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Subject: ESMA34-45-569, ESMA35-43-1210 (Consultation Papers on *Sustainability Risk in MiFID II, UCITS, and AIMF Directives*)

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RESPONSE

This response consolidates both of the aforementioned Consultation Papers to advance the position that the natural environment, notwithstanding its importance for our subsistence, does not constitute subject matter for legislation of financial markets.

The Commission's objective "*to explicitly require the integration of sustainability risks in the investment decision process*", *p.11*[1], is naive and detrimental, starting from the strangeness of its definition of "*sustainable finance*". In the context of finance, *sustainability* denotes the issue of whether an investment or business strategy is functional enough to run its course without the imminence of insolvency in the long term. Thus, conflating in financial legislation the notion *sustainability* with environmental, social, and governance factors ("the ESG factors") will lead to needless conflicts that foreseeably will worsen as regulatory controversies arise.

Financial markets legislation should not obfuscate the assessment of entities' financial situation, as that would subject the EU financial industry to a competitive disadvantage. The ESMA's admission that "*the existing UCITS and AIFMD frameworks do not include a legal definition of 'sustainability risks'*" (*p.15*, with the meaning of *sustainability* as implied from the ESMA's draft) reflects the obvious abyss between the topic of ecology and the topic of financial markets legislation.

The fact that ecology may be a paramount concern in some *specific* sectors of the economy does not merit enacting a *generalized* duty to collect, model, and evaluate data which oftentimes is of negligible or non-existent relevance to an entity's financial condition and prospects[2]. And imposing that the entity's investment decision process be significantly premised on ESG factors will ultimately deter investments.

The closest the Commission could get toward promoting ESG factors is by *stimulating* --rather than prescribing-- a transformation of what economists abstract as agents' *utility function* and which is reflected in those agents' decision making.

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[1] Except where indicated, paragraph numbers refer to ESMA34-45-569 (*in re* UCITS, AIFM)

[2] The boilerplate text suggested in ESMA35-43-1210 admittedly uses the qualifying language "*where relevant*", but it nonetheless leaves the door open to subsequently heightening the compulsory inclusion of ESG factors.

Directing to the end users [of goods and services] such stimulus will be more effective than any framework of compulsory investment premised on ESG factors. Likewise, fiscal stimulus can promote ESG factors. Nevertheless, neither sort of stimulus is within the ESMA's province.

The ESMA points out that "*Sustainability has long been at the heart of the European project*", *p.4*. But that motivation does not warrant overstretching the scope of financial markets legislation either. The rhetoric used in the Consultations at issue can set a harmful precedent for a staggering obfuscation of EU legislation apropos of each and every value that "*has long been at the heart of the European project*".

The ideal of democracy exemplifies the danger inherent to that type of rhetoric: Despite democracy being another long standing value at the heart of the European project, it would be unproductive to burden financial analyses and financial planning with a notion of "democratic finance" (in the vein of "sustainable finance") regarding the extent to which an entity's decisions are made *democratically*.

Moreover, the drafts indicate that "*this [environmental] taxonomy [...]* ***at least initially****, will not cover social and governance issues*", *p.35* (emphasis added), which does not rule out the possibility that delving also in social and governance issues may eventually become compulsory. Quite the contrary, *p.27* already suggests that "*social risks could be considered as material for the valuation of instruments*". This ambivalence in legislative developments is certain to confuse investors and market participants (thereby defeating the caution outlined in *p.6* of Annex I).

The drafts depict "*over two thirds of retail investors considering environmental and social objectives as important for their investment decisions*", *p.13* (ESMA35-43-1210). But the ESMA should not blindly assume that responses in a survey consistently reflect the respondents' *actual* investment decisions. The ESMA's efforts should focus on the latter and on ensuring a transparent disclosure of each *financial* risk (be it market, credit, liquidity, or related), not on emphasizing political correctness.

To be clear, values such as the preservation of the natural environment, world peace, human dignity, and a person's development are essential in our civilization. But discerning the *proper* venue to promote each one of those values is important and smart. Financial valuations with compulsory commentary on non-financial issues are not a proper venue for the Commission's mislabeled concern of environmental challenges.