JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

Response form for the Joint Consultation Paper concerning ESG disclosures

23 April 2020

Date: 23 April 2020
ESMA 34-45-904

JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

Responding to this paper

The European Supervisory Authorities (ESAs) invite comments on all matters in this consultation paper on ESG disclosures under Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial sector (hereinafter "SFDR") and in particular on the specific questions summarised in Section 3 of the consultation paper under "Questions to stakeholders".

Comments are most helpful if they:

1. contain a clear rationale; and
2. describe any alternatives the ESAs should consider.

When describing alternative approaches the ESAs encourage stakeholders to consider how the approach would achieve the aims of SFDR.

Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

Q1 Insert your responses to the questions in the Consultation Paper in the present response form.

Q2 Please do not remove tags of the type <ESA_QUESTION_ESG_1>. Your response to each question has to be framed by the two tags corresponding to the question.

Q3 If you do not wish to respond to a given question, please do not delete it but simply leave the text "TYPE YOUR TEXT HERE" between the tags.

Q4 When you have drafted your response, name your response form according to the following convention: ESA_ESG_nameofrespondent_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESA_ESG_ABCD_RESPONSEFORM.

Q5 The consultation paper is available on the websites of the three ESAs and the Joint Committee. Comments on this consultation paper can be sent using the response form, via the ESMA website under the heading 'Your input - Consultations' by **1 September 2020**.

Q6 Contributions not provided in the template for comments, or after the deadline will not be processed.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESAs rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESAs Board of Appeal and the European Ombudsman.

Data protection

The protection of individuals with regard to the processing of personal data by the ESAs is based on Regulation (EU) 2018/1725[1]. Further information on data protection can be found under the Legal notice section of the EBA website and under the Legal notice section of the EIOPA website and under the Legal notice section of the ESMA website.

[1] Regulation (EU) 2018/1725 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data, and repealing Regulation (EC) No 45/2001 and Decision No 1247/2002/EC, OJ L 295, 21.11.2018, p. 39.

General information about respondent

Name of the company / organisation	Vanguard Asset Management Limited
Activity	Investment Services
Are you representing an association?	☐
Country/Region	UK

Introduction

Please make your introductory comments below, if any:

<ESA_COMMENT_ESG_1>

A. About Vanguard

The Vanguard Group, Inc. - Vanguard's parent company - was founded in 1975 and is based in Pennsylvania. Vanguard's global assets under management (AUM) were just over €4.8 trillion (as of 31 March 2020).

In Europe, Vanguard has nearly 700 employees based in London, Frankfurt, Paris, Dublin, Amsterdam and Zurich. Further European expansion is a strategic objective for Vanguard. Vanguard's UCITS funds are domiciled in Ireland, with assets under management of just under €130 billion (as of 31 March 2020). Our investors range from direct retail investors to institutional and intermediary investors, such as banks, pension funds, independent financial advisers and discretionary wealth managers.

Vanguard's core purpose is to take a stand for all investors, to treat them fairly, and to give them the best chance for investment success. One aspect that sets us apart from the rest of the asset management industry – and lets us always put investors first around the world – is the ownership structure of Vanguard in the US. Rather than being publicly traded or owned by a small group of individuals, Vanguard is owned by the US mutual funds and ETFs it manages. Those funds, in turn, are owned by their investors, meaning Vanguard is structured as a "mutual" fund company. This unique structure aligns our interests with those of our investors – benefiting investors worldwide – and drives the organisation's culture, philosophy and policies.

Our inspiration is to change the way the world invests. For more than 40 years we have advocated for the Vanguard way of investing – clear goals, balance, low costs, and discipline. These enduring principles have helped millions of people save for retirement, fund their higher education, or buy a new home. The investment industry has followed our lead, resulting in better outcomes for many more investors. Indeed, while investors can't control the markets, they can control the cost of investing. The funds we offer are amongst the lowest-cost funds available in their peer groups; this is not a pricing strategy for us, it is how we do business and is good for the returns of our clients. Vanguard's scale also helps to keep costs low. As our assets increase, we can reduce costs for those that invest with us.

B. Summary of response

Vanguard welcomes the opportunity to comment on the European Supervisory Authorities (ESAs) consultation on draft Regulatory Technical Standards (RTS) under the Sustainable Finance Disclosures Regulation (SFDR). As a fundamentally long-term orientated fund provider, we have every expectation that we will be invested in a company for the long run. As it is our mission to maximise the long-term value for our clients, we have a responsibility to our funds' shareholders to ensure companies take a holistic and long-term view of shareholder value. ESG considerations are an integral part of any such assessment, therefore we believe that they can contribute to long-term investment value and a more sustainable financial system.

However, we believe that any transparency rules should support a holistic view into sustainable practices and pay due consideration to the fiduciary duty of asset managers to their clients. In addition, such rules should take into account the current range and quality of available ESG data so as to ensure that investors are not provided with too complex and/or misleading information. As currently proposed, we believe that the rules for both entity and product level disclosure do not sufficiently take into account the above considerations and instead offer an overly prescriptive approach. Therefore, this is unlikely to be beneficial to retail investors, who are not only our core clients but are also set to be at the centre of the next phase of the EU's Capital Markets Union (CMU).

In addition, we would like to express our concerns with the implementation timeframe of the new rules. We consider the current implementation deadline overly ambitious given that the framework for both entity and produc level reporting will not be finalised before the end of January 2021. Given that SFDR will gradually start applying shortly after, as of 10th March 2021, the industry will only have around five weeks for the legal assessment and subsequent operational implementation of an entirely new and complex framework. We consider this insufficient time, especially as it pertains to obtaining and aggregating the significant volumes of data necessary to comply with the proposed rules. We would therefore like to join industry calls for the existing timeframe to be revisited. Postponing the application date of SFDR will not only provide market participants with a more realistic deadline for implementation but is also likely to result in more regulatory coherence, aligning SFDR with the first batch of the EU Taxonomy disclosures and the new rules on the integration of sustainability risk and into MiFID II, UCITS and AIFM Directives.

Entity-level disclosures

Vanguard believes that the proposed approach to entity-level disclosure is highly prescriptive and unnecessarily granular and thus goes beyond the scope of the Level 1 text. As such, it:

- Does not provide adequate flexibility for firms to define and evaluate their key sustainability risks;
- Is unlikely to provide investors with meaningful and easily comprehensible information; and
- Has the potential to increase the costs of investing.

We have concerns that the new rules would prescribe aggregated scores against indicators that don't necessarily allow firms to make own assessments of how they truly take account of ESG issues into practice, which is the core purpose of the Level 1 text. By having to disclose against such a large number of mandatory indicators, we consider it somewhat impossible to complete the evaluation of key sustainability impacts and risks prescribed by the Level 1 text. In addition, due to the lack of data from investee companies in relation to most of the indicators as well as the lack of a set methodology for calculating some of them, we see a risk of asset managers having to potentially aggregate flawed data, which could mislead investors through the proposed template.

In order to still deliver on the spirit of the Level 1 text, we suggest:

- Reducing the number of the mandatory indicators; and
- Introducing a mechanism for firms to be able to provide an explanation of their (non) assessment of indicators in cases where a quantitative assessment would not be available or useful to investors.

While we agree in principle with the need for consistency and comparability as it pertains to disclosure requirements, we question the usefulness of the proposed template with 32+2 mandatory indicators, both in terms of its relevance and comparability across sectors and strategies. At this stage, we suggest limiting the number of mandatory indicators and revisiting the list as ESG data becomes more reliable and available. As climate indicators are currently the most widely disclosed indicator, we suggest an initial focus on them. This would also allow for further regulatory alignment, in particular between the SFDR and the Taxonomy. In addition, we propose the introduction of a mechanism for firms to explain their approach where a quantitative analysis is either impossible due to lack of data, or not meaningful due to the nature of the investment or the investee company. This will ensure that asset managers are able to quantitatively report on the indicators that they believe are relevant for them to focus on based on their investment strategy and key sustainability risks, and explain why they have not chosen to report other indicators. Having the possibility of adding qualitative assessments would contribute to a more meaningful and genuinely useful picture at the level of the firm.

Product-level disclosure

Vanguard cautions on the use of templates for pre-contractual and periodic product-level disclosure.

While we understand the need to achieve comparability for end-investors, it is unclear whether that can be achieved under the current proposal. In addition to the continued challenges with the data required to complete the templates, we believe the templates should vary by products and ESG strategy type to further support comparability. It is our belief that having detailed templates is unlikely to account for the different product types being offered to clients and might thus lead to a box-ticking exercise, or even, lead investors to believe they are better able to compare when the underlying data is inconsistent. Instead, a prescribed order of the disclosures, as already stated in the RTS, would be our preferred approach.

Should the proposal for templates be adopted after all, we would favour the inclusion of such template in the existing documentation, rather than making changes to existing disclosures within the investment objective sections of the fund documentation. We would also like to point out that the delayed consultation on the mandatory templates for pre-contractual information will only aggravate the challenges with implementation mentioned above.

Further, while the Level 1 text is clear in its differentiation between what qualifies as Article 8 and Article 9 products, we share industry concerns that the RTS, as currently drafted, risk going beyond the requirements of the Level 1 text. We therefore ask the ESAs be clearer in its differentiation between Article 8 and Article 9 products in the context of the RTS.

We also share industry-wide concerns as it pertains the “do not significantly harm” (DNSH) principle as included in the RTS as well as the alignment between the respective requirements under SFDR and the Taxonomy Regulation. In particular, we would be in favour of the ESAs further clarifying the requirements for Article 8 products. In principle, Vanguard does not believe that the application of the Taxonomy concept of the DNSH principle to Article 8 products is fit for purpose as Article 8 products do not have an objective of sustainable investment, as part of the DNSH assessment is determining whether an investment is sustainable.
<ESA_COMMENT_ESG_1>

- **: Do you agree with the approach proposed in Chapter II and Annex I – where the indicators in Table 1 always lead to principal adverse impacts irrespective of the value of the metrics, requiring consistent disclosure, and the indicators in Table 2 and 3 are subject to an "opt-in" regime for disclosure??**

<ESA_QUESTION_ESG_1>
Following careful consideration, Vanguard disagrees with the overall approach taken in Chapter II and Annex I as we consider it to be highly prescriptive and unnecessarily granular. We believe that the current approach goes beyond the Level 1 requirements which leave a certain level of flexibility, especially as it pertains to the number and content of the Principal Adverse Impact (PAI) indicators. The proposed approach also has the potential of not keeping with the spirit of the Level 1 text in that it does not, in fact, support financial market participants to identify and prioritise principle adverse sustainability impacts and indicators (Article 4 (2)(a) SFDR). Rather, its prescriptive nature precludes firms from making their own assessment of adverse impacts in a way that is truly meaningful to how they take account of these issues in practice. Complying with the full list of impacts and indicators laid out in Table I of Annex I, for certain asset classes, will be impossible in practice and potentially misleading for investors. Furthermore, we question whether each of the indicators may be relevant for each company that we invest in. For example, it may not be material or relevant for a technology company to create and disclose a policy on biodiversity, as their business may not have an impact on this environmental aspect. Therefore, while we understand the desire of the ESAs, based on the text of the SFDR, to introduce a set of unified and standardised indicators, we believe that full standardisation and comparability are neither possible, nor desirable.

Second, we believe that the aggregated figure of principle adverse impacts is unlikely to be particularly meaningful due to limitations related to the availability and comparability of the underlying data, particularly due to the use of differing methodologies at investee company level. Investee companies currently do not disclose comprehensively on almost any of the indicators in Annex I, thereby making it unclear what added value aggregation could have. If an investee company does not disclose the data required, asset managers will need to rely on data from third parties as well as make their own assumptions, which may result in serious data reliability issues and unavoidably inconsistent information being provided to end-investors. In addition, some of the indicators ask firms to aggregate the share of investee companies in their portfolios that have a certain policy in place or monitor a certain aspect of an indicator (e.g. Indicator 9: Biodiversity and ecosystem preservation practices, Indicator 11: Deforestation, Indicator 17: Implementation of fundamental ILO Conventions). Although we do recognise the value of having such policies in place, just having them or monitoring a certain aspect of a particular activity does not provide a good view of the quality of that policy or how successful an investee company is at mitigating the assumed adverse impact. It is also our concern that each company may take a different approach to disclosing across the number of these factors which will significantly reduce the ability to meaningfully compare data, even when readily available. This will be further complicated by the fact that the certain indicators will be subject to a qualitative assessment rather than quantitative, making full comparison inevitably imperfect. Consequentially, we would be concerned about inadvertently misleading investors by trying to aggregate underlying data that is not complete or is essentially flawed and as a result misleading them about the comparison across asset manager.

Third, we believe that it is not clear from Annex I what firms should do when they do not have access to all the required data in order to present an aggregated figure. We appreciate the guidance provided by Art 7.2. RTS which says that if indicators are not available, firms would need to provide details on best effort used to obtain the information from companies and, if not available from companies' best efforts used, to asses adverse impacts. Nevertheless, we would support further clarification as to the level of detail and format of such disclosure. For example, it would be helpful to know what type of qualitative information might be appropriate in place of a quantitative figure if asset managers are unable to aggregate data, as well as clear reference to the fact that complying with the legislation is possible, even if a firm is unable to obtain the necessary data for (possibly the majority of) the prescribed indicators.

To avoid the proposed approach turning into a box-ticking exercise, we would suggest the number of mandatory indicators to be reduced to a smaller subset of indictors. These should be determined on the basis of the availability of reliable ESG data and should be meaningful and relevant across different sectors and asset classes. At this stage, we propose an initial focus on climate indicators as these are currently the most widely disclosed indicator. This approach would also allow for further alignment between the SFDR and the Taxonomy (please see our response to Question 5 and 9 for further detail). All remaining indicators currently included in Table 1 should be made optional and moved to Tables 2 and 3, respectively. As data becomes more available and standardised, the set of indicators should be revisited and potentially expanded.

In addition, we propose the introduction of a mechanism for firms to be able to explain their approach where a quantitative analysis is either impossible due to lack of data, or not meaningful due to the nature of the investment or the investee company. This will ensure that asset managers are able to quantitatively report on the indicators that they believe are relevant for them to focus on based on their investment strategy, and key sustainability risks, and explain why they have not chosen to report other indicators or to provide a qualitative assessment instead.

By ensuring that only those indicators that are genuinely meaningful at entity-level are mandatory to disclosure and that asset managers have a mechanism to deal with information which is not easily quantifiable, the ESAs will ensure that the template provides clear and relevant information which allows for a more meaningful understanding of the sustainability characteristics of investment decisions.
<ESA_QUESTION_ESG_1>

- **: Does the approach laid out in Chapter II and Annex I, take sufficiently into account the size, nature, and scale of financial market participants activities and the type of products they make available?**

<ESA_QUESTION_ESG_2>
We would question if the proposed approach sufficiently takes into account aspects related to size, nature, and scale of financial markets participants' activities and the type of products available. In terms of nature in particular, it is our belief that beyond equities and bonds, the framework, as currently proposed, is not applicable to all other asset classes. The current template would put many firms in a position where they have to provide a statement that they take no consideration of sustainability adverse impacts, despite this not being factually true.

In addition, given the fragmentation of the available investee company data and the complexity of needing to aggregate the data at entity level, we see an increased possibility of significant added costs from obtaining the necessary data (please see our response to Question 27 for further detail).
<ESA_QUESTION_ESG_2>

- **: If you do not agree with the approach in Chapter II and Annex I, is there another way to ensure sufficiently comparable disclosure against key indicators?**

<ESA_QUESTION_ESG_3>
As outlined in our response to Q1, we suggest that the number of indicators is reduced and that a qualitative element is added to the entity disclosure template.

We believe that there are currently serious data constraints which make obtaining, aggregating, and comparing all the requested data a potentially counter-productive exercise which might serve professional institutional clients more than their retail counterparts.

It is our belief that retail investors might find the disclosed data confusing and not fit-for-purpose as a result of the one-size-fits-all approach and the sheer length of a report containing 32+2 mandatory indicators. The EU has continuously and successfully worked on simplifying and shortening information documents for retail investors, notably in the area of costs and charges. It is our belief that the same standards should be applied in this area too. The current format runs the risk of potentially overwhelming end-investors who are likely to struggle to understand the implications of the entity-level disclosures for the individual investment in a fund. We therefore believe that firms should report on a limited set of indicators based on availability of data and applicability to a largest number of sectors. It is our belief that an initial focus on climate indicators is the best way forward. All remaining indicators currently included in Table 1 should be made optional and moved to Tables 2 and 3, respectively. As data becomes more available and standardised, the set of indicators should be revisited and potentially expanded (Please see our response to Question 5 and 9 for further detail)

In addition, we suggest the introduction of a qualitative element in the format so as to account for situations where a purely quantitative assessment would not be possible or appropriate. This would allow firms to explain their approach and avoid misleading investors with calculation that may not be reflective of the underlying strategy. It would also contribute to a more meaningful and genuinely useful picture at the level of the firm.

While we remain appreciative of the benefits of having a standardised format for disclosure (i.e. a summary followed by details of the assessment of PAI using a table), our concerns are with the content of the prescribed template. Acknowledging the significant gaps in ESG data availability as well as persistent questions around the quality and comparability of the available ESG data, we ask the ESAs to take account of the fact that the majority of the data currently under consideration is not readily available and may serve to confuse retail investors.
<ESA_QUESTION_ESG_3>

- **: Do you have any views on the reporting template provided in Table 1 of Annex I?**

<ESA_QUESTION_ESG_4>
We believe that the proposed approach is unlikely to provide meaningful data to our clients, who are largely retail investors. This is due to the number of indicators and lack of available data in relation to the indicators. The proposed approach runs the risk of becoming a box-ticking compliance exercise which might serve to confuse retail investors due to the amount and somewhat problematic quality of information provided (please see our response to Question 1, 2, 3, 5 and 9 for further detail).
<ESA_QUESTION_ESG_4>

- **: Do you agree with the indicators? Would you recommend any other indicators? Do you see merit in including forward-looking indicators such as emission reduction pathways, or scope 4 emissions (saving other companies´ GHG emissions)?**

<ESA_QUESTION_ESG_5>
As previously mentioned in our response, we do not think that all 32 indicators included in Table 1 are equally relevant or useful for disclosure at entity level. In fact, it is questionable if we would be able to obtain complete data from our investee companies on any of the indicators at this present time due to the lack of or inconsistent disclosure from investee companies and the lack of standardised methodology used by investee companies. As such, we do not believe that aggregating data will result in reliable or meaningful information for retail investors.

To address these concerns, we would suggest that as a first step, the European Commission and/or ESMA should perform an in-depth analysis as to whether each indicator is available for aggregation. If an indicator is not available for aggregation, it should be removed or ESMA should provide detailed guidance as to how asset managers should report on this in the template, if a qualitative element is not added to the template.

As climate indicators are currently the most widely disclosed indicator in the table, we suggest an initial focus on this. This would also allow for further alignment between the SFDR and the Taxonomy. For example, we believe that the proposed greenhouse gas emissions (Scope 1 and 2) are probably the most widely available indicators. However, should Scope 3 emissions be included, this would make it unlikely that asset managers will be able to provide a reliable aggregate figure for carbon emissions, as this is not a commonly disclosed metric by all companies. Therefore, asset managers might have to rely on third parties to help estimate this data point, which could lead to the proliferation of different methodologies. Similarly, it is unlikely that there would be reliable figures that could be aggregated across all investments in relation to indicators such as waste or energy performance.

As mentioned previously, some of the indicators are focused on whether an investee company has a policy in place. Unfortunately, having a policy does not necessarily equate to effective mitigation of adverse impact – and so we would question whether these are useful indicators of adverse impact. This is particularly true for the indicators on biodiversity, social and employee matters, human rights, and anti-corruption and bribery (Please see our response to Question 9 for further detail).

In addition, not all indicators will be relevant for all companies and sectors. For example, it would not necessarily be relevant for a technology company to create and disclose a policy on biodiversity. Therefore, we would question the value in asking all investee companies for disclosure on this data. Under the current framework, as we understand it, if a technology company does not have a biodiversity policy, then it would contribute to having an adverse impact on the environment and thus increase an asset managers' overall entity-level adverse impact, which would not necessarily be the case.
<ESA_QUESTION_ESG_5>

- **: In addition to the proposed indicators on carbon emissions in Annex I, do you see merit in also requesting a) a relative measure of carbon emissions relative to the EU 2030 climate and energy framework target and b) a relative measure of carbon emissions relative to the prevailing carbon price?**

<ESA_QUESTION_ESG_6>
The current formula includes Scope 3 emissions, which most companies do not currently disclose data on. Therefore, the calculation of the emissions data, as currently outlined in the template, would result in unreliable information once aggregated. As an alternative, we would suggest having a formula in place which refers to international market standards on the calculation of carbon footprint, such as the Task Force on Climate-related Financial Disclosures (TCFD).
<ESA_QUESTION_ESG_6>

- **: The ESAs saw merit in requiring measurement of both (1) the share of the investments in companies without a particular issue required by the indicator and (2) the share of all companies in the investments without that issue. Do you have any feedback on this proposal?**

<ESA_QUESTION_ESG_7>
We believe that introducing these measurements runs the risk of misrepresenting asset managers' contributions to and role in sustainability. By simply relying on quantitative data, these measurements do not take into consideration the role of stewardship and consistent engagement with investee companies.

For example, having a large share of investee companies with a certain issue should not necessarily be presented as negative in its own right. Many asset managers, including Vanguard, will have in place specific engagement strategies to try to encourage investee companies to improve their practices – and therefore, one could argue that, over time, adverse impacts could be reduced. That being said, one should also acknowledge that it is often difficult to attribute change at an investee company to one particular asset managers' activities.

In addition, one should remain mindful of the fact that an asset management company's share of ownership in investee companies is a direct result of underlying investor decisions. Asset managers act as intermediaries on behalf of their clients, which ultimately leaves the final choice of where and how to invest with the end-investor. The product-level disclosures, also mandated by SFDR and addressed in the second part of this consultation, will assist investors in making these determinations, not the entity-level disclosure.
<ESA_QUESTION_ESG_7>

- : **Would you see merit in including more advanced indicators or metrics to allow financial market participants to capture activities by investee companies to reduce GHG emissions? If yes, how would such advanced metrics capture adverse impacts?**

<ESA_QUESTION_ESG_8>
Given the lack of availability for most metrics outlined in the template, we do not believe more advanced indicators should be included, and advocate for the inclusion of fewer indicators, with the ability to provide a qualitative assessment in relation to the indicators. Once more comprehensive and higher quality ESG data is available, this can be revisited (please see our response to Question 5 for further detail).
<ESA_QUESTION_ESG_8>

- **: Do you agree with the goal of trying to deliver indicators for social and employee matters, respect for human rights, anti-corruption and anti-bribery matters at the same time as the environmental indicators?**

<ESA_QUESTION_ESG_9>
In principle, we support the inclusion of social and employee matters as we consider them as relevant as environmental and governance indicators.

However, given that the EU Taxonomy currently focuses on environmental aspects, we would focus on those aspects for the time being until the Taxonomy is further developed to incorporate social issues. The Level 1 text also clarifies that the RTS on the social and employee matters is only due by the 30th December 2021 and we fully appreciate the rationale behind distinguishing between environmental indicators and indicators in other areas as these are relatively new and investee companies have not necessarily dealt with thus far.

As mentioned in our response to Question 5, we find there to be flaws with the indicators already suggested by the ESAs in this area. For an asset manager, the relevant consideration is not whether a company has a certain policy in place but to understand the way the policy is implemented and how effective it is. The risk, for instance, of slavery or human trafficking depends to a large extent on the context the company operates in, including geographical location, the type of industry, and the supply chains used. Indicators cannot apply to all companies in the same manner in the way the RTS suggest. For instance, the absence of a policy against human trafficking in a European tech company would not necessarily mean that the company is engaging in such activities but may simply be the result of it operating in a highly-regulated market and in countries with strong anti-human trafficking law enforcement. Similarly, the proposed indicator on the amount of fines issued to a company for corruption or bribery is dependent on where a company is located. If the company is domiciled in the UA or the EU, one could expect more fines than in developing countries simply because the latter are less likely to have the administrative capacity to prosecute for these issues.

Thus, we think that more consideration should be given to the social and employee matters, before any of the respective indicators are mandatory.
<ESA_QUESTION_ESG_9>

- **: Do you agree with the proposal that financial market participants should provide a historical comparison of principal adverse impact disclosures up to ten years? If not, what timespan would you suggest?**

<ESA_QUESTION_ESG_10>
We would question how useful a 10-year lookback is for investors, in particular for retail clients. We continue to stress that receiving that much information, based on different levels and quality of data, might be overwhelming and confusing for retail investors.

Second, we consider a 10-year stretch is be far too back for the data on these matters to be genuinely meaningful. Given how rapidly the ESG data space is evolving, such a long time span would require drawing comparison between data that is not in fact comparable due to potential differences in the context in which it is gathered or the methodology used for its analysis and aggregation. Instead, it feels more sensible to align the lookback with a more general time period for a performance measure (i.e. 1, 3 (to align it with financial statement) and/or 5 years). The shorter time span will also better reflect the ESG profile of companies in transition.

Third, we believe that absolute figures over a historical period may distort information to investors. Therefore, we would argue that figures should be presented in a normalized format (i.e. indicator per EUR AUM invested).
<ESA_QUESTION_ESG_10>

- **: Are there any ways to discourage potential "window dressing" techniques in the principal adverse impact reporting? Should the ESAs consider harmonising the methodology and timing of reporting across the reference period, e.g. on what dates the composition of investments must be taken into account? If not, what alternative would you suggest to curtail window dressing techniques?**

<ESA_QUESTION_ESG_11>
Currently, the approach set out by the ESAs is overly prescriptive and it is unlikely that most asset managers will be able to report on most of the data outlined in the template anyway. Therefore, we would question the need for additional measures to be put in place at this stage as they might increase the prescriptive nature of the approach.
As outlined in our previous responses, there are significant challenges associated with the implementation of what is already proposed in the RTS and some data will simply not be available. The reporting on some of the existing indicators is unlikely to be uniformly applied, largely due to the fact that some of the indicators require qualitative assessment by each financial market participant. Additionally, flexibility is needed to account for the lack of data available. This could be re-examined as data provision evolves over time and more robust ESG data is available.
<ESA_QUESTION_ESG_11>

- **: Do you agree with the approach to have mandatory (1) pre-contractual and (2) periodic templates for financial products?**

<ESA_QUESTION_ESG_12>
We agree that the interest of ensuring comparability across ESG products is necessary and has merit. However, we believe that the effectiveness of templates will be determined based on its ability to clearly provide investors with the right amount of comparability metrics and the underlying data that supports it. Thus, given the difference in fund characteristics and investment strategies, it is important to provide enough flexibility in disclosures/templates to distinguish amongst different ESG considerations.

While we agree and are supportive of the need to facilitate comparability across ESG products, it is difficult to comment appropriately on the use of templates as they have not been published at this time. However, considering the text of the RTS, which we deem already sufficiently prescriptive, any templates that may seek to standardise disclosures to provide investors with better comparability tools could yield potentially the opposite outcome.

While there is a need for standardisation to compare products, this approach could provide for incompatible comparisons if the template is too prescriptive and standardised. This is mainly driven by our view that the data sourced to provide such comparability is still largely inconsistent (non-standardised) and not widely available, leading firms to use different data sources to complete the templates. This risks undermining the goal of providing comparability amongst products, leading investors to believe that they are more informed when the underlying data is inconsistent or inaccurate. We would encourage the ESAs, in order to fulfil the objective of comparability, to focus on the data that will be necessary to effectively do so.

We also believe that being too detailed provides limited flexibility for firms, keeping in mind the various product types being offered to clients. We thus argue that an overly prescriptive template may lead to a box-ticking exercise, which may not provide any meaningful benefit to investors. While some form of standardisation in disclosures is admittedly needed for investor comparability, which is already offered by the prescriptive text of the RTS with regard to pre-contractual disclosures, such standardisation should not be all-encompassing (i.e. using the same template for all types of products).

Further, we do see a potential risk in using lengthy prescribed templates in pre-contractual documents in that, from an optical perspective, it may suggest to investors that some products / factors / risks / product aspects take precedence over others, noting that all investors have different investment preferences and risk appetites. Therefore, we believe that while a prescribed order of the disclosures would be beneficial for the purposes of comparability, as is already provided for in the RTS, too specific and granular disclosures would be counterproductive.
<ESA_QUESTION_ESG_12>

- **: If the ESAs develop such pre-contractual and periodic templates, what elements should the ESAs include and how should they be formatted?**

<ESA_QUESTION_ESG_13>
If adopted, both pre-contractual and periodic templates should be formatted in such a manner which provides enough flexibility to ensure the information provided allows for a meaningful and relevant consideration of the product being considered by investors.

Among the factors to be considered are:

- Asset class(es) the product invests in (e.g., shares, bonds, real estate)
- Investment strategy employed (e.g., active, passive)
- ESG strategy utilized (e.g., exclusionary screening, integration)
- Other factors which may be pertinent (e.g., constraints, firm-wide policies)

In addition, if templates are introduced for pre-contractual disclosures, the inclusion of such template in the existing documentation is likely the best approach to meet the requirements, rather than making changes to existing disclosures within the investment objective/policy sections of the fund documentation.
<ESA_QUESTION_ESG_13>

- **: If you do not agree with harmonised reporting templates for financial products, please suggest what other approach you would propose that would ensure comparability between products.**

<ESA_QUESTION_ESG_14>
Please see our response to Questions 12 and 13 for our proposed approach.

In addition, we would like to echo industry concerns with the implementation timeline of both the Level 1 text and the RTS in question, especially as it pertains to product-level disclosure for which the templates are yet to be consulted on. If the ESAs publish the final draft RTS by the end of 2020, at the earliest, financial market participants will have a very limited time period for legal assessment and implementation of the new rules. On product-level disclosure in particular, consideration needs to be given to the fact that different regulatory review processes and timelines for updates to the pre-contractual documents exist, depending on the National Competent Authority (NCA) in question, with certain NCAs having a prior review process before offering documentation updates can be effected. The more detailed the templates and disclosures are in terms of content mandated to be included in the pre-contractual documents, the less likely it is that it will be feasible to achieve NCA approval of such revised pre-contractual documentation within the prescribed time period, noting that each NCA will have to review and approve hundreds of prospectuses as part of this process
<ESA_QUESTION_ESG_14>

- **: Do you agree with the balance of information between pre-contractual and website information requirements? Apart from the items listed under Questions 25 and 26, is there anything you would add or subtract from these proposals?**

<ESA_QUESTION_ESG_15>
In general, the information disclosed in the pre-contractual documents should be information that is static and not updated on a regular basis. Depending on the relevant National Competent Authority (NCA), there will be time and costs involved in updating pre-contractual documents, changes to which are subject to a prior review process by many NCAs. We therefore believe that information that should be updated regularly should be shown on the websites rather than the pre-contractual documents. As it pertains to Questions 25 and 26, we would note the following:

- **Environmental or Social characteristics promoted by the financial product:** The descriptions/references noted in this section are relevant for both, however, any graphical representations should be shown on the websites rather than pre-contractual documents for ease of update and where clients would usually go for this information.
- **No sustainable objective**: Consideration should be given to provide more clarity than the current disclosure / text of the RTS. It could be confusing to clients who are looking for ESG products but the disclosure that there is "no sustainable objective" could be mis-construed as meaning there is no legitimate ESG element to such fund. Instead of a negative statement, we would recommend a disclosure that states the fund is an article 8 product and promotes ESG factors / that has environmental and social factors considered vs. an article 9 fund that has a sustainable objective.
- **Investment Strategy**: No concerns.
- **Sustainability Indicators:** We do not believe the data for this is easily accessible and attainable. We would not want this data disclosed on the web or pre-contractual documents if it provides inaccurate or incomplete information. This could be misleading to investors.
- **Use of Derivatives**: We would be in favour of an inclusion in pre-contractual documentation if a negative statement is available and allowable (e.g., fund's derivatives cannot be guaranteed to meet the same environment or social characterises as promoted by financial product) as there are not sufficient ESG derivatives available in the market currently.
- **Website Reference**: No concerns.
- **Reference Benchmark**: No concerns.
- **(Article 9) Objective of a reduction of carbon emissions**: No concerns with including in pre-contractual documents.
- (**Web**) (**not noted below**) - No concerns.
- (**Web) (f) (g) (h) (j) (k)** – Agreed as long as index providers have this information and are able to provide it for public consumption.
- (**Web) (i**) - As long as this is only for funds' objectives that note this strategy, then we would not have any concerns.
- (**Web) 3(a)** - Indicators for adverse impacts should not be included on the web.

<ESA_QUESTION_ESG_15>

- **: Do you think the differences between Article 8 and Article 9 products are sufficiently well captured by the proposed provisions? If not, please suggest how the disclosures could be further distinguished.**

<ESA_QUESTION_ESG_16>
While the text of the Level 1 Regulation is clear in its differentiation between what qualifies as Article 8 and Article 9 products, we share industry concerns that the RTS, as currently drafted, risk going beyond the requirements of the Level 1 Regulation and have possibly introduced a level of ambiguity with regard to the distinction between Article 8 and Article 9 products which didn't exist in the text of the Level 1 Regulation.

In particular, Article 16(2) of the RTS currently requires that for Article 8 products, which invest in a sustainable investment, one must indicate how investments that significantly harm the sustainable investment objectives are excluded. In principle, we don't believe that the application of the Taxonomy concept of "do not significantly harm" (DNSH) to Article 8 products is fit for purpose as Article 8 products do not have an objective of sustainable investment, as part of the DNSH assessment is determining whether an investment is sustainable. As currently drafted, this also has the risk of conflating Article 8 and Article 9 products. We would recommend that Article 16(2) therefore be removed from the RTS and that the RTS does not go beyond what was contemplated in the Level 1 Regulation with regard to Article 8 products. Additionally, it should be clarified that firm-wide ESG characteristics (meaning a simple ESG exclusion(s) or a simple ESG integration) should not by default qualify the product as an Article 8 product.

We therefore request the ESAs to provide further clarity in their differentiation between Article 8 and Article 9 products in the context of disclosures.
<ESA_QUESTION_ESG_16>

- **: Do the graphical and narrative descriptions of investment proportions capture indirect investments sufficiently?**

<ESA_QUESTION_ESG_17>
We would question the suggested description of investment portions and have concerns that this information may not be particularly clear or meaningful for end-investors

If mandated, any such graphical representations, would specify what the fund intends to do, not necessarily what the fund will do. Graphical representation could be misleading if seen as a binding commitment instead of parameters set and should not be required to be set out in a fund prospectus which typically only contains static information given the time and costs involved in updating and issuing prospectuses.
<ESA_QUESTION_ESG_17>

- **: The draft RTS require in Article 15(2) that for Article 8 products graphical representations illustrate the proportion of investments screened against the environmental or social characteristics of the financial product. However, as characteristics can widely vary from product to product do you think using the same graphical representation for very different types of products could be misleading to end-investors? If yes, how should such graphic representation be adapted?**

<ESA_QUESTION_ESG_18>
Yes, we agree that using the same graphical representations across different funds and asset / strategy types would be misleading to end-investors. While potentially beneficial, we believe that there is a need for at least some level of discretion for asset managers.

For certain strategies it may prove difficult, or even meaningless or misleading to include such a graphical representation. For example, in case of an exclusionary approach, a percentage reduction might be a more meaningful representation than a graphical representation. Therefore, further clarification should be provided on how to apply any such graphical illustration for products relying on negative screening.

We would therefore propose less prescriptive requirements and allow asset managers to have flexibility, firstly as to whether to disclose / include a graph, as appropriate for their products, and secondly, if discretion is exercised to include a graph, flexibility as to how that graph is presented.
<ESA_QUESTION_ESG_18>

- **: Do you agree with always disclosing exposure to solid fossil-fuel sectors? Are there other sectors that should be captured in such a way, such as nuclear energy?**

<ESA_QUESTION_ESG_19>

Disclosing exposure to solid fossil-fuel sectors does not raise any materials concerns. We have no further suggestions as to the inclusion of other sectors and would leave any such considerations to the ongoing scientific assessments being performed by the European Commission.
<ESA_QUESTION_ESG_19>

- **: Do the product disclosure rules take sufficient account of the differences between products, such as multi-option products or portfolio management products?**

<ESA_QUESTION_ESG_20>
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<ESA_QUESTION_ESG_20>

- **: While Article 8 SFDR suggests investee companies should have "good governance practices", Article 2(17) SFDR includes specific details for good governance practices for sustainable investment investee companies including "sound management structures, employee relations, remuneration of staff and tax compliance". Should the requirements in the RTS for good governance practices for Article 8 products also capture these elements, bearing in mind Article 8 products may not be undertaking sustainable investments?**

<ESA_QUESTION_ESG_21>
We would not support the inclusion of good governance practices disclosures for Article 8 products, given that Article 8 products are not pursuing an objective of sustainable investment. Additionally, at present, there is no common reference as regards "good governance practices" and governance rules and best practice, along with company law, varies across different jurisdictions. Also, even though quantifiable data on sound management structures is available to a certain extent, data on employee relations, pay for staff, and tax compliance is still largely missing.
<ESA_QUESTION_ESG_21>

- **: What are your views on the preliminary proposals on "do not significantly harm" principle disclosures in line with the new empowerment under the taxonomy regulation, which can be found in Recital (33), Articles 16(2), 25, 34(3), 35(3), 38 and 45 in the draft RTS?**

<ESA_QUESTION_ESG_22>
We share industry-wide concerns as it pertains the "do not significantly harm" (DNSH) principle as included in the RTS as well as the alignment between the respective requirements under SFDR and the Taxonomy. We understand that the consideration of DNSH based on the indicators for adverse impact, proposed in the draft RTS, should apply at the investment, meaning the investee company, level. This is different by the approach taken by the EU Taxonomy Regulation where the consideration is at the level of the economic activity

In particular, Article 16(2) of the RTS currently requires that for Article 8 products, which invest in a sustainable investment, one must indicate how investments that significantly harm the sustainable investment objectives are excluded. In principle, we don't believe that the application of the Taxonomy concept of DNSH to Article 8 products is fit for purpose as Article 8 products do not have an objective of sustainable investment, as part of the DNSH assessment is determining whether an investment is sustainable. We would recommend that Article 16(2) therefore be removed from the RTS and that the RTS does not go beyond what was contemplated in the Level 1 Regulation with regard to Article 8 products.
<ESA_QUESTION_ESG_22>

- **: Do you see merit in the ESAs defining widely used ESG investment strategies (such as best-in-class, best-in-universe, exclusions, etc.) and giving financial market participants an opportunity**

to disclose the use of such strategies, where relevant? If yes, how would you define such widely used strategies?

<ESA_QUESTION_ESG_23>
We believe that from an investor perspective, providing clear definitions for ESG investment strategies would be helpful for investors and would provide firms with a level of certainty as to the type of product. Currently, there is no such consistency in the markets which could sometimes lead to retail investors being offered misleading or potentially confusing definitions. We would, however, stress the need for strategy-neutral descriptions. Otherwise, these descriptions could become too prescriptive and infer that one strategy has more value than another.

Based on our own classification of ESG-related strategies, we believe that the following descriptions could be adopted:

1. **Portfolio screening**
- An active or index strategy that selects from a universe of investments that meet specific screening criteria determined by the investor, a hired asset manager or a separate third party.
- Uses two methods: Exclusionary (negative) screening, which excludes or underweights securities of certain countries or companies based on specific ESG-related criteria; and Inclusionary (positive) screening, which overweighs or only purchases securities of companies with higher ESG ratings than industry peers ("best-in-class") or other investment opportunities.

2. **ESG integration**
- Systematic inclusion of financially material ESG information (risks and opportunities) to complement standard investment analysis. Does not necessarily preclude investment in an organisation or country because of undesirable activity.

3. **Impact investing**
- Targeted investments, often made in private equity or debt markets, with the dual objective of generating measurable, positive societal and/or environmental impact and a level of financial return.

4. **Ownership**
- Use of internal or external resources to positively impact corporate behaviour on ESG-related issues.

<ESA_QUESTION_ESG_23>

- **: Do you agree with the approach on the disclosure of financial products' top investments in periodic disclosures as currently set out in Articles 39 and 46 of the draft RTS?**

<ESA_QUESTION_ESG_24>
We agree in principle with the approach proposed in Articles 39 and 46 of the draft RTS on the disclosure of financial products' top investments in periodic disclosures, and in particular regarding the number of lines to be disclosed. However, we question the choice of 25 top investments as currently the industry standard practice is to disclose top 10 investments. It is unclear whether the extra 15 investments would be helpful to investors or whether they would result in information overload.
<ESA_QUESTION_ESG_24>

- **: For each of the following four elements, please indicate whether you believe it is better to include the item in the pre-contractual or the website disclosures for financial products? Please explain your reasoning.**

1. **an indication of any commitment of a minimum reduction rate of the investments (sometimes referred to as the "investable universe") considered prior to the application of the investment strategy - in the draft RTS below it is in the pre-contractual disclosure Articles 17(b) and 26(b);**

2. **a short description of the policy to assess good governance practices of the investee companies - in the draft RTS below it is in pre-contractual disclosure Articles 17(c) and 26(c);**
3. **a description of the limitations to (1) methodologies and (2) data sources and how such limitations do not affect the attainment of any environmental or social characteristics or sustainable investment objective of the financial product - in the draft RTS below it is in the website disclosure under Article 34(1)(k) and Article 35(1)(k); and**
4. **a reference to whether data sources are external or internal and in what proportions - not currently reflected in the draft RTS but could complement the pre-contractual disclosures under Article 17.**

<ESA_QUESTION_ESG_25>
We have a general preference for website disclosure, especially in cases when information is subject to frequent changes or uncertain in the pre-contractual context at the time of the product launch. As it pertains to the above-mentioned items more specifically, we believe the following:

a) The item should remain in the Prospectus as it's a committed disclosure.
b) The item should be disclosed on the website so that it can be accessed through the web links and thus easy to update.
c) The item should remain on the website.
d) The item should be disclosed on the website

<ESA_QUESTION_ESG_25>

- **: Is it better to include a separate section on information on how the use of derivatives meets each of the environmental or social characteristics or sustainable investment objectives promoted by the financial product, as in the below draft RTS under Article 19 and article 28, or would it be better to integrate this section with the graphical and narrative explanation of the investment proportions under Article 15(2) and 24(2)?**

<ESA_QUESTION_ESG_26>
We do not believe that the use of derivatives should be stated given the lack of ESG specific derivatives. In addition, derivatives use by UCITS is already regulated and dealt with under the UCITS Directive. As such, derivatives should not be singled out in a separate section, as they are an essential instruments of portfolio management and contribute to the liquidity of a security and, in turn, its pricing. Therefore, we would argue that the draft RTS should be amended accordingly with the removal of Articles 14(e), 23(e), 19 and 28, as well as the reference to the use of derivatives in Recital 30.
<ESA_QUESTION_ESG_26>

- **: Do you have any views regarding the preliminary impact assessments? Can you provide more granular examples of costs associated with the policy options?**

<ESA_QUESTION_ESG_27>
Similarly to our position with regards to entity-level disclosure, we would argue that the cost implications related to the implementation of the product-level requirements will be quite significant. These are likely to include the costs for an external counsel, compliance costs, and access to data providers as well as resourcing to address RTS needs. Specifically, we anticipate costs associated with sourcing and processing the data from one or more providers to address the required metrics and disclosures to be fairly significant as internal infrastructures will need to be built to support the on-going reporting requirements. This is also inclusive of additional personnel resourcing that will required to manage, maintain, and oversee the development, implementation, and aggregation of data, among other responsibilities.

As noted previously, both at the entity and product level disclosures, the availability of the data required to complete the disclosure/template requirements are still not widely available. While we are seeing more providers with improved ESG data capabilities, these are often still limited to what is available for consumption by underlying companies. This could be a multi-year effort to have sufficient data across all investee companies. We can concur the sentiment from our peers that the ESAs should consider a more modest, less-prescriptive, approach to implementing these requirements, evolving them over time and them based on investor response. This will enable firms to build the necessary infrastructure and minimise the immediate and significant cost impacts in the near-term.
<ESA_QUESTION_ESG_27>