDR, **an inefficient asset is defined as an asset whose EPC** (Energy Performance Certificate) score **is less than or equal to C.**

Data collection is often associated with the reliability of EPCs. Primonial REIM is engaged in collecting energy performance certificates in order to report/communicate on the share of its inefficient assets.

Choice of additional indicators:

1. Carbon emissions – Scope 1, 2 and 3

Primonial REIM is committed to aligning assets over 1,000 m² on a 1.5°C by 2050 trajectory, in application of the Paris Agreements. The CO_2 emissions of scopes 1, 2 and 3 are systematically monitored with the aim of gradually reducing them.

Scopes 1, 2 and 3 on the Primonial REIM scale are defined as:

- Scope 1: Direct building emissions (gas, fuel, refrigerant leaks)
- Scope 2: Indirect building emissions (electricity, urban heating and cooling)
- Scope 3 emissions due to manufacturing and transport of raw materials in the development and heavy restructuring phase.

Primonial REIM therefore undertakes, in agreement with the RTS of Annex 1 to the SFDR, to publish annually its CO_2 emissions for scopes 1, 2 and 3.

Do Not cause Significant Harm-Principle

To classify a financial product Article 9 within the meaning of SFDR Regulation 2019/2088, it is necessary to pursue a sustainable investment objective, the definition of which is given in Article 2(17) of the aforementioned Regulation:

“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.”

The Regulatory Technical Standards (RTS) from April 2022 indicate that financial products with sustainable investments must include information on how they have complied with the principle of "not causing significant harm" with respect to the Principal Adverse Impact Indicators (PAI) in Annex I to the RTS. PAIs are therefore a means of demonstrating how the fund does not cause significant harm to sustainable investment objectives.

In this sense, the RTS, which refer to the notion of not causing material harm, require financial products to explain how PAIs are taken into account. Reaching any threshold on PAIs at a time t (x% maximum of low energy efficiency real estate assets) would be inconsistent with the "best-in progress" objective of limiting global warming. The "best-in-progress" approach aims to improve these real estate assets, qualified as inefficient, over time in order to align them with the objectives set by the Paris Agreements.

The SFDR DNSH (do not significant harm) for Primonial REIM Article 9 funds is based on taking into account the principal adverse impacts at the product level by seeking to avoid or even reduce these PAIs over time without imposing a threshold level to be achieved.

Alignment with the EU-Taxonomy Regulation (EU) 2019/2088

The RTS provide for the obligation for Article 8 products with a share of sustainable investment and Article 9 products to calculate the share of the product's underlying investments in sustainable activities aligned with the European Taxonomy Regulation (EU) 2019/2088. This "sustainable share" must be presented in graphic form in the pre-contractual documentation and the periodic report.

According to the current definitions of the European taxonomy, real estate asset management companies can only be aligned to the "Climate Change Mitigation" objective because the "Climate Change Mitigation" DNSH associated with the "Climate Change Adaptation" objective has not been defined for the sector.

Buildings aligned with the Climate Change Mitigation objective as defined by the European taxonomy can be distinguished on the basis of the following criteria:

- For buildings built before 2021, the indicator is based on primary energy consumption. The top 15% of the local market, by type of building, must define the minimum threshold.
- Buildings demonstrate high energy performance via an EPC A

- Buildings built after 2021 must align with the criteria established for the Construction of New Buildings activity in order to be considered "green".

The funds managed by Primonial REIM are composed of recently built assets, but also many assets that make up the existing European building stock. While the EPC A level is achievable for a recently constructed asset, it is difficult to envisage on an older asset or involves CapEx whose result will only be visible in the long term. Primonial REIM is actively working to improve the assets so that they are, among other things, aligned with the 1.5°C trajectory. Our ESG strategy is based on the conviction that as an investor and asset manager, Primonial REIM has a responsibility to improve the stock of existing assets over time, even if they are not the best performers, in ESG terms, on the market. In addition, the benchmark used to identify the top 15% of the European market is currently being developed by the market players.

Thus, the **sustainable investments of the Article 8 and 9 Primonial REIM funds can be categorised as aligned or not aligned with the taxonomy**. Once the fund has set itself an improvement target for assets held, as well as demanding criteria for assets under acquisition, it contributes to improving Primonial REIM's impact on the environment and society. Primonial REIM relies on a "best-in-progress" approach for the majority of assets managed, which implies continuous improvement over an asset base that has to face major challenges and investments.

A RANGE OF RESPONSIBLE FUNDS

As a responsible investor, the Primonial REIM undertakes to follow one or more environmental or social characteristics across all of its open funds. **All open funds are therefore categorised, at least, as Article 8** within the meaning of the SFDR. In addition, funds with quantitative objectives and a monitoring process are classified as Article 9 within the meaning of the SFDR.

Systematisation of Article 8

Primonial REIM intends to be able to classify newly created funds at least as Article 8, and to move the categorisation of all marketed funds towards Article 8.

In this perspective, the Primonial REIM prerequisites for an Article 8 classification on a fund in creation or already existing are as follows:

- **For any direct acquisition of an asset** within the open-end fund range, the following acquisition process applies, as described in the ESG Acquisition Process:

  - Completion of an **ESG scoring grid**
  - Assessment of exposure to **physical risks**: 8 risks projected at 50 years (IPCC source), and risk scales and threshold of proven risks
  - Positioning on the **1.5°C carbon trajectory** according to the CRREM methodology.

  These analyses are systematically presented to the management company's internal investment committee in order to fully take into account extra-financial points of attention in the final investment decision.

- **In the event that Primonial REIM is required to take an interest in an external fund (i.e. managed by a manager other than Primonial REIM), then a due diligence is carried out at the fund level**. This makes it possible to assess the consideration of the double materiality at the level of the fund being acquired (carbon and climate risks), but also biodiversity or governance issues.

Starting in 2023, an extra-financial report will be published each year on the evolution of performance in relation to the indicators chosen, the increase in the coverage rate, and the potential actions taken or to be taken. The extra-financial reports will in particular be aligned with the template of Annex IV of the RTS, and will document the evolution of sustainable investments within the existing funds, the consideration of the main negative impacts, and the alignment with the taxonomy.

Contribution to sustainable finance (Article 9)

Although all Primonial REIM open-ended funds and marketed closed-ended funds can achieve the Article 8 classification by applying the matrix described in the previous paragraph, only some of these are classified as Article 9 within the meaning of the SFDR. These funds must have a sustainable, significant investment objective.

In order to contribute to sustainable finance within the meaning of the SFDR, quantifiable targets must be added.

In addition to the prerequisites for the acquisition to be classified as Article 8, as described above, the Article 9 classification requires the following additional elements, both on a fund in creation or a fund already existing:

- **The setting, as a minimum, of an environmental or social objective,** quantitative and significantly binding on more than 90% of the fund's assets (in value or in securities). The development of a list of sustainability indicators used by the fund to measure the achievement of the sustainable investment objective. Description of the methods for obtaining these sustainability indicators;

- **Verification of the principle of DNSH (Do not Significantly Harm)**: for the real estate sector, the induced negative externalities of the asset are mainly the carbon emissions emitted during the construction and operation phase (scope 1, 2 and 3). Consequently, the principle of **not causing significant harm** amounts to systematically monitoring and reducing the main negative impacts produced by the assets which are carbon emissions.

- **Demonstration that the management company applies good governance practices** (see stakeholder engagement policy):
  - Regulate 100% of significant works, where feasible, (i.e. greater than €2 million in overall cost) on the portfolio's assets by means of a specific site charter incorporating ESG clauses (examples: treatment of site waste, respect for safety, fight against concealed work, etc.) ;
  - Aiming for inclusion ofan ESG Annex for 100% of the new leases or lease renewals signed with the tenants occupying the properties;
  - Incorporate an ESG clause into Property Management mandates, including a commitment:
    - to apply the management company's ESG procedures (ESG rating, due diligence, etc.) ;
    - to collect extra-financial data at the asset level (buildings, facility manager tenants, etc.) ;
    - to integrate ESG clauses into contracts with tier 2 service providers (maintenance, repairs, green spaces, etc.).

- **Demonstration, within the fund's annual extra-financial report, of the performance of sustainability indicators**, the alignment with taxonomy, and how the sustainable investment objective and indicators are monitored throughout the life cycle of the financial product, as well as the corresponding internal or external control mechanisms.