

Aviva response to ESMA Consultation Paper: On integrating sustainability risks and factors in the UCITS Directive and AIFMD

https://www.esma.europa.eu/system/files_force/library/esma34-45-569_consultation_paper_on_integrating_sustainability_risks_and_factors_in_the_ucits_directive_and_aifmd.pdf?download=1

A. General remarks

1. Aviva is strongly supportive of targeted policy and regulatory measures to promote sustainable finance. We have been closely involved in this agenda for many years, including as members of the EU Sustainable Finance High-Level Expert Group (HLEG).
2. We therefore welcome the European Commission and European Supervisory Authorities' (ESAs) willingness to enact legislative and regulatory change to promote a more sustainable financial system in the EU.
3. We believe the European Commission, in consultation with the ESAs, should develop an indicative, non-binding list of relevant sustainability risks, for firms who wish to do so to use as a reference point when complying with these changes and others introduced elsewhere in the Commission's Sustainable Finance Action Plan (e.g. the Disclosure Regulation).

B. Response to questions.

Q1: How do you understand or how would you define the notion of “sustainability risks” for the purposes of the delegated acts adopted under the UCITS Directive and AIFMD?

See e.g. <https://materiality.sasb.org/> . As above, we believe the European Commission, in consultation with the ESAs, should develop an indicative, non-binding list of relevant sustainability risks, for firms who wish to do so to use as a reference point when complying with these changes and others introduced elsewhere in the Commission's Sustainable Finance Action Plan (e.g. the Disclosure Regulation).

Q2: Do you agree with the proposed amendments relating to organisational requirements included above following a high-level and principles-based approach? If not, please elaborate on the reasons for preferring a more granular approach and describe how you would incorporate such view in the aforementioned provisions.

Yes.

Q3: Do you see merit in expressly requiring or elaborating on the designation of a qualified person within the authorised entity responsible for the integration of sustainability risks and factors (e.g. under Article 5 of the Commission Directive 2010/43/EU and Article 22 of the Commission Delegated Regulation (EU) 231/2013)?

We would recommend that the revised rules make specific reference to the need for firms to ensure there is sufficient knowledge and understanding of sustainability issues to assess risks and factors properly.

Q4: Would you propose any other amendments to the provisions on organisational requirements in the Commission Directive 2010/43/EU or Commission Delegated Regulation (EU) 231/2013 as set out in Annex III to ensure the effective and adequate integration of sustainability risks and factors?

No.

Q5: Do you agree with the proposed amendments to provisions relating to due diligence included above following a high-level and principles-based approach? If not, please elaborate on the reasons for preferring a more granular approach and describe how you would incorporate such view in the aforementioned provisions.

We would propose the following wording:

Article 23 Due diligence requirements 1. Member States shall require management companies to ensure a high level of diligence in the selection and ongoing monitoring of investments, in the best interests of UCITS and the integrity of the market. Management companies shall seek to mitigate sustainability and other risks identified in investments through engagement with issuers of those investments and use of voting rights associated with them (if applicable) in the best interests of the UCITS and its investors.

Q6: Do you see merit in further elaborating in the provisions above on the identification and ongoing monitoring of sustainability risks, factors and indicators that are material for the financial return of investments?

We would recommend that the following provisions be added to Article 22 of Delegated Directive 2010/43/EU and Article 17 of Delegated Regulation 231/2013/EU in order to meet the request from DG FISMA that sustainability risks be explicitly integrated into the duties owed by UCITS Management Companies and AIFMs to their funds and unit-holders. We consider that this would also be consistent with the approach taken by EIOPA regarding their technical advice for the integration of sustainability risks into the 'prudent person' principle in Solvency II, which saw them recommend an additional article to be added to the Delegated Regulation.

UCITS Delegated Directive 2010/43/EU

Article 22 Duty to act in the best interests of UCITS and their unit-holders

- 1. Member States shall require management companies to ensure that unit-holders of managed UCITS are treated fairly. Management companies shall refrain from placing the interests of any group of unit-holders above the interests of any other group of unit-holders.*
- 2. Member States shall require management companies to apply appropriate policies and procedures for preventing malpractices that might reasonably be expected to affect the stability and integrity of the market.*
- 3. Without prejudice to requirements under national law, Member States shall require management companies to ensure that fair, correct and transparent pricing models and*

valuation systems are used for the UCITS they manage, in order to comply with the duty to act in the best interests of the unit-holders. Management companies must be able to demonstrate that the UCITS portfolios have been accurately valued.

4. Member States shall require management companies to act in such a way as to prevent undue costs being charged to the UCITS and its unit-holders.

5. Member States shall require management companies to consider all financially material risks and opportunities, including sustainability factors, in undertaking their duty to act in the best interests of the UCITS they manage and their duty to act in the best interests of the unit-holders of the UCITS.

AIFMD Delegated Regulation 231/2013/EU

Article 17 Duty to act in the best interests of the AIF or the investors in the AIF and the integrity of the market

1. AIFMs shall apply policies and procedures for preventing malpractices, including those that might reasonably be expected to affect adversely the stability and integrity of the market.

2. AIFMs shall ensure that the AIFs they manage or the investors in these AIFs are not charged undue costs.

3. AIFMs shall ensure that, in undertaking their duty to act in the best interests of the AIF they manage and their duty to act in the best interests of the investors of the AIF, they consider all financially material risks and opportunities, including sustainability factors.

See also our general remark above on preference for an indicative, non-binding definition of “sustainability risks and factors”.

Q7: Do you agree with the proposed inclusion of recitals relating to conflicts of interest? Should the technical advice cover specific examples? If so, what would be specific examples of conflicts of interests that might arise in relation to the integration of sustainability risks and factors and should be covered in the advice?

Yes. Firms should ensure that they consider the way in which they can manage the conflicts of interest that may arise between different investors in the same collective investment product, when pooled investors may have different ESG preferences and different investment time horizons, so that the fund is run in the best interests of all investors as a whole.

Q8: Would you propose any other amendment to the provisions on operating conditions in the Commission Directive 2010/43/EU or Commission Delegated Regulation (EU) 231/2013 as set out in Annex III to ensure the effective and adequate integration of sustainability risks and factors?

No.

Q9: Do you agree with the proposed amendments to provisions relating to the risk management included above following a high-level and principles-based approach? If not, please elaborate on the reasons for preferring a more granular approach and describe how you would incorporate such view in the aforementioned provisions.

Broadly, yes. We would suggest the following addition:

Article 38 Risk management policy 1. Member States shall require management companies to establish, implement and maintain an adequate and documented risk management policy which identifies the risks the UCITS they manage are or might be exposed to. The risk management policy shall comprise such procedures as are necessary to enable the management company to assess for each UCITS it manages the exposure of that UCITS to market, liquidity, sustainability and counterparty risks, and the exposure of the UCITS to all other risks, including operational risks, which may be material for each UCITS it manages. [...]
In considering materiality of risks, management companies should take a long-term approach, including through considering the recommended holding period of the UCITS (if any).

Article 40 Risk management policy 1. An AIFM shall establish, implement and maintain an adequate and documented risk management policy which identifies all the relevant risks to which the AIFs it manages are or may be exposed. 2. The risk management policy shall comprise such procedures as are necessary to enable the AIFM to assess for each AIF it manages the exposure of that AIF to market, liquidity, sustainability and counterparty risks, and the exposure of the AIF to all other relevant risks, including operational risks, which may be material for each AIF it manages. In considering materiality of risks, management companies should take a long-term approach, including through considering the recommended holding period of the AIF (if any).

Q10: Do you see merit in further specifying the content of the risk management policy by expressly listing key elements for the effective integration of sustainability risks (e.g. techniques, tools and arrangements enabling the assessment of sustainability risks, probability of occurrence and time horizon of sustainability risks with regard to the expected time of holding of the positions bearing the risks, quality of underlying data and methodologies etc.)?

Yes, in order to provide consistency and comparability.

Q11: Do you see merit in amending risk management provisions relating to regular review of risk management policies and systems in order to more specifically refer to elements related to sustainability risks (e.g. quality of the arrangements, processes, techniques and data used, need for authorised entities to highlight the limitations, and demonstrate the absence of available alternatives)?

Yes, in order to provide consistency and comparability.

Q12: Would you propose any other amendment to the provisions on risk management in the Commission Directive 2010/43/EU or Commission Delegated Regulation (EU) 231/2013 as set out in Annex III to ensure the effective and adequate integration of sustainability risk and factors?

No.

Q13: What level of resources (financial and other) would be required to implement and comply with the proposed changes (risk management arrangements, market researches and analyses, organisational costs, IT costs, training costs, staff costs, etc., differentiated between one off and ongoing costs)? When answering this question, please also provide information about the size, internal organisation and the nature, scale and complexity of the activities of your institution, where relevant.

See e.g.

https://www.moodys.com/login?lang=en&cy=global&ReturnUrl=https%3a%2f%2fwww.moodys.com%2fviewresearchdoc.aspx%3fdocid%3dPBC_1127353%26lang%3den%26cy%3dglobal