A&O DRAFT 1 (10 March 2021)

SUSTAINABILITY RISK POLICY
ADVISORY PROCESS

EFFECTIVE 10 MARCH 2021, VERSION 1.0

1. PURPOSE

1.1 This policy outlines our commitment and approach to integrating sustainability risk within our advisory practices. It is put in place in light of the Sustainable Finance Disclosure Regulation (**SFDR**).[1] Among other things, this refers to relevant advisory firms having to:

> *"integrate in their processes, including in their due diligence processes, and … assess on a continuous basis not only all relevant financial risks but also including all relevant sustainability risks that might have a relevant material negative impact on the financial return of an investment or advice. Therefore, financial market participants and financial advisers should specify in their policies how they integrate those risks … "* (recital 12, SFDR).

SFDR also notes as follows:

> *"To enhance transparency and inform end investors, access to information on how financial market participants and financial advisers integrate relevant sustainability risks, whether material or likely to be material, in their investment decision making processes, **including the organisational, risk management and governance aspects of such processes**, and in their advisory processes, respectively, should be regulated by requiring those entities to maintain concise information about those policies on their websites"* (recital 23, SFDR, emphasis added).

1.2 The European Commission has also proposed amendments to the AIFMD[2], which would require alternative investment fund managers (**AIFMs**) to integrate the consideration of sustainability risks into investment processes and internal organisational arrangements. Specifically, AIFMs would be required: (i) to take into account sustainability risks when conducting due diligence in the selection and monitoring of investments; (ii) to ensure that they retain the necessary resources and expertise for "*the effective integration of sustainability risks*"; (iii) to include conflicts that may arise as a result of the integration of sustainability risks in its processes, systems and internal controls when identifying and addressing potential conflicts that may damages the interests of their funds; (iv) to ensure that their risk management policies include procedures enabling the assessment and management of exposures to sustainability risks; (v) to take into account sustainability risks as part of their organisational systems and controls; and (vi) to ensure that senior managers are responsible for integration of sustainability risks.

1.3 To be clear, we are not ourselves subject to SFDR and will not be subject to the proposed amendments to AIFMD. However, from time to time, we are engaged as to provide advice to fund managers that are within scope, including one or more Luxembourg based/authorised AIFMs. Accordingly, we wish to voluntarily set out our approach on relevant matters in this document. We are also mindful of the fact that such AIFMs may request information from us from time to time to facilitate their own compliance with SFDR (and the forthcoming changes to AIFMD) – e.g. information about our approach to sustainability risk or other relevant matters.

1.4 Our approach to sustainability risk sits alongside other requirements to which we are subject under applicable law and our internal policies and procedures, such as the requirement to act in accordance with the best interests of our clients, to have appropriate product governance policies and procedures in place, to have policies and procedures in place to ensure that we understand the

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Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector at https://eur-lex.europa.eu/eli/reg/2019/2088/oj .

2 Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32011L0061&from=EN

nature, features and risks of the investments on which we provide advice, and to have robust risk management policies and procedures.

2. OUR APPROACH

2.1 This policy is currently in the process of being rolled out across Round Hill[3]. and it applies when Round Hill provides investment recommendation to the AIFM. The processes and procedures detailed herein may not yet be in place. However, this policy should be read by employees as the basis of our approach sustainability and should be followed as closely as possible (to the extent appropriate and relevant). We aim to fully implement this policy during the course of this year. Separate investment-, entity- and jurisdiction-specific processes and procedures relating to sustainability are in the process of being developed; these will need to be applied in conjunction with this policy.

3. SCOPE

3.1 This policy has been adopted by the following firms in our group (in this document, "we" or "us"):

3.1.1 Round Hill Capital Markets Limited, being a UK domiciled company and an appointed representative of Thornbridge Investment Management LLP (a UK/FCA authorised firm);

3.1.2 Round Hill Capital LLC, being a Delaware limited liability company (together **Round Hill**).

3.2 This policy is binding on us to the extent we conduct advisory activities from time to time in relation to a fund manager that falls within the scope of SFDR, as explained above. It does not apply to any other advisory or other activities we conduct.

3.3 To the extent this policy applies (as noted above), it applies whenever we provide advice regardless of the asset class. It therefore applies in relation to advice given on the following types of investments or assets, without limitation:[i]

Core asset classes – i.e. these are likely to comprise the bulk of any relevant fund portfolio

(a) Real estate (normally held via a special purpose vehicle);

(b) Investments in unlisted private companies (which may take the form of equity, or may take the form of a debt instrument that gives a right to acquire equity);

Secondary asset classes – i.e. these are likely to comprise a minor part of any relevant portfolio

(c) Investments in other investment funds that invest in the type of asset referred to in paragraph (a) above; e.g. early stage investment funds, incubators or accelerators;

(d) Hedging transactions that may be conducted to mitigate the risk of currency or interest rate fluctuations;[4]

(e) "Liquid Assets", which refers to (i) bank deposits; (ii) money market instruments; (iii) securities admitted by the European Central Bank or the Deutsche Bundesbank as collateral for relevant credit transactions; (d) undertakings for collective investment in accordance with the European Directive 2009/65/EC (the UCITS Directive) and certain

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[3] See paragraph 3.1 of this policy

[4] Note: We do not give advice on derivatives or hedging transactions to be entered into for speculative purposes.

other investment funds which according to the fund rules may solely invest in assets falling within paragraphs (i), (ii) and/or (iii) above; or (e) any other listed securities which are listed on an organised market as defined in European Directive 2004/39/EC (MiFID II). E.g. these may be recommended pending the completion of an investment in one of the core types of asset classes for a particular client, or the making of a distribution.

4. WHAT IS SUSTAINABILITY RISK?

4.1 Sustainability or ESG (environment, social, governance) is becoming a key consideration in the financial services industry.

- Significant numbers of investors are seeking to invest in funds with an environmental or social objective or element, with a proliferation of new environmental, social and governance (ESG) funds being launched in Europe.

- Climate change is one of the defining issues of our time, and the subject of increasing focus by regulators, governments and central banks. There is widespread recognition that climate change poses systemic risks, which could lead to serious negative consequences for certain individual companies, insurers, financial institutions and the broader economy.

- At a more granular level, we recognise that sustainability issues can have a real financial impact on the value of investments and investor returns over the long term, with some sectors being particularly vulnerable.

4.2 "Sustainability risk" has been defined in SFDR as "*an environmental, social or governance event or condition that, if it occurs, could cause an actual or potential material negative impact on the value of the investment*".[5]

4.3 For example, climate change can give rise to a range of sustainability risks. Financial risks from climate change arise through two primary channels: (i) physical risk from abrupt and acute weather events or chronic longer-term shifts in climate patterns, each causing disruptions to businesses and economic activities (and the value of investments in them) and (ii) transition risk from a shift to low carbon and climate resilient policies, laws and technologies and changes in societal attitudes.

4.4 Similarly, infringements of human rights can have a significant impact on the financial performance of an investment; for example, where they are the subject of global or regional media coverage, thus causing reputational – and financial – damage. Human rights issues can also give rise to disruptions in supply chains and other business interruptions, such as the cessation of operations or activities. All of these factors can have a material negative impact on investment returns.

4.5 Some common examples of sustainability risks include the following. This is by no means exhaustive given the breadth of what can be considered as a sustainability issue.

- Climate change impacts (physical and transitional).

- Biodiversity loss and degradation.

- High energy consumption.

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[5] Article 2(22), SFDR.

- Poor management of water and marine resources.
- Pollution and waste.
- Human rights issues.
- Gender pay gap and excessive executive pay.
- Lack of diversity.
- Poor stakeholder engagement.
- Community impacts and displacement.
- Social inequality.
- Insufficient whistleblowing channels and poor whistle-blower protection.
- Bribery and corruption.

5. INTEGRATING SUSTAINABILITY RISK IN OUR PROCESSES

5.1 Sustainability risk integration is a risk management process through which we seek to support long-term investment returns by taking into account, on an ongoing basis, ESG events or conditions that could (in a negative and material way) affect the value of an investment if they occur.

5.2 We believe that sustainability risks can be financially material inputs when we research and assess investments for potential acquisition by funds. We also believe that ESG should form an integral part of investment cases.

5.3 In this regard, we seek to integrate and appraise material sustainability risks in our processes in a number of ways. This means that, alongside more traditional financial criteria, we systematically consider where appropriate whether – and to what extent – financially material ESG risks might meaningfully impact our clients' investments. This does not mean that all sustainability factors and risks will be relevant for each investment. Rather, we apply a risk-based approach. The relevance – and materiality – of such matters will depend on a range of factors, including the nature of the investment, the likelihood of the sustainability risk arising, and the likely scope and scale of its impact. As such, whilst we attach importance to these factors in our processes, they are not definitive in considering whether, for example, a given investment will or will not be recommended for acquisition. Rather, they are considered in the round and in an integrated way with other factors.

5.4 **General approach**

5.4.1 In general, our risk management approach in relation to assets that are considered for acquisition by a fund from time to time, or that are held by a fund from time to time, focuses on four key phases:

5.4.1.1 **Due diligence phase**: we consider relevant risks in the due diligence conducted on a new asset considered for potential investment by a relevant fund;

5.4.1.2 **Acquisition phase**: we manage the risk involved in the acquisition process itself;

5.4.1.3 **Monitoring phase**: we establish acceptable risk thresholds; measure and monitor identified risks (e.g. market risk, liquidity risk, operational risk, funding risk, credit risk, counterparty risk, concentration risk and valuation risk); conduct periodic stress tests and scenario analysis;

5.4.1.4 **Exit phase**: we manage the risk involved in the process of exiting a particular investment.

5.4.2 As regards sustainability risk, this is an ongoing area of focus in the due diligence and monitoring phases in particular.

5.5 Due diligence phase

5.5.1 A high level summary of our internal due diligence process, conducted as part of this phase, is outlined below (subject to investment-, entity- and jurisdiction-specific processes and procedures).

5.5.2 The consideration of material sustainability risks is incorporated into this process as follows.

5.5.3 In **Step 1**, an investment opportunity is identified and put through an initial screening process to identify the most viable investment opportunities for further research and due diligence. This step in the process generally involves a consideration of economic fundamentals, whether the investment complies with the investment objectives, criteria and restrictions for the relevant fund, and whether the opportunity may be a "good fit" commercially, rather than broader risks and potential issues.

5.5.4 In **Step 2**, one or more associates are allocated to the potential investment opportunity, leading a thorough due diligence and analysis process. Key points to note:

- The team will generally be chosen on the basis of extensive industry and sector expertise.
- Using all available information, the team will consider in the ordinary course any factors that may have a material impact on the value of the potential investment, including but not limited to the following:
  - for investments in real estate – market opportunity, key drivers of value, market expert opinions, financial and operational projections, source and sustainability of income/margin, historic returns, pending risks and litigation, proposed deal structure, expected exit strategy, and key business risks and issues;
  - for investments in a company or investment fund – manager/board/executive team quality and experience, strength of proposition, approach to risk management, performance/benchmark, cost, any hedging methods used, gross market exposure, leverage, strategies, performance-based fees etc.

Alongside these factors, relevant and material sustainability risks will be identified, measured (to the extent possible) and assessed.

In relation to real estate assets, environmental risks if appropriate will be considered such as land contamination and other regulatory requirements that may be relevant, cognisant that each individual real estate asset will differ in nature.

- In conducting their due diligence on sustainability risks, the team may raise specific questions (in the form of market standard, jurisdiction specific templates or otherwise) to elicit further more detailed information; e.g.:

    - these may be issued to the sellers (in the case of real estate), fund manager (in the case of an investment fund) or senior executive team (in the case of a potential investment in a proptech company);

    - in relation to an investment fund and proptech company, among other things, this will seek to enable the associates to understand the extent to which and how the manager/senior executive team considers sustainability risks, what the main risks are, how they are monitored, managed and mitigated in practice, and (overall) how sustainability risks may affect performance or returns/value.

- The team will engage external third parties to conduct technical due diligence on a deal by deal basis where appropriate. For example:

    - a technical consultant engaged to provide a report on a potential real estate investment. The report may involve a site assessment to consider any relevant environmental conditions of the land or any relevant environmental risks (e.g. flood risk), as well as consider energy efficiency issues; and

    - market-specialist consultants to provide a report if an investment is being considered in a "proptech" company and the underlying technology is both highly specialised in nature and constitutes the core IP of the business.

- Where available, in the context of the transaction/asset, the team will obtain and consider ESG ratings and scores obtained from independent ratings agencies. It is acknowledged, however, that at the present time, these are not often available in relation to the core types of assets in which the relevant funds may wish to invest.

- Beyond this, the team will use and consider available sources of information, which are relevant to the transaction/asset in question, including publicly available studies and other resources that may contain an analysis of environmental issues or risks relating to the location of the relevant asset (e.g. exposure to the risk of floods, cyclones, rising sea levels etc).

- If the relevant fund requires any particular ESG criteria to be met (e.g. negative screening criteria or exclusions) these are also considered by the team.

5.5.5 Following the completion of its information gathering and due diligence enquiries, the team will analyse the data and information so as to form a view as to:

- whether it wishes to proceed to propose the investment opportunity or not; and

- the position on sustainability risk – in particular, whether it is considered low, medium or high for the relevant investment.

This will reflect the team's view as to the level of sustainability risk per se, together with its view as to the extent to which it can be monitored and managed.

Example 1: In relation to a potential investment, the team may identify risks that (if they crystallise) will have a highly significant impact on the value of the investment. However, the team also considers, with a high degree of confidence, that these risks can be successfully monitored and managed. The overall assessment may therefore be a "medium" rather than "high".

5.5.6 If the team forms the view that the level of sustainability risk is high (and there are no steps which can reasonably be taken to mitigate that risk) it is unlikely to proceed to propose the investment opportunity.

5.5.7 In **Step 3**, if the team decides to proceed, it prepares a report or memorandum in the standard internal format. This contains a summary of the investment opportunity, the team's recommendation, the reasons why it is making a positive recommendation, and a detailed explanation of its due diligence findings. If any third party reports have been obtained, these are either summarised or attached.

5.5.8 If appropriate to the transaction/asset in question, the report shall also include a section headed "Sustainability Risks". Among other things, this covers the following types of information to ensure the report includes a robust summary and analysis of the relevant issues, which may include (but not be limited to) any of the following:

- the types of sustainability risks that are considered to arise in relation to the potential investment;

- the level of such risks considered to arise;

- the circumstances in which they may crystallise;

- the consequences of sustainability risks crystallising, including the impact on the value of the investment;

- whether, and if so, how, this has affected the overall recommendation;

- the recommendation as to monitoring and management of relevant sustainability risks, if the investment is in fact ultimately acquired – and any costs involved;

- the overall level of sustainability risks – i.e. low, medium or high.

5.5.9 Importantly, where the report contains the Sustainability Risks section, there will also be attached to the report an excel spreadsheet prepared by the due diligence team to set out their analysis against a list of key ESG factors and serve as a form of scorecard.

- These are categorised as "risks" and "opportunities" and grouped under the following headings: Environmental Assessment, Social Assessment, Governance Assessment.

- Each row includes the team's risk assessment in respect of the relevant risk. For each row, the team ticks: Considered, Potential Risks, Risks to address ASAP, Risks to address before IC. There is also an overall assessment for each risk (with four levels of response), and additional comment boxes for mitigants, a timeframe and resources/budged needed for the mitigation strategy.

- For Environmental Assessment, the list of risks may include asbestos or other hazardous material pollution, air, water, soil, vegetation pollution, lack of flooding defences, risk of sea level rise leading to land erosion, etc.

- For Social Assessment, the list of risks may include Lack of H&S best practice standards, H&S potential future liabilities (i.e. asbestos workers), Lack of diversity in the supply chain /partners, Potential omission of Indigenous Rights, Potential risk of Human Rights abuse in the supply / procurement chain, Negative impact on Government and Community Relations, Negative impact on existing employees, Lack of adequate Labour Standards across the supply/procurement chain, Negative impact on wider stakeholder community etc.

- For Governance assessment, the list of risks may include Carbon Tax implications, Task Force on Climate-related Financial Disclosures (TCFD) requirements, Lack of Business Ethics across partners, Infringement of Anti-Competitive Behaviour, Conflict of interest in Boards Composition, Poor Accounting Standards, Potential for Bribery and Corruption, Poor/lacking of Compliance standards, Adverse Lobbying risk, Lack of Risk Management procedures, Lack of Customer Complaint procedures (throughout the chain), Lack of Whistle-blower Schemes, Lack of Dispute resolution criteria, Data protection and cybersecurity risk, Adverse Landlord obligations in leases.

5.5.10 In **Step 4**, the report is provided to the relevant investment committee for consideration. By way of background, it is relevant to note that:

- for each relevant fund, a dedicated investment committee is put together; and

- the composition of the committee is tailored on a fund by fund basis – i.e. to ensure the committee has the right voting and non-voting members, based on their respective areas of expertise, their experience of the types of investments likely to be considered for that fund, and their roles within our organisation (e.g. CIO, risk etc).

The report is discussed and voted on by the voting members of the committee established in relation to the relevant fund. As part of this, the committee members will examine the material sustainability risks relevant to the proposed investment in the due diligence report.

5.5.11 If the committee decides to approve a relevant proposal, their decision is documented in the committee meeting minutes. The meeting minutes will also document the committee's consideration of the matters relevant to its decision, including any material sustainability risks associated with the proposed investment.

5.5.12 If the investment committee approves the proposal, the firm makes a formal recommendation to the fund manager of the relevant fund that steps be taken to proceed to make the relevant investment.

5.5.13 Examples of how material sustainability risks might be considered in specific scenarios, are as follows, noting that these are examples only and do not relate to specific transactions/assets invested or to be invested by any of our funds.

<u>Example 1</u>: A particular investment opportunity is considered, being the acquisition of a residential apartment block in the Netherlands. A team is put together to conduct due diligence on the opportunity. The team formulate a due diligence strategy and proceed to collect all relevant information. They also commission a report from a local expert. The expert concludes that, although the property is compliant with all current local environmental laws, new laws relating to energy consumption are expected to be introduced in the next two years – and provides an estimate to obtain compliance. Although this will require a significant "one off" cost, the expert observes that it will result in net savings over a 10 year period, as well as making the individual apartments more attractive; i.e. higher rents and better quality tenants. The associates on the due diligence team consider the change in local law an ESG risk, but have a high level of confidence that it can be mitigated in the way proposed by the local expert. The team therefore decide to proceed to propose the investment opportunity to the relevant investment committee.

<u>Example 2</u>: A particular investment opportunity is considered, being an investment in an incubator investment fund dedicated to proptech companies. A team is put together to conduct due diligence on the investment fund and its fund manager. An associate on the team formulates a questionnaire and sends this to the fund manager. The executive team within the fund manager is highly experienced in technology based start-ups and has a thorough and documented approach as to the selection of opportunities. However, its questions on sustainability risk are marked "to be confirmed" and it confirms it has no view as to the level of sustainability risk for the investment fund. It is also unable to provide copies of policies and procedures on matters such as diversity, anti-bribery, anti-corruption or tax compliance. The board is comprised of personal friends of the founder of the fund manager who have no background in fund management or corporate governance. The team is concerned about ESG risk (and "G" in particular), but decides that the level of sustainability risk for the fund should be considered "medium", and puts the investment forward to the relevant investment committee. The committee notes the recommendation, but on balance, decides not to proceed. The committee minutes document various ESG concerns, including as regards governance in particular. However, they also request for feedback to be provided to the relevant fund managing, setting out a list of points that (if addressed) would make the committee view the opportunity more favourably.

5.6 **Monitoring**

5.6.1 If/when an investment is made for a particular fund, it is monitored on an ongoing basis by us. This covers general risks, as well as sustainability risks in particular.

<u>Real estate</u>

5.6.2 In relation to each real estate acquisition, a specific strategy is generally formulated, including steps to be taken as the ongoing monitoring and management of sustainability risks. This fits within our overall governance and risk management framework. In this regard, we are particularly mindful of the need to:

- include ambitious and yet viable environmental (E) and social (S) initiatives in our strategies, plans and budgets for each asset;

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- measure asset resilience against a range of climate change scenarios;
- set specific targets for energy and carbon;
- the need to collect data on energy, water, waste and carbon;
- conduct regular sustainability/net zero audits;
- take advantage of renewables where possible;
- regularly consider new entrants to the market with sustainability solutions and innovation opportunities;
- draft and review a detailed plan, with annual sign off and quarterly review.

6. OUR APPROACH TO INDEPENDENT DATA PROVIDERS

6.1 How we use them

6.1.1 To the extent considered useful from time to time, we may utilise inputs from leading independent ESG research, ratings and analytics firms. This includes ESG ratings and scores, where available. The ESG data is used (where available) to determine sustainability risks.

6.1.2 For example, in relation to a company, independent data providers can measure:

- Exposure: the degree to which a company's enterprise value is exposed to material ESG issues. Exposure is driven by industry affiliation, business model, cultural background, financial strength, geographic structure of revenues and assets, etc.
- Management: a company's preparedness and track record in managing its exposure to material ESG issues through an assessment of policies, programs, management systems and controversies.

6.2 Selection and oversight

6.2.1 Due diligence is applied to any independent data provider we use or rely on to a material extent for any investment, and is reviewed annually. The selection criteria used in the selection process includes the following:

- Leading firm.
- Expansive coverage.
- Reputation.

7. OTHER MATTERS

7.1 Record keeping

7.1.1 Records are kept to evidence compliance with the requirements of this policy, as well as serving as an audit trail. This includes the following:

- Due diligence reports prepared from time to time;
- Reports commissioned from third parties for the purposes of due diligence;
- ESG ratings and scores obtained from independent ratings agencies if relevant;
- Minutes of investment committee meetings, including decisions made and the analysis/reasoning in support;
- ESG monitoring strategies in relation to real estate asset.

7.2 **Compliance monitoring**

7.2.1 Our internal compliance team formulate an internal compliance monitoring programme on an ongoing basis, with regular reports being made to our risk and compliance committee. The team will regularly consider whether compliance with all or relevant aspects of this policy should be included in that monitoring programme, and if so, how and when that monitoring will take place. This decision shall be made in line with our usual governance framework.

8. FURTHER INFORMATION

8.1 For further information about this policy or the integration of sustainability risk within our advisory processes, please contact head of compliance.

9. POLICY GOVERNANCE

9.1 We revisit our processes and governance frameworks on an on-going basis to make sure they are informed by current best practice. In regards to sustainability risk integration in particular, noting this is a rapidly evolving and dynamic area, we would expect that our processes and governance will develop over time to reflect market practice and investor/client expectations.

9.2 The ESG team is responsible for the development and upkeep of this policy.

9.3 The ESG team and identified Heads of Division are responsible for updates to our approach to integrating sustainability risk into our processes.

9.4 The ESG team and Senior Executives are responsible for the implementation of this policy.

Policy owner	Head of ESG
Approved by	Executive Committee
Version	1.0
Last reviewed	March 2021
Frequency of review	Annually, or more frequently as required to address regulatory or business changes

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