

## RESEARCH ARTICLE



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# EU financial regulations and social impact measurement practices: A comprehensive framework on finance for sustainable development

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## Abstract

Sustainability is becoming the main character of the financial industry in Europe, especially after the Sustainable Finance Disclosure Regulation (SFDR) 2019/2088, which came into force on March 10th, 2021. However, despite the top-down indications for disclosing and reporting sustainability practices provided by this new policy, financial actors still lack a comprehensive framework on how to track and measure their social and environmental contributions within the perimeter of this novel institutional context. This paper discusses the implications for financial actors brought by the SFDR and builds a conceptual link with social impact measurement practices. In particular, the article provides a comprehensive framework that identifies strategic approaches and measurement tools for financial actors for building a more sustainable finance, that is a finance focused on the purest dimension of blended value and more attentive to sustainable development.

## KEYWORDS

blended value, ESG, impact finance, SFDR, social impact measurement, sustainability, sustainable development, sustainable finance

## 1 | INTRODUCTION

The new policy of the EU Sustainable Finance Disclosure Regulation (SFDR) 2019/2088 came into force on March 10th, 2021. The SFDR stresses social and environmental compliance disclosure and reporting obligations for financial services participants such as asset managers and investment funds, which are now required to define their strategic positioning (e.g., Mintzberg, 1987; Porter, 2008) with respect to sustainability.

Such regulation defines a new institutional context in which sustainability issues can become a game changer for the functioning of the financial sector. However, despite the regulation indicates various types of obligations in terms of what to disclose and report, this new

policy still lacks to highlight a clear pathway for application by asset managers and investment funds. In particular, one of the main limitations is that it hardly reconnects to the practices of social impact measurement that are currently available for financial actors to assess their environmental, social and governance contributions (from now on ESG).

Moving from this issue, this paper provides a systematization of the sustainable finance field and offers some conceptual grounding for practical action. Specifically, we evidence social impact measurement practices and procedures that financial actors may adopt in implementing the EU SFDR 2019/2088. To do this, we develop a framework which builds a conceptual link among the financial approaches of sustainability, the tools of social impact measurement,

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and the investment firms' strategic positioning within the EU SFDR 2019/2088. Methodologically, this is a theory to practice type of conceptual paper based on the case study of the EU SFDR 2019/2088. Specifically, the paper aims at offering a framework that can stimulate decision making and guide social impact measurement approaches that investment firms can consider for their strategic positioning within the novel EU Regulations for sustainable finance. For social impact measurement approaches, we refer to tools, practices and methodologies that considers aspects of sustainability including the social, environmental and governance components (e.g., Bengo & Calderini, 2016; Broccardo et al., 2020; D'Apice et al., 2021; Engle et al., 2019; Krlev et al., 2014; Stubbs, 2019).

This is a very relevant topic both from an academic and policy implementation points of view. Academically, there is a lack of comprehensive frameworks supporting actors' orientation in the enactment of social impact measurement practices within the evolving institutional field of sustainable finance (Clarkin & Cangioni, 2016; Rawhouser et al., 2019). In particular, we contribute to the emergent literature that poses the regulatory framework as the main variable to improve the understanding of the context of sustainable finance, while helping practitioners to orient themselves in this blurred environment. From a practice point of view, this is a new regulation that requires adaptations and new practices from several key actors, so there is the possibility to use scholarship to shape how actors will behave to implement this new policy. In this respect, following Carboni et al. (2019) we embrace in this paper the philosophical foundation of a scholarship committed to start with a real problem and to contribute to a relevant community of practices (i.e., asset managers).

The article is structured as follows: the second section presents our theoretical backdrop; the third section describes the evolution of regulatory frameworks for sustainability, with a focus on the European case; the fourth section proposes a strategic approach to sustainable finance, discussing the role of social impact measurement; some key conclusions are then presented in the fifth and last section.

## 2 | THEORETICAL BACKDROP: FINANCIAL ACTORS AND THEIR ROLE TOWARD SUSTAINABILITY

Academic literature in business and finance mostly considered regulatory frameworks as taken for granted, with only few works that treated regulatory changes as one of the key elements for explaining the decisions and the behaviors of financial actors for sustainability (e.g., Ahlström & Monciardini, 2021; Yan et al., 2019). According to Esposito et al. (2019), extant literature lacks studies that focus on the role of regulatory changes in determining actors' attitude and actions toward sustainable finance; this concern is shared by other scholars such as for example Nicholls (2010) and Brest and Born (2013).

The literature in the field of sustainable finance highlighted that the set of stakeholders involved in the finance industry can be divided into four main typologies (Harji & Jackson, 2012; Jackson, 2013): asset owners, who provide resources and capital; asset managers who

invest the resources and capital provided by asset owners; demand-side, the recipient of the resources, so actors who receive and exploit the capital; and service providers, such as advisors, consulting firms, or think tanks that help connecting previous actors and making deals.

According to this framework, the category of actors that should align with the new European regulation are, in particular, asset managers. Asset managers are experts in the field of investments, that gather in specific investment firms collecting capital from asset owners—that are mainly foundations, high net worth individuals, or pension funds—and investing capital and resources in specific ventures or projects having certain sustainability criteria. Thus, asset managers are investors that can take a key position in the financial market as regards embracing a strategic orientation to risk, return, industry, and the contributions to sustainability of their investments. However, these actors may be very heterogeneous along these levers, especially as regards their level of commitment to sustainability.

Nowadays, the specific context of sustainable finance is characterized by multiple typologies of actors that can be distinguished mainly for their different integration of sustainability objectives within their investment approaches (Eurosif, 2018). There are indeed several facets of sustainable investment strategies that often co-exist, mirroring the variety of aspirations that different types of investors have toward sustainability goals (Boni et al., 2021).

From a theoretical standpoint, despite their differences, these actors share the desire to combine economic and sustainability goals from their activities in the financial markets, contributing to what it is commonly known as blended value. The concept of blended value reconsiders the understanding of previously separated economic and social value in an integrated approach (e.g., Abate et al., 2021; Emerson, 2003). According to the definition of blended value proposed in Emerson (2003), blended value is used to express commitment toward the generation of financial as well as social and environmental contributions, thus embracing a holistic approach to value generation and impact. Thus, blended value identifies an increasingly expanding framework of investment and governance approaches where sustainable development and human capabilities empowerment can act as crucial drivers of operations across all sectors of the economy (Bugg-Levine & Emerson, 2011; Sancino, 2016).

Traditionally, the literature pointed at impact investors as those actors mostly called to act upon the concept of blended value, because they typically craft financial instruments for the achievement of social and environmental value while generating also financial returns, seeking for investment opportunities that intentionally aim at generating ex ante defined social and/or environmental impacts (Cooper et al., 2016). However, the boundaries of the perimeter of blended value are not well defined, stimulating the entry of actors that are committed to generate social and environmental value, but often subordinated to the financial value. For example, some private equity and venture capital actors propose the introduction of ESG principles as drivers for the generation or the protection of financial returns, either screening investment opportunities with relevant ESG performances or excluding those presenting certain ESG risks (Eccles

et al., 2020). Conversely, others consider certain ESG criteria as the main drivers for achieving positive impact out of their portfolios of investments (Bugg-Levine & Emerson, 2011).

Given these contradictions in the implementation of a blended value approach to finance and considering the new institutional context emerging after the EU SDFR policy, there is the opportunity to provide a new conceptualization of the different strategies of sustainable finance around the application of the ESG criteria. Here, we follow a conceptual scheme of three concentric circles, distinguishing for low, medium, or high levels of centrality of impact for sustainable finance (Figure 1).

The first and smaller circle (light blue) considers the minimum requirement for entering in a blended value context. Investors engage in the use of ESG approaches to mitigate potential long-term financial risks deriving from negative ESG externalities (Cort & Esty, 2020; O'Donohoe et al., 2010). Extant research reports that certain responsibility practices are well endorsed as insurance-like tools to preserve the financial return of investments (Godfrey et al., 2009; Liu & Lu, 2021). Avoiding the management of ESG and sustainability-related risks may indeed incur investors in reputation drops while penalizing economic returns (Godfrey, 2005; Godfrey et al., 2009; Koh et al., 2014; Liu & Lu, 2021).

The intermediate circle (green) considers an investment opportunity that not only assess potential ESG risks, but also generate top ESG performances. Accordingly, such investors position themselves in the blended value context among those defining stringent ESG parameters for their pipeline of opportunities. Several studies evidenced the positive relationship between financial returns and top corporate social performances of potential investees (Cheng et al., 2014; Flammer, 2013; Parker et al., 2019), interpreting high-ESG as a source of competitive advantage.

The largest circle (orange) considers the purest dimension of blended value, in which an investment strategy endorses ESG criteria from risk and performance standpoint, but also aims at measuring and generating the impacts deriving from their activities. Thus, this

investment strategy requires the fulfillment of ESG criteria and the definition of a trajectory of impact for potential investment opportunities. Accordingly, investors select only those projects or ventures whose business model builds around the intentionality and the measurability of certain social and environmental impacts (Bengo et al., 2021). In line with this, investors do not abandon financial returns, but they can bear below-market rate returns to maximize impact variance. This type of approach to blended value in the sustainable finance sphere aims at extracting positive value and impact from ESG criteria.

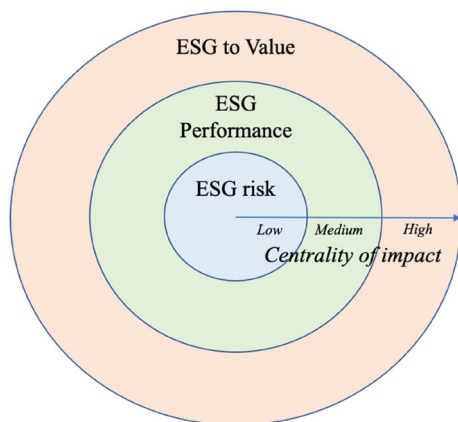
Summing up, investors may build on ESG criteria to provide various interpretation of a blended value approach. They may elevate ESG to seek impact in their investment opportunities, purely conducting an impact investing strategy—orange circle—; they could seek ESG performances to drive the definition of the investment pipeline—green circle; or consider ESG to exclude potentially harming and risky investees—light blue circle. Within this scattered context of investment firms with different shades of blended value and without a top-down policy indication, the measurement approaches and the reporting practices for the social and environmental contributions so far mainly followed mechanisms of voluntary non-financial disclosure. However, as we discuss in the next section, there is now in Europe a new institutional context with new European policies that demand adaptations and new practices by asset managers and investment funds.

### 3 | REGULATORY FRAMEWORKS FOR SUSTAINABILITY: THE EUROPEAN CASE

#### 3.1 | Evolution of the EU policy framework for ESG factors

Sustainability criteria such as today's well-known ESG pillars made their first appearance in international declarations and covenants, after World War II. The Universal Declaration on Human Rights in 1948, and the International Covenant on Economic, Social, and Cultural Rights in 1966 have set the first framework of regulations of social factors ("S") related to safeguard and respect of human rights, social rights, and cultural rights. These acts expressed a large international political consensus among governing States about the definitory character of ESG factors. In fact, they represented, although without being legally binding instruments—"so called soft law," the initial milestone of the path toward ESG factors, which was then further developed in the 1990s with a specific focus on environmental issues ("E") and, in the last decade, on governance ("G").

It is indeed only starting from 2010 that the ESG framework was consolidated at the EU level, when specific mandatory rules ("hard law") were adopted and implemented.<sup>1</sup> However, the turning point in the "ESG timeline" is represented by the adoption of United Nations'



**FIGURE 1** Blended value approach and the centrality of impact for sustainable finance. Source: own elaboration [Colour figure can be viewed at [wileyonlinelibrary.com](https://onlinelibrary.wiley.com)]

<sup>1</sup>For example: "EMAS" Regulation 2009/1221; "Timber" Regulation 2010/995; "NFR" Directive 2014/95; "Conflict minerals" Regulation 2017/821.

2030 Agenda and the Paris Agreement in 2015, a year in which regulatory obligations started increasing investors' interests in social issues and sustainability (Bauer et al., 2021; Dyck et al., 2019). Thus, the year 2015 represented a crossroads toward more structured sustainability policies, in particular in the financial sphere. Since then, the EU strategy has started to be increasingly focused on sustainable development, leveraging the role played by private investors and companies to face global challenges and crises and mobilizing, through a set of specific regulations, the role of finance for climate and social-oriented problems. Re-orienting investments toward more sustainable technologies and businesses with a long-term vision<sup>2</sup> became the backbone of the EU strategy, giving rise to a pool of norms on ESG issues.

### 3.2 | “SFDR” regulation

On November 27, 2019, the EU Parliament and Council adopted Regulation 2019/2088 “on sustainability-related disclosures in the financial services sector” (“SFDR”). The innovative goal of this regulation is the consideration of environmental impacts and of the social value that might be generated by the financial sector, mainstreaming ESG disclosure and upgrading this practice from voluntary initiative of a few innovators to a precise obligation of the general market. SFDR aims to reduce information asymmetries toward investors on the integration of sustainability risks, adverse sustainability impacts, sustainable investment objectives, and environmental or social characteristics promoted by the financial market participants. Such information is generally not deepened nor disclosed at all due to the lack of harmonized requirements and rules on sustainability impacts (negative or positive).

The first important step taken by the EU through the SFDR is about definitions. Besides specifying what is meant by Sustainability Factors (“environmental, social and employee matters, respect for human rights, anti-corruption and anti-bribery matters”) and, more specifically, Sustainable Investment<sup>3</sup> and Sustainability Risk, the regulation provides a clear framework concerning what financial market participants shall put in place in terms of disclosure and reporting practices, as reported in Table 1.

To be noted, the regulation identifies various levels of disclosure processes and practices, depending on the extent to which financial products are based on the achievement of sustainability objectives. Article 7 poses the entry level, making mandatory aspects for sustainability disclosures and asking to providing explanations of whether and, if so, how a financial product considers principal adverse impacts on sustainability factors. The key connection between disclosure and

**TABLE 1** Breakdown of the articles part of the SFDR regulation

Entity disclosure	Article 3	Publish on their website information about their policies on the integration of sustainability risks in their investment decision-making process
	Article 4	Publish on their websites whether they do consider or not the adverse impacts generated on sustainability factors and the due diligence policies adopted with respect to those impacts
	Article 5	Publish on their websites information on how remuneration policies are consistent with the integration of sustainability risks
Product level disclosure	Article 6	Provide in pre-contractual disclosures information on how sustainability risks are integrated into investment decisions and the impacts of sustainability risks on the returns of the financial products
	Article 7	Provide in pre-contractual disclosures a clear and reasoned explanation of whether and, if so, how a financial product considers principal adverse impacts on sustainability factors
	Article 8	Provide in pre-contractual disclosures and periodic reports information on how the financial product promotes and respects social or environmental characteristics and the methodology used for measuring social or environmental characteristics
	Article 9	Provide in pre-contractual disclosures and periodic reports information on how the financial product contributes to the achievement of the sustainable objective and how the sustainable goal stands out from a traditional market objective

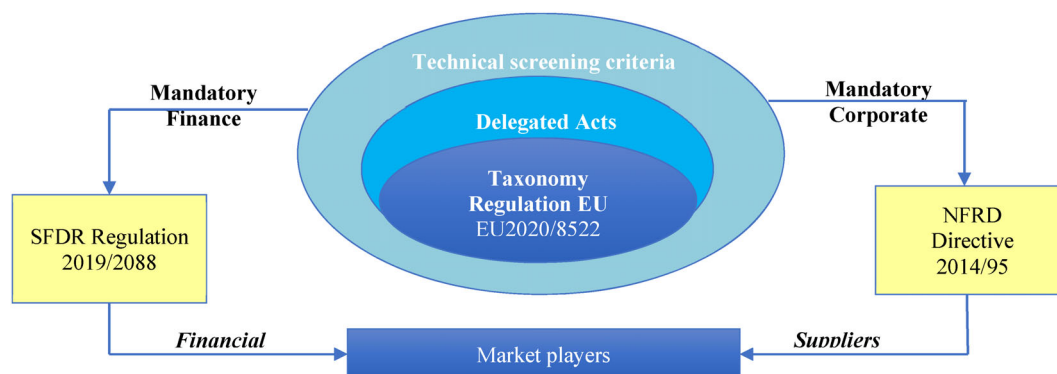
Source: Own elaboration.

Abbreviation: SFDR, Sustainable Finance Disclosure Regulation.

measurement for each financial product referred to article 8 and article 9 “(a) a description of the environmental or social characteristics or the sustainable investment objective; (b) information on the methodologies used to assess, measure and monitor the environmental or social characteristics or the impact of the sustainable investments selected for the financial product, including its data sources, screening criteria for the underlying assets and the relevant sustainability indicators used to measure the environmental or social characteristics or the overall sustainable impact of the financial product.” Thus, the measurement of sustainability levers in a financial product becomes crucial, as it represents the tool through which SFDR defines a financial product which is coherent with the idea of a sustainable finance and/or of a finance for sustainable development as our title recalls.

<sup>2</sup>EU Action plan on financing sustainable growth (2018); European Green Deal (2019); European green deal investment plan (2020); Next generation EU (2020).

<sup>3</sup>“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 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,” Article 2(17) SFDR.



**FIGURE 2** EU sustainability policy framework. Source: Own elaboration [Colour figure can be viewed at [wileyonlinelibrary.com](https://onlinelibrary.wiley.com)]

### 3.3 | “Taxonomy” regulation

Since every measurement system requires objectives, targets and KPIs, the Regulation EU 2020/852 (“Taxonomy”) set a common language for sustainability, amending SFDR and aligning the criteria to determine whether or not an economic activity could be deemed as sustainable (EU Taxonomy provides, under article 9, a full list of environmental objectives<sup>4</sup> and, in the following articles, an explanation of what they mean and the actual planning for the implementation of technical screening criteria through specific Commission's Delegated Acts).

As explained in Figure 2, the taxonomy is the core of the schemes of the EU sustainability policy framework. In the EU strategy, this taxonomy plays a pivotal role around which an integrated ESG regulatory framework of binding rules for financial actors and corporations will be created. So far, the taxonomy regulation integrates both the SFDR and the Non-Financial Reporting Directive (EU 2014/95) and will be further supplemented and detailed by the EU Commission through specific delegated acts, establishing the technical screening criteria for determining the conditions under which an economic activity qualifies as sustainable.

However, despite the environmental issues are fully embedded—Green Taxonomy can be based on metrics—, this regulatory framework present gaps concerning social objectives such as human rights, access to healthcare, decent employment, equality, non-discrimination, which necessarily shall be based on international norms, principles, and goals instead of specific KPIs. Thus, this unbalanced framework makes the compliance mechanisms for financial products characterized by both social and environmental objectives hard to detect, and, more importantly, to apply. Nevertheless, the European Legislator has already defined the next steps for further expanding the scope of the taxonomy beyond the environmental goals, including also social objectives (article 26 paragraph 2), despite at the moment a gap in the definition exists. Therefore, social objectives are a core

issue of the future Taxonomy and a specific “Subgroup on social taxonomy” of the EU Platform on Sustainable Finance is responsible for advising the Commission on extending the Taxonomy to social goals.

To sum up, the regulatory framework for sustainability is defining a pathway in which EU regulations are setting the boundaries for the whole financial sector to address sustainability issues. Despite the regulation has still to provide clear and straightforward definitions, laws such as the SFDR entered into force, requiring asset managers to adopt proper actions. More specifically, SFDR is defining a ground for the actors in the finance field that increasingly requires not only to endorse and commit to sustainability issues, but also to engage in dedicated measurement practices that can validate such commitment. However, the novelty of the top-down regulatory framework requires substantial bottom-up practices from financial actors (and corporations) demonstrating that pro-sustainability claims are achieved; we cover this key issue in the next section.

## 4 | THE MISSING LINK BETWEEN UE REGULATION AND SUSTAINABLE FINANCE: SOCIAL IMPACT MEASUREMENT

The lack of agreement so far on the definition of social and environmental impact created confusion and divergence in the sustainable finance field, harming the ability to identify uniform mechanisms of measurement and reporting. However, social impact measurement is increasingly gaining momentum in non-financial disclosure mechanisms of financials actors, playing not only a crucial role from a compliance standpoint, but potentially also a strategic role in how case investors may consider impact within a blended value context (Maas, 2009; Maas & Liket, 2011). Thus, as in the aims of our paper, a comprehensive framework that interprets the binding rules of the EU regulations under the lenses of social impact measurement may help discerning a strategic pathway for dealing with sustainability issues.

According to the literature, the capital of several asset owners has been invested for long time without unlocking potential social and environmental impacts (e.g., Jackson, 2013). As times are changing, metrics of measurements emerged from debates involving industry

<sup>4</sup>(Climate change mitigation; climate change adaptation; the sustainable use and protection of water and marine resources; the transition to a circular economy; pollution prevention and control; the protection and restoration of biodiversity and ecosystems)—SFDR, Article 2—Definitions (17).



leaders, academics, and think-tanks that worked hard to generate, assess, and improve a set of cross-industry standards based on social-performance metrics for asset managers and ventures (Mura et al., 2018). However, despite measurement systems are increasingly taking a holistic perspective, the customization and the decentralization of approaches are sometimes required for context-specific impact assessments (Costa & Pesci, 2016). For these reasons, since impact is not one-size-fits-all (Maas, 2009), more than a definition of a standardized measure for impact, a definition of a framework guiding the decision of which standards to select to support both the compliance and the strategic aspects of impact can be of great support for the sustainable finance field. Indeed, this field is metrics-rich but poor of a framework helping to navigate what metrics fit better financial actors' approaches to understand the impact of their financial products.

In this respect, considering the importance of social impact measurement in the wake of the upcoming requirements of the EU Regulation, we develop in this paper a framework for identifying coherent measurement tools depending on the strategic positioning that investors may adopt for their financial products. Since March 10, 2021, financial actors are indeed forced in Europe to position financial products within articles 7, 8, or 9 of the Regulation 2088, with, as we show later, different implications in terms of level and intensity of strategic orientation of finance toward a blended value approach and sustainable development. Thus, understanding the coherent social impact measurement practice is fundamental to ensure the compliance of financial actors to the definitions reported in the taxonomy. Here, we identify a set of methodologies and criteria of social impact measurement that fit within the various articles of the regulation.

#### 4.1 | Article 7 and ESG risks

Considering the requirements of Article 7, the financial market participants are required for each financial product to provide disclosure on whether and how financial products consider adverse sustainability risks. If a financial market participant does not consider the negative effects of investment decisions on sustainability factors, they must publish a detailed explanation of them on their website. The measurement of social impact takes in this case a narrative shape in the reporting activities, with a low centrality of the impact part, but rather aiming at shedding light on the mechanisms of negative evaluations for certain investment opportunities, and at how ESG issues are considered to achieve the financial returns proposed to capital owners. The literature already approached ESG from risk perspective, evidencing that better ESG performances lead to insurance-like protection with respect to the financial returns (Godfrey, 2005; Godfrey et al., 2009; Koh et al., 2014). From a financial actor standpoint, previous studies approached ESG risks through negative screening and exclusionary dynamics (Aslaksen & Synnestvedt, 2003; Haigh & Hazelton, 2004): the literature refers here to absolute exclusion, when potential investment opportunities do not fulfill certain standards for ethical performances.

To this regard, the evaluation is based on the narrative reported by third party information, such as UN reports, in which entire industries are rejected—such as the weapons, or tobacco. Accordingly, ESG risks may follow a product-based exclusion. However, process-based exclusion may occur too: for example, use of plastics in the supply chain and child labor dynamics may lead to exclusion. Scholars evidenced the ESG risks of investments also in terms of the ethical approaches of finance (Haigh & Hazelton, 2004): often used interchangeably with socially responsible investments (Hellsten & Mallin, 2006), ethical approaches attempt to provide control for exogenous factors with respect to stakeholders' values, making economic returns going hand in hand with moral and responsible conducts. These approaches should lead to “healthier” returns for investments, avoiding opportunities that the relevant audience dislikes for their inadequate moral.

For these reasons, more than pure measurement system of social impact, the categorization within Article 7 requires actors to identify what ESG criteria are considered in terms of potential risks that may generate on the financial component. From this perspective, asset managers adopt ESG criteria with a passive approach, aiming at avoiding risks for the financial returns more than seeking ESG value besides economic value. Certain principles of the UN PRI criteria fit this framework. The UN PRI criteria are high-level guidelines that aim at defining an overall vision for investment approaches that consider ESG principles also from a risk mitigation perspective (Table 2).

For example, financial actors' signatories of UN PRI criteria should *incorporate the ESG issues in investment analysis and decisions—Principle 1—*, in a way that the management of such issues are reflected in the exclusion of certain sectors, companies or practices based on specific sustainability criteria—for example, tobacco industry, weapons—from an investment fund or portfolio, and should be considered in the *ownership policies* and *procedure* too—*Principle 2*. To comply with this position, investors often develop and disclose a risk matrix in which they represent a dashboard of combinations involving a list of industries, sectors and contexts whose potential ESG risks may damage the long-term protection of the financial returns of investments, *avoiding harm* more than generating impact.

**TABLE 2** UN PRI principles

Principle 1	We will incorporate ESG issues into investment analysis and decision-making processes.
Principle 2	We will be active owners and incorporate ESG issues into our ownership policies and practices.
Principle 3	We will seek appropriate disclosure on ESG issues by the entities in which we invest.
Principle 4	We will promote acceptance and implementation of the Principles within the investment industry.
Principle 5	We will work together to enhance our effectiveness in implementing the Principles.
Principle 6	We will each report on our activities and progress toward implementing the Principles

Abbreviation: ESG, environmental, social and governance.

## 4.2 | Article 8 and ESG performance

Considering the requirements of Article 8, the information about a financial product to be communicated must include: (i) how social and environmental characteristics are respected and addressed; (ii) the methodology to use for the measurement of these characteristics. The social impact measurement criteria for financial products that can be positioned within Article 8 require the absorption of *ex ante* defined sustainability criteria that outline eligible investment opportunities. Differently from what reported for Article 7, there is a positive screening approach for which the investments in selected sectors should obtain a higher overall performance under sustainability criteria than their peers to be considered eligible for financial products part of this category; in alternative, investment opportunities may be selected depending on norm-based screening, for example considering only those ventures that possess prosocial certifications—for example, B Corps, Organic.

Despite certain scholars beware of the lack of standardization and transparency about ESG performances (Consolandi et al., 2020), ESG performances increasing play a strategic and relevant role in the financial sphere. Academic literature in management and finance investigated the implications for firms evidencing particularly high performances on ESG criteria; for example, scholars evidenced that several financial actors extract financial values out of portfolios presenting higher ESG performances than peers with average ESG performances (Cheng et al., 2014; Flammer, 2013). Investment solutions presenting higher ESG performances than peers are deemed to have more chances to generate better financial returns.

Accordingly, these types of approaches are in line with the shade of blended value finance that proactively considers and builds on ESG measurements to identify investment opportunities from which extracting financial returns. For these reasons, asset managers adopt mechanisms of performance measurement on ESG criteria. There are over 1000 examples of ESG ratings, indices and managerial dashboards available to assess whether and how organizations assess Environmental, Social and Governance criteria. Among those most adopted, the GIIRS ratings help asset managers to assess their portfolio's contributions to sustainability to deliver a comprehensive audit portfolio's performance on workers, governance, customers, communities, and the environment. They rely on the questionnaire proposed by the B Impact Assessment to measure the sustainability performance of investment funds. This tool allows a comparison of performance against 13,000 investees of overall 90 funds. In alternative, and still compatible with the criteria of Article 8, we can find the global reporting initiative (GRI). Using the GRI guidelines, organizations disclose their most critical impacts, whether positive or negative, on the environment, society, and the economy (Ortas et al., 2015). The GRI generates reliable, relevant, and standardized information to evaluate opportunities and risks, and to enable a more informed decision-making process, both within the company and among its stakeholders. The GRI is designed to be universally applicable to all organizations of all types and sectors, large and small, around the world.

These types of ESG approaches help financial products to navigate investment opportunities with specific characteristics and requirements, distinguishing them from business-as-usual opportunities for their relevant ESG aptitude, and thus offering a proactive interpretation to sustainability practices. These investment criteria may not only use tools to exclude contexts that potentially harm the society and the environment but may adopt metrics and performance measurements to identify investment opportunities that strategically considers relevant ESG performances.

## 4.3 | Article 9 and ESG to value: Theory of change

Considering Article 9, the legal requirements involving a financial product that has sustainable investments as its objective (and for which an impact objective to be pursued is designated *ex ante*) are to: (i) indicate how the investments are contributing to achieve the impact objective; (ii) indicate how the impact objective differs from a traditional market objective.

Actors willing to positioning within Article 9 are required to disclose the impact objective that distinguishes the financial product and its final target of impact. Conversely, actors positioning in Article 8 are required to present the characteristics for which they select investment opportunities avoiding anticipating *ex ante* impact objectives. Differently from Article 8, the positioning in Article 9 goes beyond ESG performances, requiring highest ESG performances to be associated with the generation of positive impacts on *ex ante* defined overarching sustainability objectives. In this respect, since Article 9 poses the impact target at the core of the disclosure mechanisms, the impact measurement approach should cover all the processes and procedures of the financial product. For example, for investment funds that position in Article 9, the compliance with the regulation requires asset managers to have an active approach with respect to the target investees, ensuring that social value can be extracted from activities and outputs of their business models.

These types of products are suitable with the purest principles of blended value that recall to impact investing practices in which a sustainability objective is the prerequisite for the enactment of a financial product. The use of financial products for impact investing purposes involves the application of a theory of change (ToC) for investment opportunities. A theory of change (ToC) describes how and why an investment opportunity is supposed to lead to a desired result—environmental and/or social (Ebrahim & Rangan, 2014). Often a ToC is defined as the connection between activities and results (outputs, outcomes, and impacts). The measurement of social impact through a ToC approach defines the social and/or environmental problem that a financial product aims to solve, and the context in which it is supposed to be enacted. Similarly, logic models have been used to measure social innovation practices of entrepreneurial activities (Krlev et al., 2014), which is a complementary feature of the generation of social impact (Arena et al., 2018; Calderini et al., 2018). Thus, the identification of a precise impact objectives makes the ToC suitable for the compliance with Article 9 of the Regulation, which assumes the

construction of an impact measurement infrastructure that allows to report on the ex ante defined sustainability objective(s) for which the financial products have been created. Within this framework, the sustainable development goals (SDGs) impact standards are a set of practices that help companies and investors to align their activities with the SDGs, facilitating the mobilization of resources toward the generation of outcomes and impacts on the SDGs and implementing ToC to identify the impact targets. The standards provide a common language and best practices that can guide the achievement of social and/or environmental impacts from the screening of activities to their monitoring over time and to the exit strategies. The SDG Impact Standards also consider a predetermined set of KPIs to be applied to investment opportunities as impact targets to be achieved, linked to specific SDGs to contribute for.

In addition, the Impact Management Program (IMP) is a coherent recipient for the application of ToC approaches, thus aligning with the Article 9 of the regulation. The IMP has defined five dimensions through which evaluating the impact: What, Who, How Much, Contribution, Risk. In relation to these dimensions, a set of categories has been defined to allow companies and investors—mostly private investment funds—to set impact targets and evaluate performances. These categories are building blocks that can be used by an organization to frame their impact picture or as a checklist to ensure they cover any elements essential to managing impact (Figure 3).

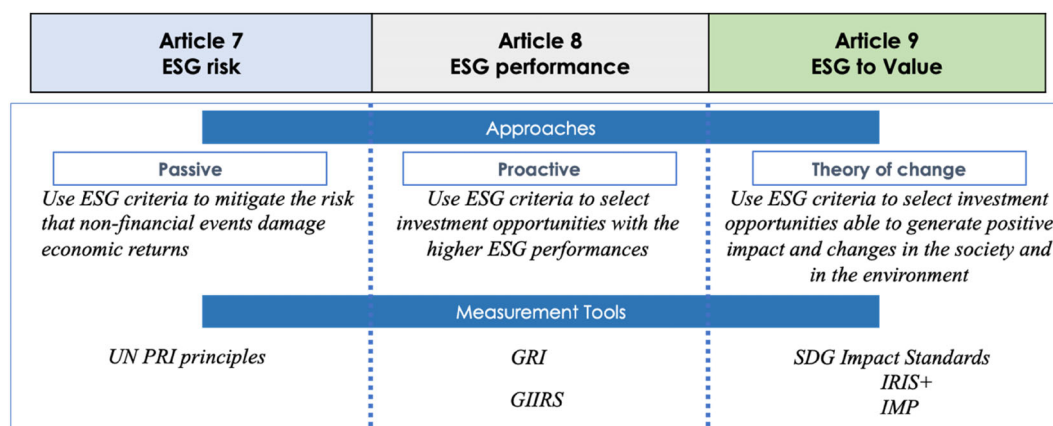
## 5 | CONTRIBUTIONS AND CONCLUSIONS

With this article, we aim to build a conceptual and practical link that may align the non-financial disclosure practices of financial products and the requirements imposed by the upcoming European regulatory frameworks and in particular the Regulation 2019/2088. We argue that mechanisms of social impact measurement can play a relevant role for defining the boundaries of non-financial disclosure practices, given the lack of current guidelines to be followed.

As the literature acknowledged, finance took time to unlocking potential social and environmental impacts out of capital availabilities (Jackson, 2013). Nowadays, the hype for impact in finance is so spread that the risk of misleading, mistrustful practices (greenwashing) urged Regulators to define strict boundaries in the ways sustainability issues are considered and disclosed in a financial product. Accordingly, metrics for the measurements of sustainability commitment emerged to give substance to sustainability disclosures requirements, but, throughout the myriad of approaches, a strategic framework is still missing to guide the decision of which type of standard or metrics to adopt for maximizing impact.

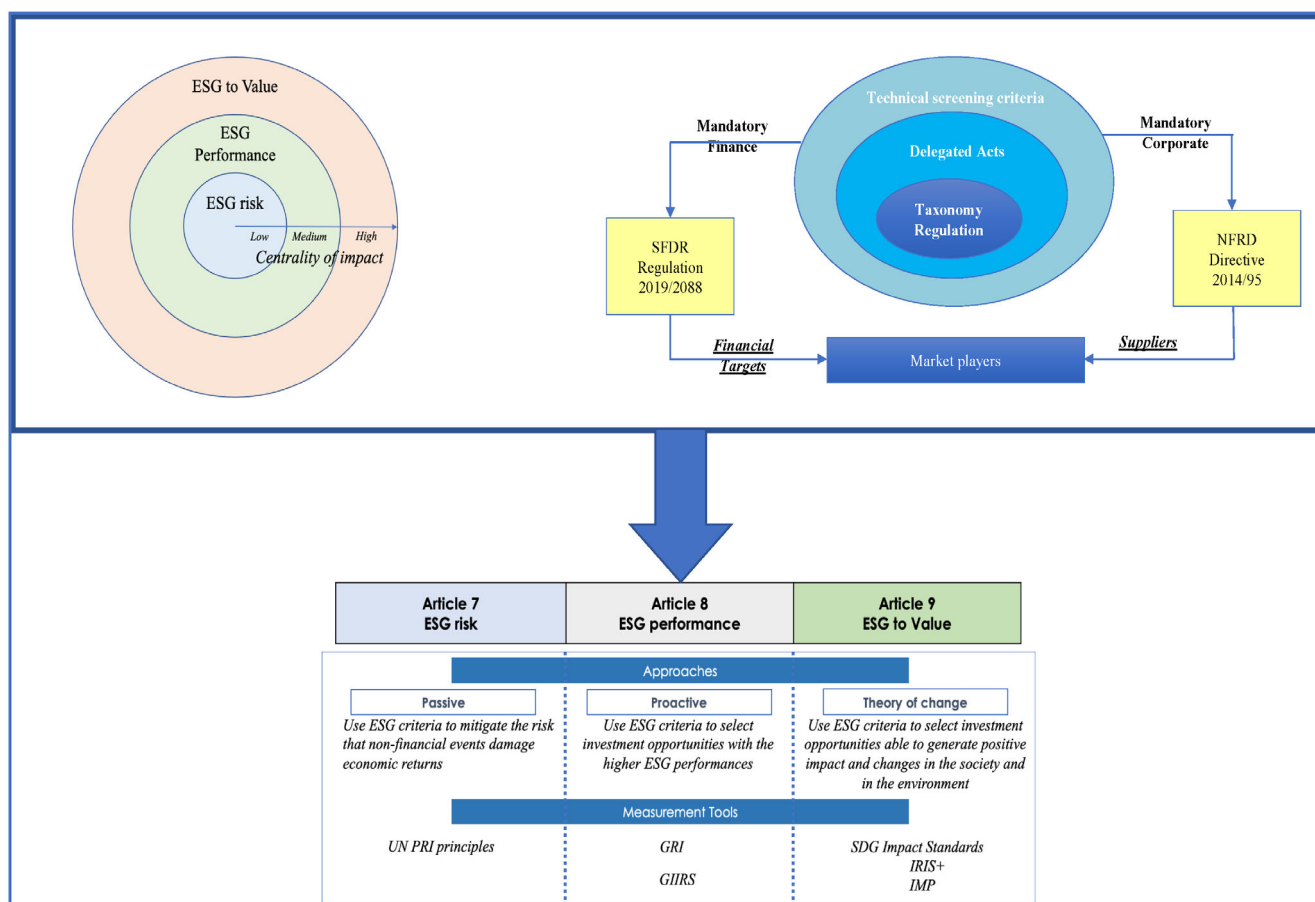
The Regulation 2019/2088 represents the case of a policy that actors operating in the finance industry must absorb and implement in their strategies. Following on previous studies on the nexus between regulations and strategies (see e.g., Krlev et al., 2020 for policy implementation in the social innovation context), our paper builds on current literature that is advancing the importance of regulatory frameworks to explain sustainable finance. In particular, since extant literature evidenced mechanisms through which regulatory systems can act to either spur or harm profit-oriented investors' engagement on sustainability objectives (Yan et al., 2019), we explored within the specific EU regulatory framework for sustainable finance which social impact measurement practices can play a role to establish a real link between regulations and their strategic, rather than formal and cosmetic (e.g., Abrahamson, 1996; Marcuccio & Steccolini, 2005), implementation in the impact finance field.

As reported in Figure 4, this work combined a new perspective on the blended value framework (Emerson, 2003) within the overall new EU sustainability regulatory framework. First, we distinguished the various facets of sustainability value integration in the economic values, referring to the extent which ESG criteria respectively mitigate risks, are exploited as a source of performance, or are the starting point to generate impact by recognizing the increasing importance of the ESG component in a profit-oriented investment activity. Second, we analyzed how EU regulations are setting the rules for the adoption of sustainability approaches in the marketplace, discussing that the



**FIGURE 3** Conceptual framework of strategic approaches and measurement tools for coherently measuring impact within Article 7, 8, and 9 of the Regulation 2088. Source: Own elaboration [Colour figure can be viewed at [wileyonlinelibrary.com](https://onlinelibrary.wiley.com)]





**FIGURE 4** Resume of the reasoning adopted to develop the conceptual framework presented in the paper. Source: Own elaboration [Colour figure can be viewed at [wileyonlinelibrary.com](https://onlinelibrary.wiley.com)]

three levels identified in the theoretical backdrop in Figure 1 (the centrality of impact) can reflect the three specific positionings within respectively Article 7, or 8 or 9 of the Regulation 2019/2088.

In particular, we focused on the strategic features of the blended value literature to help developing a new conceptualization that reinterprets the upcoming changes in the regulatory frameworks for sustainable finance in Europe with the aim of providing recommendations to be considered by practitioners active in the sustainable finance field. Specifically, we identified a mechanism linking EU Regulations' obligations and measurement approaches of social impact, offering answers for the compliance requirements. Our arguments have three main implications.

First, we developed a comprehensive and applicable toolkit that may drive the compliance to the novel Regulation, helping actors involved to understand the various facets of social impact measurement. Given the upcoming updates on the regulatory frameworks affecting the business and financial industries, our work aims at guiding decision makers to embrace a transformative and strategic repositioning shift toward impact finance for sustainable development, rather than to implement the new EU policies with a bureaucratic and passive attitude toward sustainable finance. Moreover, the toolkit provides relevant academic advancements with respect to the

literature involved in impact finance. As impact finance literature is quite fragmented and scattered (Clarkin & Cangioni, 2016), we proposed a conceptual advancement that frames the spectrum of sustainable finance strategies within an ESG interpretation that links responsible investing and impact investing.

Second, we highlighted the importance of sustainability impact for the new era of the financial sector, with the intent of stimulating the application of the social impact measurement practices not just for matters of compliance, but increasingly with a strategic, value added vision. In particular, we contribute to the social impact measurement literature providing a structure for interpreting the tools for measuring impact within an institutional perspective. Considering that scholars in the field evidenced the lack of standardized approaches (Rawhouser et al., 2019; Salazar et al., 2012), we argue that by linking and embedding social impact measurement with the institutional setting may help future research, policy and practice to overcome the downsides of the heterogeneity of approaches in the field. Our conceptual framework proposed a toolkit of measurement tools with a strategic relevance for financial products, but they may be suitable also for hybrid organizations presenting different facets of the sustainability component (Santos et al., 2015). Especially in the context of the B Corp movement, the literature evidenced that the hybrid



condition is no one-size-fits-all (Conger et al., 2018), so that a three-level measurement framework of approaches to the ESG criteria may clarify the organizational identities of complex entities, such as hybrids, through a proper way of measuring their contributions to the ESG pillars (Al Taji & Bengo, 2019).

Third, considering that the regulatory framework is evolving, and will demand for increasingly relevant sustainability-oriented practices, there is a gap in both research and practice to better understand, research and implement the role of social impact measurement as either a top-down or bottom-up tool for implementing regulations on sustainability. In this respect, future studies may explore the strategic opportunities of anticipating the institutional and regulatory evolutions, where the advantage of a strategic approach combining a competitive positioning while contributing to sustainable development appears to be a desirable praxis for the progressive transformation of the entire finance field.

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