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Response to the Joint Consultation Paper by the European Supervisory Authorities in relation to ESG disclosures

Introductory comments and key observations

The Irish Funds Industry Association ("**Irish Funds**") is the representative body for the international investment fund community in Ireland. Irish Funds represents fund managers, administrators, depositaries, transfer agents, professional advisory firms and other specialist firms involved in the international fund services industry in Ireland. Net assets of Irish domiciled investment funds stand at EUR 3,024 billion (source: Central Bank of Ireland, June 2020), representing approximately 17% of total net assets of European investment funds (source: EFAMA, Q1 2020).

Irish Funds is supportive of the goals of the EU's Action Plan on Sustainable Finance and is actively engaged on the sustainable finance agenda. We are keen to ensure that industry is well positioned to rise to the challenges and harness the opportunities that the sustainable finance agenda presents. We fully recognise the need for and benefit of a regulatory framework in order to ensure appropriate standards and a level playing field that achieves the intended goals regarding sustainability, while protecting end investors from 'greenwashing'. A clear, effective and well-sequenced implementation of the new EU sustainable finance regime is central to the success of EU's Action Plan on Sustainable Finance. We commend the ESAs on the extensive and valuable work that has been rapidly progressed in order to fulfil the ESAs' mandate under the Level 1 text of the Sustainable Finance Disclosure Regulation ("**SFDR**") to provide the Regulatory Technical Standards ("**RTS**") necessary for implementation. We welcome the opportunity to respond to the specific questions on the proposed RTS in the Consultation Paper. We have a number of key observations regarding the overall approach to implementation of the SFDR which we would like the ESAs to consider, in addition to some points that do not fall neatly within the response to the specific questions the ESAs have asked:

- **Principal Adverse Impacts Statement**

  Achieving intended objectives with meaningful disclosure at entity level

Building on SFDR Level 1, we agree with the ESAs' ultimate objective in approaching ESG disclosures to ensure that they enhance comparability (of financial products), reduce information asymmetries vis-à-vis end investors and provide meaningful and comprehensible information for consumers in order to enable them to make informed decisions. In doing so, the ESAs have emphasised avoiding excessive disclosure with a focus on simplicity. We also understand that under the Level 1 text, disclosure is required as to how financial market participants ("**FMPs**") approach sustainability and identify and deal with principal adverse impacts. Bearing this in mind, conceptually, we have identified some challenges with the proposed template for the Principal Adverse Impacts ("**PAI**") Statement at Annex I of the Consultation Paper.

By mandating 34 PAI indicators for completion (often to be expressed using two different metrics), we are concerned that end investors could be overwhelmed with data points that will not enable them to make informed decisions on either individual financial products or the FMPs themselves. Our understanding of SFDR Level 1 is that FMPs are required to identify, prioritise and disclose any PAIs and explain what actions they are taking to address these. This lends itself to a more qualitative, principles-based approach with a focus on a smaller range of universally applicable indicators. Since the PAI Statement will be provided at the entity level, the disclosure must be relevant to that level. In our view, many of these indicators could only serve a meaningful purpose at the product level whereas aggregating this data at the entity level could create confusion. The PAI Statements cannot serve as an effective comparison of individual products and if end investors try to use them in this way it will be misleading, since the aggregated indicators will not be a true representation of the sustainability profile of any individual product. For the PAIs to be useful, they need to contain only information that is relevant at the entity level and that can serve to meaningfully compare the approach and performance of FMPs in that regard.

PAI assessment and materiality

The ESAs have provided a helpful catalogue of all the possible PAI indicators. However, referring back to SFDR Level 1, we fail to see how FMPs will be able to effectively identify, prioritise and disclose on their relevant PAIs if the majority of the indicators are deemed mandatory. This omits an application of the concept of materiality that is central to existing international best practice in sustainability reporting. Consequently, we have concerns that this will lead to a checkbox style approach to sustainability on the part of FMPs and NCAs without requiring regulated entities to adequately focus on their real adverse exposures. We would not consider that any positive value for any of the adverse impact indicators automatically results in a *'principal'* adverse impact. This removes the intended responsibility of the FMP to conduct the assessment, disclose on that process and report on its identified '*principal'* adverse impact based on what impacts are "material or likely to be material" as per Recital 18 of the SFDR.

Alignment with the Taxonomy Regulation and EU policy goals

We are also concerned about a lack of alignment between the proposed approach and the 'Do no significant harm' ("**DNSH**") requirement under the Taxonomy Regulation, which embeds a concept of materiality. Since the Taxonomy will set the standard for economic activities and investments that are deemed 'sustainable', the PAI Statement should not apply a divergent and more granular and onerous approach than it.

We fully agree with the ESAs that the relationship between the concepts of DNSH and principal adverse impact requires clarification. However, while the ESAs have suggested that this is something that the Commission might look at in the future, we see the clarification as necessary during the implementation phase of the EU sustainable finance regime in order to ensure a coherent regulatory framework that works for all stakeholders concerned. We would like the ESAs to consider further the possibility of aligning DNSH and PAI assessments under the SFDR with the existing DNSH criteria for environmental objectives and minimum social safeguards in the Taxonomy. In particular we would like the ESAs to reflect the materiality concept contained in Recital 18 of the SFDR in the PAI and use the RTS as an opportunity to address misalignment to the extent possible within the ESAs' mandate.

Data challenges

The challenge associated with data gaps and sourcing reliable, comparable and publicly available ESG data is well acknowledged, including by the European Commission, as well as the ESAs. We have major reservations over whether the data points could be effectively completed by FMPs in time for compliance. Compliance with such a wide range of data points would be required in advance of the envisaged update to the Non-Financial Reporting Directive ("**NFRD**") that is intended to set a new standard for consistent, reliable and audited sustainability reporting. In the absence of publicly available sustainability data, we understand that the ESAs want to drive the market to deliver these new data points. This, in essence, means sourcing the data on a 'best efforts' basis from sustainability reporting vendors.

We have undertaken a survey of data vendors (full results provided in response to Question 1) and the responses from the vendors themselves reveal that data in respect of 16 of the 32 'principal' indicators will be difficult to provide and a further 8 will be very difficult for them to provide, based on the responses of the vendors. Of the 18 'additional' indicators, 1 is difficult and 13 are very difficult. Acquiring such data is expensive and the more complexity associated with the data point, the greater the cost, which will disproportionately impact on smaller FMPs. In the absence of an EU public data register and an update to the NFRD, we envisage that the costs will be prohibitive for many FMPs.

Furthermore, in a demonstration of concerns about the consistency and therefore reliability of the data from the different vendors, our survey revealed a high level of consensus among the vendors on just 6 of the indicators. The reliability and consistency of the data reporting to clients will be in question and results could potentially be misleading. It is probable that a high number of data points would be provided by a small number of vendors, which will increase their ability to charge significantly for such data in a heavily concentrated market.

Need for a targeted approach to PAI reporting

All of these factors point to the need to rationalise the range of mandatory data points to make the completion of the PAI Statement feasible, as well as targeted and meaningful, at entity level and for end investors as well as supervisors. We have set out our proposals in that regard in response to Question 3.

Finally, we do not think it is realistic to expect that actions taken during the reference period will have such an immediate effect in terms of reducing any adverse indicators. The focus will be on a multi-year transition in keeping with existing stewardship codes and best practice.

- **Timeframes for compliance and overall coherence with the EU sustainable finance regulatory regime**

We share the concern expressed by the ESAs in your letter to the European Commission dated 28 April 2020 regarding the condensed timeframe for compliance following adoption of the RTS. The ESAs have now advised the Commission of the intention to deliver the RTS by the end of January 2021. The Commission will then need to consider and adopt the RTS, which will leave a matter of weeks to comply before the SFDR applies on 10 March 2021. This situation is clearly not tenable and we support the ESAs in requesting an appropriate delay to allow FMPs and NCAs sufficient time to properly implement the provisions in the RTS.

Like the ESAs, we recognise the strategic importance of sustainable finance and the ambition to introduce policy measures on disclosure as early as possible. Accordingly, we want to be ambitious but also realistic in relation to the compliance timeframes in order to ensure an orderly, well-sequenced and well-coordinated implementation. In this regard, we propose to progress with compliance by 10 March 2021 where it is possible to do so but to defer compliance in relation to obligations that rely on the final RTS being in place. Additionally, we think it makes sense to coordinate compliance timeframes with related and pending regulatory requirements, such as the disclosure requirements under the Taxonomy Regulation.

The ESAs will be aware that the substantive organisational level requirements to integrate sustainability risks will likely take effect by the end of 2021 based on the current timeframes, with the Commission having recently published the draft Delegated Acts. Sequentially, from this perspective, again it would again make sense to align SFDR obligations to a 1 January 2022 to the extent possible.

Managing the orderly updating of prospectuses under SFDR and the Taxonomy Regulation

Interaction with the Taxonomy Regulation is also an important aspect to consider when planning for compliance with disclosures relating to the Article 8 ("**Light Green**") and Article 9 ("**Dark Green**") products, as prospectuses would need to be reopened after updating for the SFDR in order to take account of these additional product disclosures. Industry, NCAs and end investors are therefore facing the prospect of having prospectuses updated multiple times in the one year to meet with the new requirements. Logistically, we are uncertain as to how NCAs plan to review thousands of prospectus updates within such tight timeframes. In addition, it is conceivable that some of these prospectus updates may require shareholder approval, which would also need to be factored into the review process from a timing perspective. Barring a delay, market participants and NCAs could have little over one month in which prospectuses have to be updated, submitted, reviewed and approved under the SFDR by 10 March 2021. Furthermore, we do not think it would be a good outcome for end investors if they will be receiving multiple versions of documents or if documents they have seen before will be constantly updated.

We understand that it is envisaged to finalise the Level 2 text under the Taxonomy Regulation by mid-2021. It makes sense from a practical perspective to coordinate the timeframes for the filing of the prospectus updates so that both the SFDR and Taxonomy updates can be filed and reviewed at the same time. Doing this under a proposed new compliance timeframe of June 2021 in respect of the SFDR would not work because while the SFDR updates would need to take effect, sufficient time needs to be allowed for completion and adoption of the Taxonomy Level 2 texts. An NCA is unlikely to approve a prospectus until the applicable legislation is legally adopted and in effect. It is also important that the sale of products and the effective operation of the market is not hindered while awaiting prospectus updates. Therefore, logistically it makes sense to defer the timeframes for compliance with prospectus updates until 1 January 2022 to align with the application of the Taxonomy Regulation. Such an approach will not only ensure a more realistic and workable updating and approval process for NCAs and FMPs, but would also minimise disruption to and the possibility of confusing consumers who will otherwise receive multiple updates to documentation in the space of a year.

Our proposals on the SFDR compliance timeframes

Taking the above challenges into account, while also cognisant of the sense of urgency related to the implementation of the SFDR, we propose the following timeframes as a pragmatic way forward:

- Publication of policies on the integration of sustainability risks in the investment decision-making process and in investment advice (Article 3) by **10 March 2021** (no change)
- Transparency of adverse sustainability impacts at entity level (Article 4) by **1 January 2022**
- Transparency of remuneration policies in relation to the integration of sustainability risks (Article 5) by **10 March 2021** (no change)
- Transparency of the integration of sustainability risks in pre-contractual disclosures (Article 6) by **1 January 2022**
- Transparency of adverse sustainability impacts at financial product level (Article 7) by **30 December 2022** (no change)
- Transparency of the promotion of environmental or social characteristics in pre-contractual disclosures (Article 8) by **1 January 2022**

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- Transparency of sustainable investments in pre-contractual disclosures (Article 9) by **1 January 2022**
- Transparency of the promotion of environmental or social characteristics and of sustainable investments on websites (Article 10) by **1 January 2022**
- Transparency of the promotion of environmental or social characteristics and of sustainable investments in periodic reports (Article 11) (**see below request for clarification on timeline**)
- Review of disclosures (Article 12) by **10 March 2021** in respect of Articles 3 and 5 (no change)
- Article 13 on marketing communications by **10 March 2021**

- **Approach to pre-contractual disclosures**

That the planned templates regarding pre-contractual disclosure have been delayed and will not be consulted on until September 2020 is also a point of major concern to industry in seeking to plan and prepare for implementation. We understand the rationale for templates to foster consistent, concise and comparable disclosure. On that basis we are not opposing templates but note that in keeping with the approach taken in a prospectus, it would be more appropriate for the pre-contractual templates to be qualitative, rather than quantitative in nature and take a narrative, rather than a data focussed approach. Furthermore, any templates need to be sufficiently flexible to allow for each FMP to emphasise the most material sections for that particular product. The more complicated and data driven the templates, the more challenging they will be to implement on time, compounding the timing challenges related to prospectus updates outlined above.

- **Clarifying the distinctions between product categories**

We note that one of the key objectives of the SFDR is to prevent ‘greenwashing’. It would be an unusual outcome running counter to this objective if certain non-ESG funds ended up having to be categorised as Article 8 products because of basic ESG integration or exclusion approaches, based on either i) fulfilling legal obligations or ii) firm-wide ESG policies. We would welcome confirmation to that effect and a clear distinction to be drawn between Article 8 products and non-ESG products as set out in our response to Question 16.

In relation to the distinguishing between Light Green and Dark Green products, we are seeking two important amendments in the draft RTS. Firstly, we do not think that the proposed product disclaimer under Article 16(1) of the draft RTS is appropriate for Light Green products that are deemed a valid ESG product category under the SFDR, with extensive conditions applying to them. We think that this statement is likely to confuse consumers who may not fully appreciate the nuances of related legal definitions. Therefore, we ask that this statement not be required.

Secondly, we do not think that the breakdown of 'sustainable investments' as defined under the SFDR should be required in respect of the Light Green products under Article 15(2) of the draft RTS. Such products are not necessarily targeting those investments and this requirement could serve to blur the distinction between the two product categories. We also note that there are already very similar requirements relating to a breakdown of Taxonomy-compliant activities for Article 8 products and presenting two similar breakdowns based on different assessment frameworks will confuse end investors. Therefore, we ask that this requirement be deleted.

- **Periodic reports**

  We would like to seek clarification with respect to the commencement of the periodic reporting requirements under Article 11 for investment funds with different year-ends. Recital 32 states *"Since annual reports in principle summarise business results for complete calendar years, the provisions of this Regulation regarding the transparency requirements for such reports should not apply until 1 January 2022"*. We view the aforementioned as meaning that the relevant disclosures will be required in annual reports for annual reporting periods commencing *on or after* 1 January 2022. This would be consistent with the conventional approach taken in accounting relating to such application dates, to ensure that the disclosure covers an entire reporting period.

  To view this statement otherwise would mean retrospective application of the SFDR. For example, for a fund with a year-end of 31 December, the annual report issued at the beginning of 2022 will cover the period from 1 January 2021 to 31 December 2021, so three months prior to the application of the SFDR. Investment funds can have different year-ends, so for funds with year-ends in July or September for example, the situation will be even more acute.

  Furthermore, the requirement to include a statement in the annual report noting the availability of information relating to PAIs (see Article 7(b) of the SFDR) does not apply until 30 December 2022. In the periodic reports for Article 8 and 9 products, there is reference regarding the Annex I indicators and how these indicators have been considered. By applying 'annual periods beginning on or after 1 January 2022' as the interpretation, we are ensuring that the requirement under Article 7 is also effective before FMPs start reporting on consideration of adverse indicators in periodic reports.

We would welcome the opportunity to discuss these matters further with you.

Adverse impact indicators

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?

We do not agree with the proposed approach. While it is useful to provide a comprehensive catalogue of sustainability indicators, it would not be an accurate reflection if any positive value for any of the adverse impact indicators in Table I automatically leads to a 'principal' adverse impact. By definition, not every adverse impact can be 'principal'. We do not believe that this will provide meaningful disclosure regarding PAIs and will instead result in information overload for end investors and a "check box" type approach for compliance with and supervision of sustainable finance regulatory requirements.

Application of materiality

Materiality is key to assessing whether a principal adverse impact has actually occurred. The concept of materiality is central to existing best practice in international sustainability reporting frameworks and helps guide producers and users of financial and non-financial information in identifying key risks and exposures and disclosing on and addressing these.

It is also important to consider best practice with regard to sustainable investing and refer back to the Level 1 text, both of which embed the concept of materiality and focussed assessment and action with regard to sustainability impacts. SFDR refers to effects on sustainability that are "material or likely to be material" (Recital 16, Recital 18, Recital 23 of SFDR). Article 4(2)(a) refers to "*the identification and prioritisation of principal adverse sustainability impacts and indicators*". The Level 1 text therefore makes clear that the FMP should have an assessment process in place to identify and prioritise indicators and meaningfully disclose on any principal adverse impacts, as opposed to disclosure on a very wide range of indicators that may not be relevant and for which there is no materiality threshold. This will lead to a less focussed and less meaningful approach as the ability for an FMP to prioritise has effectively been removed. Applying materiality will assist in removing the potential for the ESG disclosures to become a box ticking exercise

Furthermore, the indicators chosen do not necessarily demonstrate adverse impacts. For example, the existence of a deforestation policy is not material for all sectors/asset classes. But even for those to which it is relevant, the existence of a deforestation policy does not indicate whether it is effectively implemented, just as the lack of a deforestation policy does not demonstrate that deforestation takes place. Even for sectors where such issues are material, policies can indicate appropriate governance, but do not demonstrate the lack of adverse impact.

Best practice in sustainable investing

Further to the above, we think that the RTS need a stronger focus on the processes in place to identify and manage adverse impacts, consider how this is monitored, and how to address adverse impacts that are identified, including using investor rights to prevent or mitigate against such impacts. This will encourage asset owners to act as responsible stewards of the assets in which they are invested and drive change in the real economy, which is more impactful and a crucial part of sustainable investing. FMPs need to be able to contextualise metrics on adverse impacts with a broader view of investor impact (as per the OECD guidelines on responsible business conduct for institutional investors) that includes how FMPs use influence to mitigate impacts – impacts (positive or negative) are not just captured by aggregating investee data. There needs to be a broader consideration of investor stewardship and advocacy activities.

Meaningful disclosure at the entity level for end investors

The PAI Statement at Annex I relates to an entity level disclosure. However, many of the indicators specified as mandatory are relevant only for specific products or asset classes. While some of these indicators could be usefully compared across similar types of products to help end investors make a comparison, their aggregation at entity level does not lend itself to enabling end investors to make an informed decision on any product, as the specific approach of each product is masked by the aggregation. Much of the aggregated indicator data at entity level will likewise not be useful in comparing the ESG approach or performance of different FMPs. We are concerned that presenting such a vast amount of mandatory indicator information (typically under two separate measures) in this way could overwhelm and confuse end investors, potentially leading them to make erroneous judgements on the sustainability profile of financial products and FMPs.

The Level 1 text refers to disclosing in “qualitative or quantitative terms” but the qualitative aspect is less reflected in the proposed approach which primarily relies on a very wide list of indicators. Since the PAI Statement will be provided at the entity level, the disclosure must be relevant to that level. Our view is that disclosure at this level lends itself to a more qualitative, principles-based approach with a focus on a smaller range of universally applicable indicators. As we have set out in our introductory remarks, we are concerned that this approach could undermine the ESAs’ ultimate objective of providing clear, concise, relevant, comparable and meaningful information to consumers to enable them to make informed decisions.

Need for alignment with the Taxonomy Regulation and policy goals

Additionally, we see a lack of alignment in this approach with the Taxonomy Regulation and EU policy goals on carbon transition. In terms of approach, the Taxonomy Regulation focusses on the environmental performance of the underlying activity, giving flexibility to the discloser to reference the investment approach used to improve the underlying performance. The approach to DNSH under the Taxonomy Regulation provides for the application of materiality. The focus is on ‘significant’ harm (similar to ‘principal’ adverse impact) and the Technical Expert Group (“**TEG**”) to the Commission proposed technical screening criteria that contain quantitative thresholds where possible in order to create a focussed approach. It is important that FMPs are able to contextualise the metrics, for example where adverse impacts are as a result of enabling activities. The approach taken in the draft PAI disclosures, where any positive value on the wide range of indicators is a principal adverse impact, is at odds with the Taxonomy, where specific thresholds are set for what counts as significant harm in the context of the economic activity. If the Taxonomy were to take the same approach as the RTS and consider any positive value for any of these indicators as material and therefore doing ‘significant harm’, this would exclude the majority of even the most ‘green’ economic activities from the Sustainable Finance Taxonomy.

It does not appear consistent to apply a more onerous standard to the entire investment world than that applicable under Taxonomy, which is intended to set the standard for ‘sustainable investment’. From a policy perspective, we understand that the EU wants to facilitate a largescale transition to a low carbon or carbon neutral economy and mainstream sustainability in financial services. We are concerned that approaching the PAI assessment in this way could undermine that ambition by disincentivising asset managers from investing in companies that need to finance their transition, thereby making sustainable finance too ‘niche’. We think that this inconsistency needs to be addressed.

Data challenges with the proposed approach

Aside from the issues we have raised above in regard to the conceptual approach, we would also like to highlight very significant issues with the provision of the proposed data in order to fulfil the requirements of the proposed 50 indicators. As the ESAs are aware, there will be numerous data gaps in relation to the proposed indicators and the NFRD is currently being reviewed to provide a harmonised framework to develop high quality, reliable, comparable sustainability data that we have proposed be made publicly available. Ideally it would be best to wait for the NFRD to catch up before FMPs would need to complete such an array of indicators (even at product level where many of them would be more relevant). It should at least be ensured that the NFRD reform will include the data points required for FMPs to disclose against any mandatory PAI indicators. In the absence of a common reporting standard and publicly available data, FMPs' needs will have to be met by vendors in the market with attendant costs, quality, reliability and comparability issues occurring for indicators that will not always be relevant or material to FMPs as part of their PAI.

We are aware that the ESAs want the market to rapidly evolve in order to provide the underlying data. We note that the ESAs suggest sourcing the data directly from issuers in the first instance if the data is not disclosed publicly, and if this fails then FMPs should use third parties. However, we would suggest that the level of data to be sourced in this way will place an unreasonable burden on both the investee companies and FMPs.

It is often not feasible for FMPs to collect data directly from companies due to capacity and associated costs, particularly for smaller FMPs. Moreover, it is easier for companies to provide data to a limited number of data vendors over having to respond to multiple due diligence questions from different FMPs. Information sourced from third-party data providers can only fall within the 'best efforts' standard required under the RTS. Sourcing data on the private market will present challenges (availability, costs, quality, reliability and comparability) that are unlikely to be overcome – hence the EU has recognised the need to update the NFRD in the first instance and develop a common reporting and assurance standard in this area.

We approached seven of the leading ESG data vendors and asked them to rate the 50 data points listed on the proposed harmonised reporting template as to the level of difficulty in producing the data. Four of the data vendors responded and we have used their feedback to inform our responses. Additionally, we sought to ascertain the level of vendor consensus around the data points, i.e. the extent of variability in feedback from data vendors in respect of each data point. These private market vendors are commercially motivated to provide

ESG data that they can sell where possible and yet the level of difficulty they report in being able to meet these requirements is instructive.

The responses from the vendors themselves reveal that 16 of the 32 principal indicators will be difficult to provide and a further 8 will be very difficult for them to provide, based on the responses of the vendors. Of the 18 ‘additional’ data points, 1 is difficult and 13 are very difficult. Of the PAI mandatory indicators relating to climate and environment, only 1 (biodiversity) can be provided with relative ease, according to the vendors. The situation is comparably better in relation to the social indicators, 7 of which can be provided with relative ease, according to the vendors. However, 4 of the social indicators are considered very difficult to provide.

Acquiring such data is expensive and the more complexity associated with the data point, the greater the cost, which will disproportionately impact on smaller FMPs. In the absence of an EU public data register and an update to the NFRD, we envisage that the costs will be prohibitive for many FMPs.

Furthermore, in a demonstration of concerns about the consistency and therefore reliability of the data from the different vendors, our survey revealed a high level of consensus among the vendors on just 6 of the indicators. In the absence of a common reporting standard with audited data, the reliability and consistency of the data reporting to clients will be in question and results could potentially be misleading. Furthermore, it is probable that a high number of data points would be provided by a small number of vendors, which will increase their ability to charge significantly for such data in a heavily concentrated market. This points to using a smaller range of mandatory indicators if completion of the PAI Statement is to be feasible in addition to being material and therefore meaningful, as per our earlier comments above.

The results of the findings to our survey of ESG data providers are set out in the table below.

‘Principal’ climate and other environment related

	Data Point type	Level of difficulty [1]	Vendor consensus [2]
1	Carbon emissions	Difficult	Low
2	Carbon footprint	Difficult	Low
3	Carbon intensity	V difficult	Low
4	Solid fossil fuels	Difficult	Medium
5	Non-renewable energy	Difficult	Low
6	Energy consumption	Difficult	Low
7		Difficult	Low
8		Difficult	Low
9	Biodiversity ecosystem	Easy	High
10	Protected species	V difficult	Low
11	Deforestation	Difficult	Low
12	Water emissions	Difficult	Medium
13	Water stress	V difficult	Low
14	Waste water	Difficult	Medium
15	Hazardous waste	Difficult	Medium
16	Non recycled waste	V difficult	Low

‘Principal’ social and employee, respect for human rights, anti-

	Data Point type	Level of difficulty [1]	Vendor consensus [2]
17	Individual rights of work; Labour rights & standards; Equal treatment; Job security	Easy	High
18	Gender pay gap	V difficult	Low
19	Compensation ratio	Difficult	Low
20	Board gender diversity	Easy	Medium
21	Whistleblower protection	Easy	Medium
22	Workplace accidents	Easy	High
23	Human rights	Easy	High
24		Easy	High
25	Human trafficking	Difficult	Low
26	Child labour	Difficult	Medium
27	Forced or compulsory labour	Difficult	Medium
28	Human rights	V difficult	Low
29	Weapons controversial	Difficult	Medium
30	Anti corruption & bribery	Easy	High
31	Anti corruption & bribery	V difficult	Medium
32		V difficult	Low

‘Additional’ environmental and social indicators

	Data Point type	Level of difficulty [1]	Vendor consensus [2]
33	Inorganic pollution	V difficult	Low
34	Air pollution	V difficult	Low
35	Ozone depletion substances	V difficult	Low
36	Carbon emission reduction	Easy	Medium
37	Water usage	V difficult	Low
38	Water recycled	V difficult	Low
39	Water management	Difficult	Medium
40	Land degradation	V difficult	Low
41	Sustainable land	V difficult	Low
42	Sustainable oceans	V difficult	Low
43	Securities not green	V difficult	Low
44	Accidents	V difficult	Low
45	Injuries	V difficult	Low
46	Supplier code of conduct	V difficult	Medium
47	Grievance/complaints	V difficult	Medium
48	Discrimination	V difficult	Low
49	CEO/Chair segregation	Difficult	Medium
50	Securities not certified as social	V difficult	Low

1 "Level of difficulty": Data vendors' assessment about data sourcing difficulty for each data point

2 "Vendor Consensus": Extent of variability in feedback from data vendors for each data point

Source: Survey of ESG data vendors by Irish Funds ESG Data Workstream, June-July 2020

2 **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?**

No, we do not consider that the proposed approach sufficiently takes into account the size, nature, and scale of FMPs' activities and the type of products they make available. We base our response on the following reasons:

Meaningful disclosure for diverse portfolios will be lost

As we have stressed in our response to Question 1, aggregating data from different underlying portfolios to provide indicators at the entity level will not be beneficial in assessing the PAI of any particular financial product. Fund managers will frequently manage a wide range of investment funds, which could for example include ESG themed and ESG impact funds, traditional broad based equity and bond funds, ETFs, money market funds, as well as the alternative asset classes, including hedge funds, private equity and real estate. It would not be uncommon for large fund groups to encompass all of these kinds of assets and strategies. Each of these different types of funds will have their own sustainability profile, which will vary greatly, for example the PAI of an ESG impact fund will be very different to that of a fund invested in energy or mining. These insights are lost when the PAI is aggregated and calculated across the business and therefore the approach taken loses meaning at the entity level.

A completely standardised approach cannot be applied for different types of products, strategies and investments

Indicators proposed by the ESAs will be relevant at the product level but their applicability to any given portfolio will vary greatly. For example, deforestation and biodiversity loss is more relevant for certain industries and geographies than others. The relevance of the indicators for products that invest in manufacturing industries will be very different than for those that invest in services. The absence of a sense of real or material impact compounds the issue – lacking a policy for deforestation is taken as an adverse impact, even when this is a result of immateriality, rather than an indication of actual adverse impacts, i.e. deforestation practices.

We welcome the clarification given by ESMA at the Open Hearing on 2 July 2020 that it is not mandatory to disclose on all of the indicators for every product. This acknowledgement of relevance and materiality at the product level also needs to be further acknowledged at the entity level.

We also welcome the clarification at the Open Hearing that the FMP could indicate a score of zero against an indicator it has deemed irrelevant. However, what has not been clarified is the ESAs' expectation in relation the level that will be required before an FMP can conclude that an indicator is not relevant. For example, for investee companies that are part of a wider group, is it enough to just look at the activities of the investee company as opposed to expanding this to the wider group?

We understand that the indicators are devised for direct investments in companies and will therefore be more suitable for equities and bonds but less so for investment in other asset classes, such as commodities, real assets, government bonds and derivatives. Devising a consistent methodology that could work across asset classes would be very complex and therefore we believe focusing on equity and corporate bonds is a proportionate approach, but would welcome clarification from the ESAs that this is what is intended by "investment". Otherwise, various clarifications will be needed as to how the calculations apply to various asset classes in various scenarios, e.g. to sovereign issuers or to short positions. There is also the potential for double counting if a firm has exposures to a company through both equity and debt and clarification on this point would additionally be welcomed.

Requiring disclosure of policies will not be relevant to all asset classes, e.g. an individual office building in a real estate fund would not have a deforestation policy. There can also be variations in scope e.g. for real estate, tenant-controlled areas of a building can be challenging to access data from.

Smaller FMPs will be disproportionately impacted

The difficulty with sourcing the data has been highlighted in our response to Question 1 where we have also set out aggregated feedback from data providers in respect of each proposed indicator. The burden of sourcing this data will fall most heavily on smaller FMPs. Most FMPs will not have the inhouse capabilities to populate indicators themselves and will need to rely on external parties, the costs of which may be prohibitive. This raises the prospect of only larger and niche FMPs being able to comply, although they may also be challenged. This may effectively lock some FMPs out of the market. Again, we would question whether all FMPs need to populate all mandatory indicators at great cost to effectively disclose on their individual PAI.

On page 11 of the Consultation Paper the ESAs acknowledge that the costs will be "especially onerous for smaller companies". The ESAs acknowledge the prospect of small companies being "crowded out from the market" but state the "possibilities to address proportionality are limited". The ESAs go on to state that most of the disclosure requirements contained in the draft RTS are already part of industry initiatives, such as the Eurosif Transparency Code. However, our understanding is that the PAI assessment is developmental and that many of the proposed indicators for the PAI Statement would in fact be entirely new data points for FMPs, even those that are Eurosif signatories.

SFDR does provide for a proportionality element in setting a limit of 500 employees, below which an FMP is not bound to conduct and disclose on a PAI assessment. Opting out must be justified and the focus is on opting in. However, the expansive indicator list is likely to have the opposite effect and could discourage FMPs to do more on sustainability because compliance with the reporting template is viewed as prohibitively onerous and less meaningful to their individual business. Therefore, we do not think that the approach taken will help with the mainstreaming of sustainability and should be reconsidered, especially if smaller companies are to be in a position to comply with the PAI requirements. A central publicly accessible database for disclosed company data would help reduce costs but this will not be available in time for compliance with the SFDR.

Clarifications regarding group companies

We also request further clarification in relation to the timing of the reporting in a group of companies. In a group of companies, it seems that subsidiaries that do not have more than 500 employees will need to disclose their PAI statement (or their non-consideration of principal adverse impact) by 10 March 2021 while their parent company which has more than 500 employees is not required to do so until 30 June 2021. It is anticipated that in a lot of groups wherein various entities are in scope of the regulation, the smaller subsidiaries will adopt the policy implemented by the parent, so unless clarified, it appears that the smaller subsidiaries will be required to disclose ahead of the main entity whose policy they are adopting. Our view is that FMPs that are part of the group and are subject to Article 4 on a comply basis, should align the timing of the disclosure with the rest of the group. It will not be proportionate to expect smaller subsidiaries to disclose before their parent. We would appreciate confirmation of this point by the ESAs.

We also propose that the PAI Statement template allows flexibility for group companies to issue just one PAI Statement as opposed to having one for each FMP applying the same due diligence process (which links in to the above point on timing of publication). The template should also allow the flexibility for entities to cover both the requirements as an FMP and as a financial adviser in one statement (relevant to those entities that have portfolio management and investment advice authorisation) as opposed to issuing two different statements.

3 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?

Yes, we support an alternative approach. We note at the outset the objective of SFDR Level 1 to ensure comparability of *financial products*. However, in this instance, the focus of the ESAs is on comparability of *FMPs*. As per our previous comments, this necessitates a different approach and a balance will need to be struck between harmonisation and aggregation of indicator data for comparability purposes and a qualitative, principles-based approach to enable meaningful disclosure. In addition to striving for comparability, we would also refer back to the parameters for conducting the PAI assessment set under the SFDR Level 1:

- Take due account of their size, the nature and scale of the activities and the types of financial products
- Consider PAIs that are “material or likely to be material”
- Disclose concisely in “qualitative or quantitative terms”
- Conduct identification and prioritisation of principal adverse sustainability impacts and indicators

These parameters, outlined in Recitals 18 and 20 as well as in Article 4 of the SFDR, point to an approach which does not rely on a wide list of mandatory indicators, but rather an assessment which takes materiality and individual business operations into account and that can be both qualitative and quantitative in nature, reflecting the full scope of the FMP’s impact through its stewardship activities. Against the need for flexibility and a qualitative approach at the entity level to make disclosures meaningful, we recognise the ESAs’ ambition for comparability and we think that this balance can be carefully struck in a template that builds on the extensive work that the ESAs have already undertaken.

In concurrence with EFAMA, we think that the following indicators from the proposed PAI Statement lend themselves to more general application, are relevant to the Taxonomy’s high-level DNSH conditions (particularly relating to climate change mitigation and circular economy objectives), and therefore could be retained as mandatory:

- **Indicator 1 (carbon emissions, broken down by scope 1 and 2)**. We understand that data for scope 3 emissions is largely not available. Data providers offer assumptions on scope 3 emissions that vary greatly and do not represent a suitable basis for calculation of indicators that shall be compared by end investors. Moreover, the issue of double-counting within scope 3 and between scope 2 and scope 3 emissions is not yet sufficiently addressed. Therefore, we propose to limit this to scope 1 and 2 emissions. Scope 3 emissions could be reported in the future when more data becomes available and this expectation could be signalled to investee companies.

- **Indicator 2 (carbon footprint for scope 1 and 2 emissions)**. The calculation methodologies for scope 1 and 2 are established in the market but are asset class specific. Therefore, we propose to limit this to scope 1 and 2 emissions. The suggested methodology is based on the investee company's enterprise value which is not fully adequate for direct equity investments.
- **Indicator 5 (total energy consumption from non-renewable sources and share of non-renewable energy consumption).** This is generally considered relevant for all assets although data is not readily available across all sectors. Data on GWh consumption is less available than percentages and would require further costs and efforts to be obtained.
- **Indicator 7 (energy consumption intensity)**. This is generally considered relevant for all assets, even though data is not readily available across all sectors. Data on GWh consumption is less available than percentages and would require further costs and efforts to be obtained.

In relation to social indicators, we recommend that compliance could be facilitated by reliance on the extensive provisions of the UN Global Compact that is already in operation and widely used for sustainable investing purposes. In the absence of a developed European taxonomy for social and employee matters, this is a good proxy for the minimum social safeguards in the Taxonomy and so creates further consistency between the two frameworks. Therefore, we recommend to start with reporting of severe controversies/ breaches of UN Global Compact (share of investments in investee companies that have been involved in severe violations of the UNGC principles) in place of the proposed social, employee, human rights and anti-corruption and bribery indicators. This approach could be revised over time, for example to ensure consistency with the development of social DNSH criteria in the Taxonomy.

Additionally, we would like to see more ability for each entity to explain its principal adverse impact assessment process and outcome. This kind of approach is provided for under the Level 1 text as outlined above and is necessary to provide context around any quantitative results. This is particularly the case where methodologies are still developmental and not well understood, where there are data gaps or assumptions made and where there is the potential for misunderstanding the meaning of reported data. We note that there is an explanation box in the end column of the table but this format does not seem to lend itself to a full, qualitative explanation being provided where necessary in conjunction with each indicator reported. We think it is necessary to provide an optional explanatory field in conjunction with each indicator that can enable an appropriate qualitative explanation of the assessment of the indicator and the reported result.

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

We do not think that the template, as currently structured, is consumer friendly and may serve to confuse rather than inform end investors, given the high volumes of data that will need to be reported, without any context as to the relevance of the indicators to the specific sustainability focus of the product and/or FMP in question. We are concerned that this will lead to a check box exercise that will lose meaningful impact. As per our response to Question 3, we favour an alternative approach that relies on smaller number of universally relevant indicators that can be based on data available in the market, supported by more qualitative information. The expansion of further data points can always be assessed as the sustainable finance regime evolves and in line with the update to the NFRD.

On the requirement in Article 8b to provide an explanation in the table of the impact that an action taken during the reference period has had, we do not think it is realistic to expect that actions taken during the reference period will have such an immediate effect in terms of reducing any adverse indicators. The focus will be on a multi-year transition. In line with existing stewardship codes and best practice, we suggest that FMPs report on outcomes of actions taken during the current or previous reference periods or progress (/ lack thereof) against engagement objectives.

We also have some specific questions regarding how to measure:

- Hazardous waste (against profit, revenue, raw material used)?
- Gender pay gap (equal level or absolute, percentage at equal level or overall sum)?

The treatment of fund of funds also requires clarification. It is unclear how the entity level disclosure will work if the entity making the disclosure invests in funds. Further to the Open Hearing, could the ESAs confirm that it intended that a look through applies to such fund investments, or can they to be omitted from the disclosure?

5 **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)?**

As previously stated, we do not agree with all of the indicators or the proposed approach to have 32+2 mandatory indicators. In summary, we consider that Indicators 1 (carbon emissions, broken down by scope 1 and 2), 2 (carbon footprint for scope 1 and 2 emissions), 5 (total energy consumption from non-renewable sources and share of non-renewable energy consumption) and 7 (energy consumption intensity) lend themselves better to more widespread application. However, as we have previously stressed, by aggregating that data at entity level, perspective on individual products will be lost.

Across the remaining proposed data points we have established that there will be a high degree of difficulty with the following 'principal' indicators: 3 (carbon intensity), 10 (protected species), 13 (water stress), 16 (non-recycled waste), 18 (gender pay gap), 28 (human rights) and 32 (anti-corruption and bribery). From the 18 'additional' indicators, the vendors tell us that Indicators 33, 34, 35, 37, 38, 40, 41, 42, 43, 44, 45, 48 and 50 are very difficult. These will need to be excluded or alternatively, transition arrangements will be required to allow much more time for the data to be produced.

We note that the ESAs have already provided a comprehensive catalogue of indicators and as per our previous responses, we do not propose adding to this extensive list. We consider that this area is still too developmental to include forward-looking indicators that could be universally achievable. We need to focus in the first instance on indicators that are universally applicable and for which data can be gathered, also striking the right balance in terms of costs, proportionality and usefulness of the indicators for end investors. We would also note that an emission reduction pathway is a positive forward-looking indicator and so would question its suitability as an *adverse* impact indicator.

6 **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?**

While there is merit in this reporting, this is still a developmental area and unfortunately not much data is as of yet reported under such scope 3 emissions. The Net Zero Investment Framework being worked on by the Institutional Investors Group on Climate Change ("**IIGCC**") is still in draft form and not yet ready for mass deployment. Therefore, we would not be supportive of including this requirement now, but it could be incorporated at a later date when more data would be available.

7 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?

We would have a concern about applying a double metric on the same data in a way that could serve to add confusion, particularly for retail investors. We are mindful of the ESAs' objective to provide clear, concise and easily understandable information to end investors and would question whether this might add a layer of complexity that could undermine that objective.

Accordingly, we believe that one measurement is sufficient. For most indicators we consider that the percentage of aggregate investments is the better indicator, as it takes size of exposure into account. The share of the investee companies could be applied in cases where the policies in place are to be considered.

8 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?

We think that the ESAs have produced a very comprehensive set of indicators and in that context we are less inclined to add further indicators at this stage, particularly of the 'advanced' nature referenced, when this is a developmental area. We are conscious that advanced indicators could confuse and overload particularly retail investors with complex information. As we have advised earlier, we believe that the focus should be on starting with a smaller number of universally applicable indicators, for which data is available, and then build from there.

There may be merit in including advanced indicators under a phased and considered approach that would allow sufficient time for the industry to source and report on such indicators in a consistent manner. The updating of the NFRD will provide an opportunity to expand the reporting universe of ESG data in the years ahead.

9 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?

Yes, we agree with the goal of delivering the social indicators at the same time. Reflective or our previous comments, there needs to be a consistent approach on both 'E' and 'S' indicators in terms of timing and alignment with the Taxonomy Regulation. We understand that the PAI social indicators in SFDR are intended to link to the Taxonomy's concept of "minimum social safeguards". However, the 'social' Taxonomy which is to serve as this reference for social sustainability is unlikely to be published, let alone finalised, ahead of the SFDR effective date. This creates an unequal playing field for Article 8 and 9 funds which have a 'social' focus as they will not be Taxonomy aligned. This could be misleading to end investors and put such funds at a disadvantage, which could be hugely counter-productive to achieve the EU's overarching sustainability goals.

In the absence of a developed European taxonomy for social and employee matters, we believe that it would be appropriate to adopt an approach consistent with the UN Global Compact Principles for which data is available. Therefore, we recommend to start with reporting of severe controversies/breaches of UN Global Compact (share of investments in investee companies that have been involved in severe violations of the UNGC principles).

10 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?

We would not recommend a 10-year reference period. While it makes sense to us to commence the historical comparison from the date on which the FMP first considered the indicator and to build up a rolling history from that point, we suggest that a three-year period might be most relevant for the rolling history given the rapid evolution in sustainable investment. We would recommend removing the reference to "average" in reporting on data and instead to apply a 'snapshot' at a point as the reporting approach, in keeping with existing financial performance reporting practices our comments in response to Question 11 below.

11 Are there any ways to discourage potential "window dressing" techniques in the principal ad-verse 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?

We do not believe that FMPs will engage in the type of "window-dressing" that the ESAs envisage. In light of their fiduciary duties to their investors, there is no reason to believe that FMPs will alter the investments of the financial products they offer at a particular moment in time to produce a better PAI result than they would for any other investment outcome, including financial performance, particularly when one considers the transaction costs involved in such an approach, which would breach best execution rules. Just as the financial year end is used as the appropriate reporting period for so many other purposes (e.g. balance sheets in the case of financial reports, holdings reports and valuation metrics, P/E, dividend yield, etc.), we believe it should be used for PAI results also. It would be extraordinary to adopt a different approach for this one item, as well as exceptionally difficult to implement from an administrative point of view. An appropriate balance needs to be struck in calculating and aggregating the exposures, which will already be a complex and significant undertaking.

Templates

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

We agree, with some qualifications, to the proposed approach to have mandatory (1) pre-contractual and (2) periodic templates for financial products. In doing so, we acknowledge the ambition of the ESAs in the Consultation Paper to provide for consistent, concise and comparable disclosure relating to ESG aspects. We also acknowledge the advantage of mandatory templates from the perspective of supervisors who review certain pre-contractual disclosures and (retail) investors who will be reviewing them. It is important that templates are focussed on meaningful, relevant and understandable information.

In that regard, we believe it would be more appropriate for the (1) pre-contractual templates to be qualitative, rather than quantitative in nature and take a narrative, rather than a data focussed approach. This is consistent with the approach taken in a prospectus, which is a relatively static document and a detailed, data heavy table would be out of place in such a document. To be workable, any such template must also provide sufficient flexibility to reflect the financial product's characteristics, assets and strategies. We accept that a quantitative approach could be more suitable for (2) periodic reporting.

We would stress the point that as we have not seen any proposed templates, we cannot make any judgement as to their appropriateness. A template can imply many different approaches. Our suggested approach is focussed on consistent language and disclosure, but if a very detailed, data heavy, indicator style template is proposed for the prospectus, we would not be in favour of this.

It is acknowledged that under SFDR Level 1, the pre-contractual disclosure must be made in the prospectus. While we agree that a template would assist with comparability, having additional documents is not always a consumer-friendly approach, as retail investors are unlikely to have the ability or inclination to read and digest multiple documents of technical disclosures. The ESAs will be constrained by the requirements of the Level 1 text which mandates that the pre-contractual disclosures be made in the prospectus or offering document of a UCITS or AIF. This necessitates striking a careful balance in terms of the type of information, level of detail and format of any template to be included in this documentation. As per out previous comments above, the prospectus lends itself to providing information in more qualitative and narrative form.

Finally, we recommend that the use of mandatory templates for pre-contractual and periodic disclosures be limited to products intended for public distribution, i.e. available to retail investors. This is because professional investors find mandatory templates less useful and will conduct their own due diligence, according to their own standardised templates, in order to make an informed decision on investing. Therefore, in respect of products targeted solely at professional investors (as defined in MiFID II and IDD), disclosures in accordance with the templates should be optional.

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

For pre-contractual templates we believe that a qualitative, narrative based approach would be best. The templates should:

- Focus on reflecting the relevant provisions from Level 1 and Level 2, where they are relevant to the investment product and subject to the comments we have made on the Level 2 text elsewhere in this consultation
- Ensure enough flexibility to capture the broad range of different strategies, underlying assets, investment horizons, etc.
- Contain information regarding the strategy adopted to promote ESG characteristics or to pursue sustainable investment objectives
- Make reference to the investment process, including whether products integrate ESG considerations, make use of exclusions, set investment constraints, adopt best-in-class strategies, etc.

As per our response to Question 12, we would be concerned that a quantitative, data focussed approach to pre-contractual templates would result in information being included in prospectus documents which would quickly become dated and therefore potentially misleading to end investors. It is important that a prospectus document have a continuing relevance for end investors and not become dated too quickly, given that it is generally only updated on an annual basis. In order to provide end investors with more granular information, links could be provided to periodic reports, available on the fund's website.

For periodic templates, we believe that a more data focussed approach may be warranted.

14 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.

N/A.

<u>Product disclosure at pre-contractual, website and periodic level</u>

15 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?

We generally agree that a good balance has been struck, however, we do have a number of suggestions. We believe that clear and concise information essential for decision-making should be provided in the pre-contractual disclosures while other information that is more likely to change, require updating or represents additional detail should be provided on a website. With that in mind, we have the following suggestions regarding information that we think should be moved from the pre-contractual disclosure to website disclosure:

- Article 15(2) regarding graphical representation of the proportion of investments qualifying as "sustainable investments". Our preference would be to delete this provision entirely in respect of Article 8 products (see our comments under Question 16). However, should this proposal not be accepted, we would recommend that such data is moved to the website in order to facilitate regular updating.
- Article 24(2) relating to the same graphical representation in respect of Article 9 products should also be moved to a website disclosure for the same reason.
- Disclosure relating to sustainability indicators under Article 18 should be moved to a website disclosure given that this is also data driven information that is subject to change.

For website disclosures, we recommend removing reference to summaries being two A4-sized length pages when printed in respect of the Article 5(1)(d), Article 34(1)(a) and

Article 35(1)(a). Since these summaries will be in online format rather than in an A4 document, this requirement is not directly relevant. We do not propose that such summaries should be formulated into standalone pdf documents. The Level 1 text already contains requirements relating to clear, succinct text so we do not suggest that a further requirement is necessary to specify in this regard.

16 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.

We appreciate that the ESAs are operating within the parameters of the definitions provided under the Level 1 text and the mandate given to develop draft RTS. That said, we do think that there are some helpful adjustments and clarifications that the ESAs could make within the RTS and/or in coordination with the European Commission. We have set out our proposals below.

Clarify further the distinction between Article 8 products and non-ESG products

Before looking at the distinction between 'Light Green' (Article 8) and 'Dark Green' products (Article 9) it is just as important to consider the delineation between non-ESG products and Article 8 products. We note that one of the key objectives of the SFDR is to prevent 'greenwashing'. It would be an unusual outcome running counter to this objective if certain non-ESG funds ended up having to be categorised as Article 8 products because of basic ESG integration or exclusion approaches, based on either i) fulfilling legal obligations or ii) firm-wide ESG policies. At the Open Hearing on 2 July 2020, the ESAs helpfully clarified that if there is a legal obligation to exclude certain kinds of investments, it would not be the intention of the ESAs to consider such products as qualifying as Article 8 products. We would welcome written confirmation of this in the ESAs' Feedback Statement to the Consultation Paper.

It was also stated at the Open Hearing that it is possible to have only one sectoral exclusion and qualify as an Art. 8 product. In this area we would request further clarification in order to prevent many products that are not ESG products from being brought into the Article 8 category and thereby creating the risk of confusion and undermining the value of the Article 8 designation. We would like the ESAs to clarify 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 Art. 8 product. We think a clear distinction needs to be drawn between non-ESG products and Article 8 products. Accordingly, we propose that the ESAs clarify that products with ESG integration should be in scope of Article 8 only if ESG integration impacts investment decisions such as portfolio construction and that this is communicated to clients and end investors.

Article 8 products should not need to carry a warning or disclaimer

Under Article 16(1) of the draft RTS, Article 8 products would be required to include a statement in the pre-contractual information that "*This product does not have as its objective sustainable investment*". We do not think that this statement is appropriate to include in respect of Article 8 products, which could serve to undermine a legitimate ESG product category that has been defined by the SFDR with various requirements applicable to such products. We think that this statement is likely to confuse consumers, who are likely to take from it that Article 8 products are non-ESG products as opposed to fully appreciating the legal definitions and the difference between promoting ESG characteristics and having sustainable investment as an objective.

The statement could also mislead consumers into thinking that Article 8 products may never invest in 'sustainable investments' as defined under Article 2(17) of the SFDR Level 1 when this is not the case, although they are not bound to do so. Elsewhere the draft RTS have acknowledged this possibility and required that where Article 8 products make 'sustainable investments' as defined under the SFDR, they must apply the DNSH criteria.

Article 8 products will be subject to extensive disclosure requirements under the RTS that will cover:

- Criteria for selecting investments to attain environmental or social characteristics
- Measurement by sustainability indicators that will be disclosed to end investors as part of pre-contractual information
- Information about the extent to which those characteristics were attained, including the performance of the sustainability indicators used as part of the periodic reporting
- Provision of historical comparisons about the level of attainment of environmental or social characteristics during the lifetime of a product

Therefore, we do not see the need for the proposed warning in relation to Article 8 products over and above all of the requirements specified.

Further distinguish between Article 8 and Article 9 products by removing Article 15(2)

Under Article 15(2) of the draft RTS, Article 8 products are required to disclose the proportion of investments that are 'sustainable investments' as per the definition applicable to Article 9 products. This requirement could serve to blur the distinction between Article 8 and Article 9 products. It also should be noted that the Taxonomy Regulation requires a breakdown of Taxonomy compliant and non-compliant economic activities for Article 8 or 9 products with environmental characteristics or objectives. Therefore, the envisaged approach will result in two similar disclosures based on different frameworks (the legal definition of 'sustainable investment' and the Taxonomy). This will add complexity and confusion for end investors. For these reasons, we ask the ESAs to delete Article 15(2) from the proposed RTS.

Product naming and Article 8 and Article 9 products

We would also request clarification on any implications for product names, in particular, whether only Article 9 products can refer to themselves as 'sustainable'. Whilst only Article 9 products are classed as fully meeting the criteria for "sustainable investment", both Article 8 and 9 products fall under the SFDR. We would encourage a broader view of what counts as 'sustainable' that includes Article 8 products and acknowledge the important role that the investor's strategy can play through engaging with companies to improve their sustainability performance, delivering sustainable outcomes and helping to generate additional positive real economy impact over time.

We do not propose any further defining of the distinction between Article 8 and Article 9 products at present, save for those set out above. However, it could be useful over time to provide Q&As on the product classifications as issues arise. It could be helpful if ESMA could provide some further examples of types of funds falling into either Article 8 or Article 9 categories, perhaps in a Q&A, which would foster consistent classification in different Member States.

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

We do not have any particular concerns about the capturing of indirect investments through graphical and narrative descriptions. We would note that narrative descriptions lend themselves to capturing of indirect investments more readily. You will note that in our response to Questions 15 we recommend moving such information to website disclosures and in our response to Question 16, we recommend the deletion of Article 15(2) from the draft RTS, as we do not believe that the graphical presentation is appropriate in the case of Article 8 financial products. We believe a clear explanation of the underlying process in relation to the consideration of ESG characteristics would be preferable to a graphical presentation. In responding to this question, we took "indirect investments" to refer to fund of funds. In relation to derivatives, please see our response to Question 26.

18 **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?**

Yes, we agree that such a breakdown could be misleading for the end-investor who will need to be able to distinguish how different investments relate to the overall strategy of the fund.

The approach to ESG integration is holistic and undertaken at the level of the portfolio and all assets of the product contribute to the overall objective and strategy. The breakdown is therefore not helpful to the investor in that regard and goes against the overall ambition of avoiding excessive disclosure and preventing misleading end investors.

You will note that in any case we have proposed deleting Article 15(2) as per our previous comments in response to Question 16.

19 **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?**

We think that it is reasonable to expect disclosure of exposure to solid fossil fuel sectors where relevant. This kind of exposure is one that end investors may particularly have concerns about and want disclosed. However, we have concerns that this exposure is not always readily measurable, for example in the case of sovereign issuers.

We are also concerned that proposed definition of the term “fossil fuel sectors” under the draft RTS could be misleading as it refers only to solid fossil fuels. The term “fossil fuels” is already widely understood to refer to all hydrocarbon-based fuel sources, including oil and natural gas, as referenced under the definitions promoted by the Intergovernmental Panel on Climate Change. Unless the end investor is familiar with the regulatory definition, they are likely to assume that this refers to all fossil fuels. Therefore, we would recommend updating the definition on that basis.

Other sectors where end investors may appreciate disclosure are:

- Nuclear energy

- Fracking
- Mined gas
- Tobacco
- Controversial weapons

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

We believe that the approach adopted in the EU Action Plan and reflected in the RTS of applying the same rules to all financial products is appropriate.

While not directly relevant to this question, it would be helpful from a practical perspective if FMPs who offer identical investment strategies through different financial products (e.g. collective investment schemes and segregated mandates) could provide a single website disclosure applicable to both financial products.

21 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 in-vestment 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?

We suggest that further elaboration in this area is not necessary and that the requirement under Article 17(c) of the RTS suffices to enable FMPs to detail their policy to assess good governance processes. Fund managers already have well developed policies in place that have evolved over many years and are based in regulation, recently updated under SRD II.

22 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?

As recognised in the Taxonomy Regulation, the principles of 'do no significant harm' and 'adverse impact' should be consistent. Subject to our concerns in relation to the appropriateness of the extensive list of mandatory indicators used in Annex I, we would like to see a better linkage created between the two concepts. We also believe that a consistent materiality concept should be central to any assessment of principal adverse impact or significant harm.

We agree with the ESAs' view that the Commission should consider studying the feasibility of clarifying the relationship between the concepts of 'do no significant harm' and 'principal adverse impact' in the future. As per our previous comments, we would urge the ESAs and the Commission to make this clarification as soon as possible during the EU sustainable finance regime implementation rather than down the line, as we are concerned that having different concepts with different meanings seeking to achieve broadly the same objectives could potentially confuse end investors as well as FMPs and NCAs that have to apply the regulations. As per our previous remarks, we think that any mandatory PAI indicators should be relevant to the high-level Taxonomy DNSH conditions and that the DNSH assessments under the SFDR for sustainable investments should leverage the definition of do no significant harm as set out in Article 17 and the minimum social safeguards set out in Article 18 of the Taxonomy Regulation when disclosing how the sustainable investments meet the DNSH criteria.

23 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?

We consider that these strategies are sufficiently understood in the market and question the necessity of defining them by regulation. The area of sustainable finance is also rapidly evolving and crystallising such definitions now could impede further enhancement and innovation.

24 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?

We broadly agree with the idea of including the top investments in periodic reports, which is already standard industry practice in respect of UCITS and retail funds. However, we believe that the minimum should be the top 10 holdings rather than top 25. This would align with current best practice. A balance needs to be struck in terms of the level of information provided and we are not convinced that adding an extra 15 investments to the list would significantly improve the disclosure. For private funds, where this information may be commercially sensitive and confidential, we suggest providing the top holdings information by industry sector or asset location. In keeping with our response to Questions 10 and 11 and existing practice, we recommend that the top holdings data be reported as a snapshot at a point in time.

<u>Specific questions on pre-contractual disclosure items in light of differences between types of disclosure documents</u>

25 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.

As per our response to Question 15, we believe that clear and concise information essential for decision-making should be provided in the pre-contractual disclosures while other information that is more likely to change, require updating or represents additional detail should be provided on a website. We have applied that principle in response to the individual points outlined below.

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);

We agree that this item is better included in the pre-contractual disclosure, as it applies to a commitment made prior to the application of the relevant investment strategy and so is pre-contractual in nature.

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);

We agree that this item is better included in the pre-contractual disclosure, as it lends itself to a qualitative narrative disclosure.

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

We agree that this level of detail is better included in the website disclosure, particularly as it may evolve over time and website disclosures lend themselves to more ready and regular updates.

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.**

As these relate to data sources, the availability of which is rapidly evolving, we believe these are more appropriately dealt with in website disclosures, which lend themselves to more ready and regular updates.

26 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)?

We would prefer to have a narrative explanation on the use of derivatives (to the extent required) as to incorporate this into the graphical representation (in respect of which we have reservations) could overcomplicate the disclosure and potentially confuse end investors. For managers who use derivatives extensively, they can be as integral to the achievement of their ESG strategy as direct investments. For managers who do not use derivatives extensively, we note that Recital 20 acknowledges that hedging instruments may not be relevant to environmental or social characteristics promoted by a product and so, in our view, to include a separate section for such investments could be disproportionate and misleading. We would also note that there are already requirements under the UCITS Directive relating to the disclosure of the use of derivatives.

Preliminary impact assessments

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

The ESAs have estimated the costs at between EUR 80-200k (page 74) but depending on the final outcome of the consultation on the RTS (particularly in relation to the range of mandatory indicators), the costs could be exponentially higher. Currently, a mid sized fund manager can spend anywhere between EUR 250-600k on ESG data while a larger fund manager can spend anywhere between EUR 600k – EUR 1.5mn (fund managers will often use multiple data vendors to enhance the coverage and as part of the analysis and validation). The total spend on ESG data could vastly increase in order to meet the requirements of the proposed PAI Statement.

Some of the steps involved in preparing for the RTS will include:

- Assessment and requirements analysis
- External vendor costs
- In-house research and data aggregation / analysis
- IT development and reporting infrastructure costs
- Compliance programme, validation and implementation costs
- External legal costs

The ESAs have noted progress in the ESG data market in recent years and therefore made an assessment that the situation with regard to ESG data will continue improving in order to meet demand. However, as we have outlined in our response to Question 1, the survey we conducted with vendors revealed that 24 of the 32 principal indicators will be difficult or very difficult for them to provide, based on the responses of the vendors. Of the 18 additional data points, 1 is difficult and 13 are very difficult. Difficulty in providing the data increases the cost. Also, as previously noted, the challenges with sourcing data on the private market will persist (availability, costs, quality, reliability and comparability) until there is a common (global) standard. Hence, the EU has recognised the need to update the NFRD in the first instance and we also support the establishment of a public EU ESG data register in order to increase data availability and drive down costs. Following these developments, we expect the provision of a broader range of ESG indicators to become more achievable. Until then, we must be realistic about the constraints that FMPs are operating under.