
DDV Sustainable Finance Code of Conduct

**PRODUCT AND TRANSPARENCY STANDARDS
FOR ISSUING SUSTAINABLE STRUCTURED PRODUCTS**

As at: March 2021

SUSTAINABLE FINANCE

  **Code of Conduct**



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PREAMBLE

- The Sustainable Finance Code of Conduct of the German Derivatives Association (Deutscher Derivate Verband, DDV) introduces the product group of sustainable structured products and positively distinguishes it from other structured products in accordance with the DDV product classification.¹ In addition, it contains transparency provisions for this product group.
- Pages 5 to 7 summarise the key statements of the Sustainable Finance Code of Conduct. This summary will also be available in a separate document, which will reference this Code of Conduct.
- The Sustainable Finance Code of Conduct has been formulated on the basis of current and expected future requirements and may be subject to further amendments based on these as well as changing national and international market conditions.²
- The Sustainable Finance Code of Conduct is based on the current “Typology for sustainable financial investments” (ESG Target Market) of the German Banking Industry Committee (Deutsche Kreditwirtschaft, DK), the German Federal Association for Investment and Asset Management (Bundesverband Investment und Asset Management, BVI) and the DDV.³

¹ Available at:
https://www.derivateverband.de/MediaLibrary/Document/Derivate-Liga_A3_2020_EN.pdf

² This includes, in particular, the implementation of Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088 (the Taxonomy Regulation) as a central element of the EU Sustainable Finance Agenda. The details of this were not known at the time of publication of the Code of Conduct.

³ LINK as soon as available.

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ENTRY INTO FORCE AND COMPLIANCE

- The Sustainable Finance Code of Conduct enters into force on the date of application of the amendments to MiFID II to take into account sustainability factors and preferences with regard to product governance requirements.
- The members of the DDV commit themselves to complying with this Sustainable Finance Code of Conduct when publically offering structured products to retail clients in Germany. Members of the DDV may publically state that they apply the provisions of the Sustainable Finance Code of Conduct to their sustainable structured products.
- Compliance with the Sustainable Finance Code of Conduct is to be regularly reviewed by the Sustainable Finance Code of Conduct Advisory Board.
- In the event of a breach of the Sustainable Finance Code of Conduct by a member of the DDV, the Board of Directors of the DDV shall take the decision as to appropriate measures, which could result in exclusion from the DDV.

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DDV SUSTAINABLE FINANCE CODE OF CONDUCT – SUMMARY

1. In offering sustainable structured products, the members of the German Derivatives Association (Deutscher Derivate Verband, DDV) place the protection of natural resources and universal human rights at the centre of their business activities. This applies, in particular, to the achievement of the objectives of the sustainable finance agenda of the European Union, which they support and promote with their sustainable structured products.
2. The members of the DDV undertake to label structured products as sustainable only if they meet comprehensible sustainability standards. When selecting such products, investors can rely on the fact that environmental and/or social criteria as well as issues of good corporate governance are taken into account.
3. The members of the DDV shall only label sustainable structured products as “ESG Products” if they themselves or the group to which they belong have achieved the status of a sustainable company with at least one recognised rating agency and consider the UN Principles for Responsible Banking¹ and/or the UN Global Compact and/or equivalent principles.

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¹ If the UN Principles for Responsible Banking are not relevant for an issuer and/or a specific financial instrument (e.g., because the issuer does not conduct traditional banking business), the UN Principles for Responsible Investment may be considered as an alternative.

DDV SUSTAINABLE FINANCE CODE OF CONDUCT – SUMMARY

4. The members of the DDV shall label sustainable structured products as “ESG Impact Products” only when the products pursue one or more measurable sustainability objectives, using or have been using an amount initially equal to at least the net issuance proceeds of the security to fund economic activities (within the scope of the issuer’s business activities) that contribute to these objectives. These may be green/environmental objectives, social objectives, or a combination of both. The issuers are responsible for the appropriate use-of-proceeds and are to publish regular reports on this.
5. When issuing sustainable structured products, the members of the DDV shall focus on investment products as defined in the DDV product classification.¹ Leverage products are not to be labelled as sustainable structured products. Investment products that benefit from a downward movement of the underlying asset are also to be excluded from being labelled as sustainable structured products.
6. The members of the DDV shall not label structured products as sustainable if they have companies as an underlying or reference issuer that exceed certain thresholds in their turnover from the production and/or distribution of military equipment or coal, or from tobacco production. Companies that produce or distribute controversial weapons are also to be excluded.

¹ Available at: https://www.derivateverband.de/MediaLibrary/Document/Derivate-Liga_A3_2020_EN.pdf

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7. The members of the DDV shall not label structured products as sustainable if they have agricultural commodities (soft commodities) as an underlying. Investors need to have the assurance that sustainable structured products do not encourage speculation with important foodstuffs.
8. The members of the DDV shall not label structured products as sustainable if they have companies as an underlying or reference issuer that commit serious violations of the UN Global Compact. Such companies, for example, violate the ban on child labour, do not respect human rights, or cause massive damage to the environment or natural resources.
9. The members of the DDV undertake to publish all relevant information on the sustainable structured products issued by them in an easily accessible manner on a website so that investors can inform themselves about the labelling of the products as sustainable.
10. This Sustainable Finance Code of Conduct shall be regularly reviewed and adapted to the applicable legal framework.

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DDV SUSTAINABLE FINANCE CODE OF CONDUCT – DETAILED DESCRIPTION

In detail, the DDV Sustainable Finance Code of Conduct for the public offer of sustainable structured products is organised according to the following topics:

-  Principal types of sustainable structured products
-  The underlying
-  The issuer
-  The exclusion of certain product groups
-  Transparency



PRINCIPAL TYPES OF SUSTAINABLE STRUCTURED PRODUCTS



In principle, members of the DDV distinguish between two principal types of products when issuing sustainable structured products: ESG Products and ESG Impact Products. For both types of sustainable structured products, a statement is to be made regarding the sustainability of the underlying asset as well as regarding the sustainability of the issuer (e.g., the issuing bank) or the group to which it belongs and/or the use-of-proceeds. In addition to these products, there are Basic Products, which are not classified as sustainable but take sustainability aspects into account:



1. ESG Products



Sustainable structured products in the “ESG Product” category generally pursue a broad approach to sustainability. The focus here is on ensuring a sufficiently large investment universe. If such a structured product is based on an ESG-compatible underlying (e.g., by embedding a derivative in an ESG-compatible underlying), the issuer pursues **a clear ESG strategy** when selecting the underlying. This means, in particular, that companies considered as underlyings stand out from other companies in a clearly defined way with regard to ESG factors. Furthermore, **certain underlying assets are excluded** (see “The underlying”). The **issuer** of ESG Products shall also meet **minimum criteria** with regard to its own sustainability (see “The issuer”).





PRINCIPAL TYPES OF SUSTAINABLE STRUCTURED PRODUCTS



2. ESG Impact Products

Sustainable structured products in the “ESG Impact Product” category are impact-focused bonds and thus pursue one or more measurable sustainability objectives.



As such, within the scope of the issuer’s business activities, economic activities that contribute to the defined sustainability objectives have been or will be funded with an amount that initially corresponds to at least the net issuance proceeds¹ of the sustainable structured product. The sustainability objectives can be, for example, green/environmental objectives, social objectives, or a combination of both.



For these products, a statement is to be made regarding the recognised standard² according to which a given product is issued. In addition, allocation and impact reports are to be published on a regular basis, enabling investors to track the achievement of the defined objectives.



For ESG Impact Products, only companies that do not commit any serious violations of the UN Global Compact may be selected as underlyings. This should be regarded as a minimum requirement for the selection of underlyings (see also “The underlying”).

¹ Net issuance proceeds are net of any costs, any allowances, or any expenses for derivative hedging transactions depending on the special product design.

² Recognised standards include the ICMA Green Bond Principles, the ICMA Social Bond Principles, the ICMA Sustainability Bond Guidelines, and, in future, the EU Green Bond Standard. Additional potential impact-related forms of funding could be included at a later date.



PRINCIPAL TYPES OF SUSTAINABLE STRUCTURED PRODUCTS



3. Basic Products

Structured products in the “Basic Product” category are not classified as sustainable products, but nevertheless take into account a number of fundamental sustainability aspects that also apply to ESG Products.

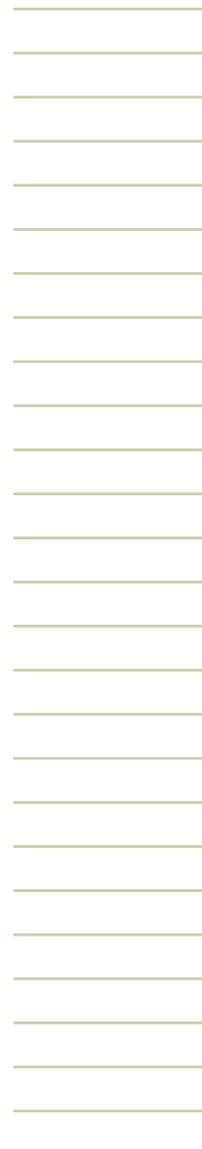


The issuer of Basic Products also meets minimum criteria with respect to its own sustainability (see “The issuer”). Furthermore, certain product groups are excluded (see “Exclusion of certain product groups”).



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THE UNDERLYING

The payment profile of a structured product is commonly linked to the performance of an underlying asset.



1. Selection of ESG-compatible underlyings¹

When selecting the underlying for their sustainable structured products, the members of the DDV undertake **to define one (or more) dedicated strategy or strategies** prior to the issuance, which must then be **disclosed** to the investor. Such strategy or strategies shall then be **applied** to the issuance of individual structured products. This is usually performed automatically. This also applies **in the case** of structured products that are only linked to the performance of a **single underlying asset**.



Certain underlyings are excluded with respect to the issuance of sustainable structured products (see “Minimum exclusion criteria” page 13).



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¹ These provisions do not apply to structured products that do not have an underlying asset or that refer exclusively to one or more interest rates or interest rates indices.



THE UNDERLYING

2. Minimum exclusion criteria¹

The ethical and moral values that investors want to see taken into account when investing in securities can vary greatly from person to person. In terms of a minimum standard, the members of the DDV undertake not to offer sustainable structured products with the following companies as underlyings or reference issuers:



Companies that generate turnover from the following sources:

- Weapons > 10%² (prohibited weapons > 0%³)
- Tobacco production > 5%
- Coal > 30%²



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¹ Relevant for individual underlyings as well as underlyings in a portfolio/basket (equities/bonds).

² Turnover from production or distribution.

³ Weapons prohibited under the Convention on the Prohibition of the Use, Stockpiling, Production and Transfer of Anti-Personnel Mines and on their Destruction (Ottawa Treaty) or the Convention on Cluster Mines (CCM), or biological or chemical weapons as defined under the respective UN conventions (UN BWC and UN CWC).



THE UNDERLYING



- Companies that commit serious violations of the following principles of the UN Global Compact (without a positive perspective):
 - Protection of international human rights
 - No complicity in human rights abuses
 - Upholding the freedom of association and the recognition of the right to collective bargaining
 - Elimination of forced labour
 - Abolition of child labour
 - Elimination of discrimination when hiring and employing
 - Precautionary approach in dealing with environmental problems
 - Promote greater environmental awareness/responsibility
 - Development and propagation of environmentally friendly technologies
 - Combat all forms of corruption

Government bodies:

- Insufficient scoring according to the Freedom House Index⁴

Agricultural commodities:

- Furthermore, agricultural commodities (soft commodities) are excluded as underlyings.

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⁴ <https://freedomhouse.org/report/freedom-world/freedom-world-2018>



THE ISSUER



Structured products are bearer bonds. It is therefore initially up to the issuer¹ (e.g., a bank) to decide how to use the funds raised in the issuance. In order not to build up a counter position to the client, derivatives can be used in the context of hedging transactions, which are usually based on the respective underlying of the sustainable structured product. A portion of the funds raised thus creates demand for the respective underlying through the trading of these derivatives. The portion of the funds raised remaining on the balance sheet of the issuer can be used to grant loans (for example) within the scope of the issuer's business activities. In this case, the contribution of the sustainable structured product to the financing of a more sustainable economy may therefore depend largely on the sustainability of the issuer's own economic activities.



Accordingly, the members of the DDV undertake to only issue sustainable structured products if they consider the UN Principles for Responsible Banking² and/or the UN Global Compact and/or equivalent principles.³



ESG Products and Basic Products (see "Principal types of sustainable structured products") shall only be issued by issuers that have been given a sustainability rating. In the case of ESG Products, the issuer shall have received the status of a sustainable company from at least one recognised rating agency.



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¹ Issuers as referred to here also mean product manufacturers within the meaning of the PRIIPs Regulation and/or the group to which the issuer belongs.

² If the UN Principles for Responsible Banking are not relevant for an issuer and/or a specific financial instrument (e.g., because the issuer does not conduct traditional banking business), the UN Principles for Responsible Investment may be considered as an alternative. Evidence that these frameworks have been taken into account can be provided by signing the corresponding document. Alternatively, the DDV Sustainable Finance Code of Conduct Advisory Board can decide on the what constitutes appropriate consideration of the respective principles. The same applies to the recognition of equivalent principles.

³ Information on the UN Principles for Responsible Banking is available at <https://www.unepfi.org/banking/bankingprinciples/>, information on the UN Principles for Responsible Investment is available at <https://www.unpri.org/>, and information on the UN Global Compact is available at <https://www.globalcompact.de/>.



EXCLUSION OF CERTAIN PRODUCT GROUPS

When issuing sustainable structured products, the members of the DDV shall focus on investment products as defined in the DDV product classification.¹



As such, leverage products are not to be actively labelled as sustainable structured products or as Basic Products.



However, this does not imply any statement with regard to the use of leverage products as hedging instruments. Structured products can play an important role in hedging risks. In securities portfolios that are fundamentally designed for sustainability (including those, for example, that are put together within the framework of asset management) these instruments should be permitted to be used, as there is also a need for hedging when investing in sustainable securities.



In addition, investment products that benefit from the falling price of the underlying asset are excluded from being labelled as sustainable structured products or as Basic Products in order not – in any case of doubt – to encourage speculative investment behaviour (to the detriment of sustainability objectives).



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¹ Available at:
https://www.derivateverband.de/MediaLibrary/Document/Derivate-Liga_A3_2020_EN.pdf



TRANSPARENCY

The **members of the DDV undertake to publish all relevant information** in an easily accessible **product policy** on a website. The relevant information shall include, in particular:



1. The **selection mechanism** (selection strategy) of the **underlying asset** (if applicable), as well as information on any (minimum) **exclusions** at the level of the underlying asset.



2. Information on the **method and data source** used to select the underlying asset as well as the relevant **sustainability indicators** used to measure the environmental or social characteristics or the overall sustainability impact of the financial product. For **ESG Impact Products**, additional information on the **criteria for the use-of-proceeds** (in terms of the requirements for the projects/companies to be funded) within the scope of the issuer's business activities is also to be included.



3. A reference on the homepage of the issuer/product manufacturer/group where all relevant information can be found, in particular with regard to their consideration of the **UN Principles for Responsible Banking** and/or the **UN Global Compact** and/or **equivalent principles**, as well as to the **reports** required under these agreements.



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TRANSPARENCY



4. For **ESG Products and Basic Products**, **information on the rating agency** and the rating qualification (rating, score, etc.) achieved by the issuer. In the case of **ESG Products**, a statement is to be made as to how the issuer has been **classified as a sustainable issuer** on this basis.



5. For **ESG Impact Products**, a **statement** is to be made as to which recognised **market standard** the products is issued in accordance with. In addition, **regular allocation and impact reports** are to be published to enable investors to track the achievement of the defined objectives. The product policy is to refer to these allocation and impact reports.



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