European Securities and Markets Authority

EUROPEAN BANKING AUTHORITY

EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY

JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

Response form for the Joint Consultation Paper concerning ESG disclosures

23 April 2020

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esma European Securities and Markets Authority · EBA EUROPEAN BANKING AUTHORITY · eiopa EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY · 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:

- contain a clear rationale; and
- 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:

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

- 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.

- 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.

- 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.

- 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**.

- 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	Jeffrey Mushens, Technical Policy Director, TISA
Activity	Non-financial counterparty
Are you representing an association?	Yes
Country/Region	UK

Introduction

Please make your introductory comments below, if any:

<ESA_COMMENT_ESG_1>

TISA, with its members, has been working specifically in this area since early 2019.
We have agreed specific objectives in three areas of work:

- Developing an industry Good Practice Guide, to help firms implement ESG regulations in a sensible, proportionate and compliant way, promoting comparability between products to enable meaningful decisions to be made. We expect publication, for comment by the industry, later this autumn.
- Communicating with Customers, where we are seeking to develop ways of visualising the investment contents of funds and mandates in ways that bring out the contents on an objective basis. These have been developed from consumer research and updated following a Hackathon day earlier this year, involving a wide spread of the industry. Versions have been shared with the UK regulator, the FCA. We should be very pleased to share our work with the ESAs.
- Data standards. Once templates/visualisations have been agreed by the industry, we will promote the development of data standards, probably through FinDatEx, similar to the approach used in developing EMT and EPT, and as proposed for ESG.

Our approach is rooted in empowering retail customers to make decisions on investing in sustainable products based on objective data, so that customer decisions can drive actions by financial firms and the companies in which they invest.

We dislike the approach of Article 8 and Article 9, which are very binary. You are either Article 8, and have a lot of obligations, are you are not. The reality is that products and firms are not binary. There will be a range of sustainability or climate sensitivity or governance or meeting of social objectives in any firm and, hence, in every product. It would be better to try to capture this range than impose a labelling approach, which is why we adopted the approach described above in Communicating with Customers. Slides 25 – 34 in the attached briefing on ESG, given to members earlier this year, brings out our approach. We should be pleased to discuss this with the ESAs in more detail.

<ESA_COMMENT_ESG_1>

Q1 : 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>

We question whether the intention in Level 1 is that there could be so many indicators that all constitute 'principal' adverse impacts as that term appears to imply a list of the most important factors. We recommend a reduced, core list of impacts and some element of discretion on the part of firms. This will be easier for firms, particularly smaller firms, to meaningfully report on.

Furthermore, we feel that the use of quantitative metrics without any context is dangerous. For example, there are financial products that acquire fossil fuel heavy companies with the intention of changing their business model . In abstract, such companies will appear to be making investment decisions that have 'adverse impacts'. The reality is that the adverse impact (the carbon emissions) is happening in any event, but the investment decision has a positive impact.

<ESA_QUESTION_ESG_1>

Q2 : 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>

As outlined under our heading "Proportionality" above, we think there is minimal allowance for the size, nature, and scale of financial market participant's activities and the types of products made available. On the contrary, only the largest and most well-resourced firms are equipped to deal with the burdens introduced by the RTS. A staggered implementation and reduced number of core indicators would be a helpful in this regard.

The draft RTS does not take into account group structures and business models. Our understanding is that small financial market participants have to disclose the PAI statement or an explain statement by 10 March 2021 but large financial market participants have until 30 June 2021, but it is unclear whether in a group structure small subsidiaries can wait for the large parent to publish until 30 June 2021, given that we would expect these small subsidiaries to adopt the parent's policy anyway.

Our member firms are concerned that the proposed requirements do not reflect appropriately the portfolio management of segregated accounts. We understand the arbitrage avoidance reasons for wanting to include these in the definition of "financial product", and firms providing such services in the definition of "financial market participant". However, as drafted the RTS make no allowance for the reality that segregated mandates operate on a significantly different basis to collective funds. As an example, with segregated mandates any sustainability preferences, including negative exclusions, will often be client-led rather than forming a standard element of the 'product', and may not be known at the point the investor becomes a client of the firm. As such, it is not clear how a firm providing a portfolio management service on this basis can comply with the pre-contractual and website disclosure requirements of the draft RTS, which have been drafted on the basis that any sustainable investment approaches are "baked in" to the product.

We would be very pleased to work with the ESAs to produce something that more appropriately reflects the operation of portfolio management services in such scenarios. Given the shortness of time before the SFDR goes live, whilst this is addressed the ESAs should consider removing segregated mandates from the definition of "financial product", and firms providing such services from the definition of "financial market participant", since the alternative is for such firms to be in a position of immediately breaching the RTS requirements when they commence in 2021.

<ESA_QUESTION_ESG_2>

Q3 : 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 indicated above, we would propose a smaller subset of core indicators in the first instance. If necessary, the number of indicators can be built up over time.

We additionally take the view that there can be comparability of key indicators without making them all mandatory disclosures. If the ESAs wish to standardise the presentation of 50+ indicators, that will ensure comparability – but there can be comparability between indicators without every firm using all of them.

Our members have indicated that priority should be given to the indicators that are already substantiated by available data, such as carbon emissions and water emissions.

<ESA_QUESTION_ESG_3>

Q4 : Do you have any views on the reporting template provided in Table 1 of Annex I?

<ESA_QUESTION_ESG_4>

TISA generally supports the use of tools that help to clarify obligations. Templates and specimen disclosures are useful in that regard.

This noted, we think it is most unlikely that these tables will be compared side by side and therefore question whether such a prescribed format is really necessary for comparison. Other prescribed aspects like the length in printed pages seem entirely disproportionate.

Our overarching themes of consumer comprehension, data availability, proportionality and timing are highly relevant here. In a world where many retail investors struggle to engage sufficiently to understand high level critical features of their investments[2] this level of detail is not going to used by retail investors.

In particular, our members would appreciate a more comprehensible summary as to when various obligations become effective.

We do not think the template takes into account group structures and instances wherein a financial market participant has got regulatory permissions to provide portfolio management and investment advice. At the moment, the template only requires LEI of the financial market participant, but our recommendation is that for a group is that this should include all subsidiaries in a group that has adopted the policy and also covered by the statement. We do not see a point for each subsidiary (that is already covered by the regulation) to issue a statement. We also think that if a financial market participant provides portfolio management and investment advice, one template should suffice instead of issuing another statement.

In addition, it is harder to see the relevance of these to existing and prospective clients of a firm providing portfolio management services on a segregated mandate basis, where the construction of individual portfolios is determined by each client's personal requirements, including sustainability preferences and any requirement for negative exclusions. The aggregate data for the indicia in Annex I will not provide an existing or prospective client with anything that can enable a meaningful comparison between firms, and yet impacted firms would still need to go to great lengths and costs to produce the disclosures. Furthermore, the production of the data may prove more onerous to firms providing portfolio management services on a segregated mandate basis, since a significant proportion of new clients will commence the relationship by transferring to the firm his or her pre-existing investment portfolios containing investments that the firm did not itself choose to invest into, which for reasons such as uncrystallised capital gains the firm may need to continue to hold within the client portfolio for a period of time. One member firm managing approximately 30,000 retail investor accounts on a segregated basis reports having over 5,000 different securities held across its portfolio managed segregated accounts such that,

[2] For example, see paragraph 66 onwards of FCA research https://www.fca.org.uk/publication/market-studies/ms15-2-2-annex-3.pdf

like other firms operating on a 'whole of market' basis, it cannot perform its own due diligence on issuers but is entirely dependent on commercial data providers for the production of any the data required by Annex I. The firm in question estimates that this data is not available from the commercial data providers for over 90% of its funds under management, which would render any such tables statistically meaningless, whilst still being costly and resource intensive to produce.
We would ask the ESAs to consider where portfolio managers operating segregated accounts on a whole of market basis should be subject instead to the same obligations as 'advisers' under the draft RTS. This would better reflect the reality that, like advisers, such portfolio managers are themselves users of product data for the products they choose to construct investor portfolios. Or, even better, review the requirements to reduce them to something that is clear and manageable.

<ESA_QUESTION_ESG_4>

Q5 : 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 indicated above, we would propose a smaller subset of core indicators in the first instance – limited to those attributes that are well-defined and measurable. If necessary, the number of indicators can be built up over time.
<ESA_QUESTION_ESG_5>

Q6 : 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>
We can see why policymakers would want firms to disclose this information. However, it appears to be beyond the scope of 'the adverse impacts'. What is proposed would represent benchmarking and is another example of an indicator that is not inherently negative.
<ESA_QUESTION_ESG_6>

Q7 : 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 would reiterate our concern that the disclosures at entity level are removed from their context. Having a high share of companies with a particular issue may just reflect the manager's level of engagement or that they have a particularly large fund that operates in a market where this issue is particularly prevalent. It does not facilitate a fair like-for-like comparison between the responsible investing characteristics of different entities.

<ESA_QUESTION_ESG_7>

Q8 : 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>

As indicated above, we feel that the indicators must be comprehensible to consumers, based on available data and proportionate to the ends in mind. Therefore, at this stage, we would not support more advanced indicators.

<ESA_QUESTION_ESG_8>

Q9 : 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>

We do indeed support this goal. However, we would again refer to our overriding principles of being comprehensible to consumers, based on available data and proportionate to the ends in mind. Until a reliable method for collecting and analysing data is available, firms will have to take a narrative approach of explaining their investment policy with respect to these factors.

<ESA_QUESTION_ESG_9>

Q10 : 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 do not consider that a historical comparison on an aggregated and decontextualised basis gives a useful indication of the financial market participant's progression.

Amplifying the point made earlier about the importance of context, some of our members have explained how the normal ebb and flow of business may be construed as an active, harmful choice by the FMP. For example:

- asset managers often inherit mandates (when taking on a client with an existing portfolio). The portfolio in question may not be very sustainable, but this would not be due to the present manager's investment decisions. While the manager may intend to enhance the portfolio, it may not be in the client's interests to do this immediately. It follows that on an aggregated basis an FMP may be seen to be 'going backwards' just by winning new business.
- a change in business mix (e.g. a growing Emerging markets fund and a shrinking European equity fund) may make it appear that some metrics are getting worse, despite the fact that the metrics for all individual funds are in fact improving due to the manager's actions.

In addition, it is possible (particularly in the early years) for there to be a series of backward steps simply through greater accuracy of the underlying data, for example as the reporting of Scope 3 emissions by issuers improves. Consequently, the presentation of an overly long time series is likely to give a misleading impression to investors.

<ESA_QUESTION_ESG_10>

Q11 : 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>

Our members consider it unlikely that window dressing would be easily achievable.

In keeping with our desire for proportionate measures, there is a strong preference amongst members for 'snapshot' reporting at period ends, rather than weighted average approaches which we believe would significantly increase operational complexity and cost of calculation, while providing at best only marginal gains in accuracy. As such, we do not agree with the proposal for the adverse impact indicators to be calculated over the entire reference period.
We believe that a specific reference date, in this case 31 December, should be used given that in practice investee companies disclose ESG-related information annually and that 'a point in time' reporting is already being used widely by financial market participants in their periodic reports (e.g. best execution annual disclosures).
<ESA_QUESTION_ESG_11>

Q12 : Do you agree with the approach to have mandatory (1) pre-contractual and (2) periodic templates for financial products?

<ESA_QUESTION_ESG_12>
Echoing previous responses, we see merit in the use of templates in choice cases. However, the most important outcome must be the quality of disclosure and this must not be sacrificed in order to achieve uniformity.

The preferred approach should be a description of the disclosure needed with adequate guidance without imposing a rigid framework that will struggle to adequately cater for the full spectrum of options available to investors or require spurious disclosure that is not relevant for a particular product (for example a government bond fund).
We would suggest that the ESAs consider issuing a 'specimen' disclosure rather than a mandatory template. Many FMPs will follow the specimen, but it would allow flexibility for the firms with sensible reasons not to.
In this regard, we draw your attention to the use of industry standard, rather than regulator mandated, Costs & Charges reporting templates. TISA members developed a series of templates for reporting that reflect best practice, meet the requirements of the Directive, enable customers to make meaningful comparisons and are flexible. This is the approach we recommend is adopted.
A copy of v3 of the TISA Approach to Costs & Charges is attached. It is currently being updated, but the updates do not materially affect the templates recommended in the guide.
<ESA_QUESTION_ESG_12>

Q13 : 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>
Please see our comments to Q12.
It is our understanding that the ESAs are proceeding with the development of templates. With our experience we should be very pleased to work with the ESAs. Mandated disclosures can become inflexible and out of date, and are hard to amend, so this should be borne in mind in the work of the ESAs.
Our overriding concern is that the disclosure is comprehensible to end investors. However, the format needs to be proportionate and flexible.
Any template must be conscious of the other information disclosed elsewhere. For example, the interaction between the sustainability-related disclosures and the product's core investment objective, policy and strategy will need to be taken into account. Repetition and inconsistency should be avoided.
Our members are also keen to avoid the creation of additional regulatory documents and therefore would be keen for disclosures to be made in existing documentation.
We would suggest that any template should avoid using any verbatim prescribed text. This tends to be legalistic and is contrary to the industry's intention of making disclosure more meaningful. Moreover, as legal documents, subject to consultation, they can be hard to amend.
<ESA_QUESTION_ESG_13>

Q14 : 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>
We are advocates for competition and recognise the part that comparability features in this. However, we also recognise that investor education, investor comprehension, and product discoverability are critical aspects. We would ask that uniformity be properly recognised as a 'means to and end' and not as an 'end' in its own right.

lTherefore, key to the success of this aspect is how this information can be ingested by distributors and platforms and packaged for easy consumption by investors.
<ESA_QUESTION_ESG_14>

Q15 : 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>
We support the use of websites for lengthy disclosures in order to keep pre-contractual disclosures concise and digestible.

As above, in the case of segregated mandates, any sustainability preferences, including negative exclusions, will often be client-led rather than forming a standard element of the 'product', and may not be known at the point the investor becomes a client of the firm. As such, it is not clear how a firm providing a portfolio management service on this basis can comply with the pre-contractual and website disclosure requirements of the draft RTS, which have been drafted on the basis that any sustainable investment approaches are "baked in" to the product.

It is also unclear in the RTS whether the ESAs expect financial market participants to use a specific classification system (e.g. NACE) in complying with the requirements to disclose the planned proportion of investments in different sectors and sub-sectors. We would welcome a more flexible approach on this with financial market participants deciding what works best for their clients perhaps by aligning sectoral disclosures under the Regulation with existing reporting/disclosures that already provides sectoral information.
<ESA_QUESTION_ESG_15>

Q16 : 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>
This is an area of significant concern. We urge the ESAs and the Commission to issue guidance on the meaning of Article 8. To be more specific, we consider the key issue to be the distinction between Article 8 products and 'everything else' (rather than the distinction between Article 8 and Article 9 products).

We have sympathy that the ESAs are not able to re-write the Level 1 text but as this is a fundamental matter of scope, this may be a case where non-binding recitals (while welcome) are an inadequate substitute for specific interpretation. It is notable that after months of efforts to understand this our members do not feel confident in their obligations and are concerned that relatively minor considerations could 'trip' otherwise standard products into being Article 8 products, moreover that this status could change from period to period.

There is also some concern amongst member firms that if the consequences of a segregated portfolio being classified as an Article 8 product are onerous for firms, and the mere presence of a negative exclusion (for example, no oil companies) is sufficient to cause a portfolio to be so classified, then some firms may cease offering negative exclusion optionality to investors. We believe there is a very real possibility that the draft RTS may have unintended adverse consequences if not carefully calibrated.

We would also appreciate clarification that entity-level exemptions are not automatically deemed as Article 8 products.

Recital 21 provides some form of clarity in terms of what will bring a financial product in scope of Article 8 of the Regulation. We understand from this recital that marketing the consideration of sustainability factors when allocating the capital of a particular financial product will bring this product within Article 8. While this recital is welcomed, we believe that the reference to 'mandatory investor disclosures' should exclude a brief and proportionate mention only in the Prospectus of the sustainability factors considered. This should help avoid a situation where a financial market participant applies an entity level exclusion (e.g. controversial weapons, tobacco) and only mentions this in the Prospectus and becomes inadvertently subject to the requirements for Article 8 products.

<ESA_QUESTION_ESG_16>

Q17 : Do the graphical and narrative descriptions of investment proportions capture indirect investments sufficiently?

<ESA_QUESTION_ESG_17>

We would prefer to defer to consumer research on these questions since, echoing our general themes, investor comprehension is paramount.

Our initial thoughts are that the sub-divisions proposed will rely too heavily on the understanding that the investor brings to bear. These rigid categorisations to not reflect our experience of the sorts of information that investors are interested in.

<ESA_QUESTION_ESG_17>

Q18 : 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>

We believe that a single representation will likely be misleading. This may be the case across product types but also between products of a similar type.

We are concerned about a reductive approach where investors are led to believe that a more widespread screening implies a superior product even if the quality of the screening is poor. We are concerned that graphically depicting the proportion will result in this metric having a greater weight in investor decision making than the more important narrative of what the screening actually covers.

We would favour a simple comparison that indicates the percentage of screening coverage but allows the manager to explain the approach (and perhaps why more widespread screening is not possible).

<ESA_QUESTION_ESG_18>

Q19 : 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>

We appreciate the clarification made during the public hearing that it was never the ESAs intention to exclude non-solid fossil fuels from adverse impact indicators as there are other indicators, which would equally apply to solid and other fossil fuels. However, we still question whether the disclosure required by Articles 15 and 41 of the proposed RTS really provides the intended transparency that consumers require to understand what they are investing in if exposure in fossil fuels will just be limited to solid fossil fuels. We propose that the sectoral disclosure required in Articles 15 and 41 cover both solid and non-solid fossil fuels.

<ESA_QUESTION_ESG_19>

Q20 : 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>

Please see our responses to other questions in respect of the significant problems posed by the draft RTS for portfolio management of segregated accounts.

We would ask the ESAs to consider where portfolio managers operating segregated accounts on a whole of market basis should be subject instead to the same obligations as 'advisers' under the draft RTS. This would better reflect the reality that, like advisers, such portfolio managers are themselves users of product data for the products they choose to construct investor portfolios.

<ESA_QUESTION_ESG_20>

Q21 : 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 consider that a uniform understanding of good governance between Articles 8 and 9 is sensible. However, there remain considerable uncertainties at Level 1 around the implications of a company within a portfolio not meeting 'good governance'. Can a single ineligible investment cause the product to cease to be an Article 8 product etc. This would be a more useful clarification.

There are similar concerns that the proposed requirement will prevent firms from investing in investee companies with historically poor but improving governance practices, for example where the firm adopts an engagement approach to help with the improvement. Such approaches are highly beneficial to sustainability factors and it would seem peverse to prevent their inclusion in Article 8 products.

<ESA_QUESTION_ESG_21>

Q22 : 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 were disappointed that the Taxonomy Regulation incorporated the following mandatory text for Article 8 products in respect of the Do No Significant Harm principle.

'The "do no significant harm" principle applies only to those investments underlying the financial product that take into account the EU criteria for environmentally sustainable economic activities. The investments underlying the remaining portion of this financial product do not take into account the EU criteria for environmentally sustainable economic activities.'

While we recognise that this is not the subject of the consultation, it is important to note that this text is cumbersome and difficult for end investors to understand. Consumers will not recognise the phrase "Do No Significant Harm", they will not understand its implications and will not know whether it is a positive or negative thing that it does not apply.

Our members thought the proposed section "No sustainable investment objective" would be misleading. The products in question have ESG characteristics and, if the distinction to be made is whether the product's investment objective is sustainable investment, then this needs to be made a lot clearer.

Rather than the suggested, prescribed language "This product does not have as its objective sustainable investment", we propose a requirement to explain that the product has some environmental and social characteristics but is not dedicated to a sustainable investment objective. However, we would urge against the use prescribed language, which is unlikely to work on one-size-fits-all basis and has, on occasions in the past, not been written in plain language.

We do not like a binary approach to this, either sustainable or not sustainable, as in reality firms and portfolios will have a range of compliance with sustainable objectives, which customers can be made aware of.

<ESA_QUESTION_ESG_22>

Q23 : 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 would urge the ESAs to recognise the substantial body of work already undertaken by industry in this regard. At this stage, a new series of definitions is unlikely to add value and could be counterproductive. On this topic TISA has itself chosen to refrain from creating new definitions and has instead endorsed the Investment Association's Responsible Investment Framework, as well as adopting a compendium of existing definitions for other terms from other organisations.

<ESA_QUESTION_ESG_23>

Q24 : 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 do not agree with the proposal to disclose the top 25 investments constituting on average the greatest proportion of investments of the financial product during the reference period. We believe that the disclosure of top 25 investments should be at a point in time (e.g. balance sheet date) as this is consistent with how investments are presented in periodic reports where the prescribed template will be inserted.

We understand that the ESAs have concerns regarding 'window dressing'. We believe that this can be addressed by also requiring financial market participants to disclose any material changes in the top 25 investments during the reference period, together with the rationale for these changes.

<ESA_QUESTION_ESG_24>

Q25 : 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.

a) **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);**
b) **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);**
c) **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**
d) **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>

As above, assuming that the ESAs proceed with a mandatory template approach, we support the use of websites for lengthy disclosures in order to keep pre-contractual disclosures concise and digestible. Nevertheless, we disagree with the idea of mandatory templates, as disclosed above.

However, the ESAs should consider whether the information requested would duplicate existing disclosure – e.g. in firms' engagement policies.

We would add that we do not consider element d) to be a useful addition.

<ESA_QUESTION_ESG_25>

Q26 : 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 consider the use of derivatives to be an area that requires significantly more thought.

Use of derivatives to access exposure to a single investment on a 1:1 basis is easily deal with as being comparable with direct investment, but that does not reflect how derivatives are used in practice and derivatives may or may not be involved in the product's environmental or social characteristics or sustainable investment objectives. We would suggest that derivative exposure should be separated from disclosure around direct exposures.

<ESA_QUESTION_ESG_26>

Q27 : 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>
No comment.
<ESA_QUESTION_ESG_27>