BETTER FINANCE
The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

Ref: Joint ESAs Consultation Paper on ESG disclosures

Link to consultation: https://www.esma.europa.eu/press-news/consultations/joint-esa-consultation-esg-disclosures

BETTER FINANCE Response to the Joint ESAs Consultation Paper on ESG disclosures

Executive Summary

General considerations	The Disclosure regulation set specific rules on how to disclose ESG policies and sustainability/factors in relation to investments for UCITs AIFMs, management companies, portfolio managers and investment advisers authorised under MiFID.[1] **Consistent disclosure of principal adverse impact:** BETTER FINANCE welcomes the introduction of table 1 of the Joint ESAs Consultation Paper on ESG disclosures requiring consistent disclosure of principal adverse impact**.** However, it is important that metrics and indicators are aligned with the non-financial reporting directive (NFRD) and it needs to be aligned with the taxonomy regarding the definition of economic activities and the environmental objectives. **There is a need for consistency with the legislation on sustainable finance.** It is important that the same "language" is used across the 3 legislations. The do not significant harm (DNSH) principle needs to be coherent with the DNSH indicators under the taxonomy regulation in regard to the environmental objectives in order to avoid contradiction and regulatory inconsistencies. In addition, Article 4 paragraph 2(e) regarding engagement policies should be in aligned with the disclosure requirements in the **shareholder rights directive.** **Regulatory time gaps**. There is a considerable time gap between the implementation of the disclosure regulation that will apply from 10 March 2021 and the ongoing works on the review of the non-financial reporting directive which is fundamental to guide investee companies in providing non-financial information. In addition, the future definition of the Taxonomy will be completed probably in 2025, thus the do not significant harm principle will come into force in the disclosure regulation without its specifications and definition in the taxonomy.
Mandatory pre-contractual and periodic templates	**Compliance with the EU financial regulatory framework:** ESG or sustainability disclosures must be concise and clear for non-professional clients, preferably in short documents. To exclude the two main documents made specifically to convey ***key information*** for "retail" investors from the SFDR is not only a mistake, but it creates different disclosure standards for the same investment products, which can also create confusion for non-professional clients. In addition, SFDR should be aligned with the PRIIPs Regulation at least by

[1] https://corpgov.law.harvard.edu/2020/03/24/new-esg-disclosure-obligations/

	extending the disclosure rules from SFDR to the PRIIPs KID; similarly, since UCITS are expected to also transition to the PRIIPs KID, until such transition is made, the UCITS KIID disclosure rules should also be amended accordingly to include information required by the SFDR in an appropriate manner. **No need to reinvent the wheel**: Disclosure for individual investors must be at all times clear (in the MiFID sense; i.e. intelligible), simple, short and concise, avoiding jargon and comparable. To be clear, simple, short and concise, it must focus only on key elements that can and should guide the financial decision making of the average investor. To be comparable, it must reach the highest degree of standardisation at a cross-sectoral levels and standardisation concerns not only the type of information to be included, but also the order flow and format; in other words, it must exhibit the same structure.
Requirements on information disclosed between pre-contractual and website	Information can be balanced between pre-contractual and website information as long as there are clear rules on which information and how the information is disclosed on the website. Information on websites and other marketing material is not regulated as pre-contractual documents as for example KIIDs and prospectuses, therefore additional rules and clarification are needed. In addition, we recommend introducing a specific warning on greenwashing. The information provided needs to be accurate, fair, clear and not misleading in order to avoid any form of greenwashing and miss-selling. A specific reference could be done with the definition of greenwashing on recital 9 of the taxonomy regulation (although not perfect but it is the only legal one): *"the practice of gaining an unfair competitive advantage by marketing a financial product as environmentally friendly, when in reality it does not meet basic environmental standards".*
Product differences between Article 8 and Article 9	There is not a clear distinction between "sustainable investment products" in Article 9 and "products that promote environmental and ? social criteria" in Article 8 of the Sustainable Finance Disclosure Regulation (SFDR). It is necessary to provide a clear definition and guidance that will help to qualify the product to the category. Lack of a clear definition would result in different interpretation by financial market participants and national supervisory authorities. For additional information see our answer to question 16.
Do not significant harm principle (DNSH)	According to recital (33): "*the do not significant harm principle is closely linked to the criteria to be developed in the context of the Regulation on the establishment of a framework to facilitate sustainable investment" (taxonomy).* As the six environmental objectives would need to be identified for the *do not significant harm* approach but they are not taken into consideration in the definition of sustainable investment (Article 2, P.17 of the SFDR), this would create incongruences in terms of the information required to assess the sustainability risks and the identification/classification of the sustainable financial products based on their environmental objectives. In addition, this would increase the complexity for individual investors who will be confronted with too much and unclear information.

About BETTER FINANCE

BETTER FINANCE, the European Federation of Investors and Financial Services Users, is the European public interest non-governmental organization solely dedicated to the interests of European citizens as savers, individual investors and financial services users at the European level to lawmakers and the public in order to promote research, information and training on investments, savings and personal finances.

BETTER FINANCE acts as an independent financial expertise and advocacy center to the direct benefit of European financial services users. Since the BETTER FINANCE constituency includes individual and small shareholders, fund and retail investors, savers, pension fund participants, life insurance policy holders, borrowers, and other stakeholders who are independent from the financial industry, it has the best interests of all European citizens at heart. As such its activities are supported by the European Union since 2012.

Instructions on how to read this paper: this document contains the response of BETTER FINANCE to the European Commission's online survey (public consultation) concerning the consultation on the renewed sustainable finance strategy but it is not the actual response form submitted.[2] Some questions include a ***short summary*** (in italics) to help the reader to understand the context. The summaries are incorporated from the Articles of the proposed regulation and the text of the Joint ESAs consultation document. [3]

Introduction

The Disclosure regulation set specific rules on how to disclose ESG policies and sustainability/factors in relation to investments for:

- insurance undertakings, [4]
- IORPs, [5]
- for managers of qualifying venture capital funds, [6]
- for managers of qualifying social entrepreneurship funds,
- for manufacturers of pension products, [7]
- for UCITS management companies,[8]
- for investment firms which provide portfolio management or provide investment advice,[9]
- for credit institutions which provide portfolio management or provide investment advice,[10]
- for insurance intermediaries and insurance undertakings which provide insurance advice

[3]https://www.esma.europa.eu/sites/default/files/jc_2020_16_-_joint_consultation_paper_on_esg_disclosures.pdf

[4] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R2088&from=EN

[5] Ibid.

[6] Ibid.

[7] Ibid.

[8] Ibid.

[9] Ibid.

[10] Ibid.

with regard to IBIPs.[11]

- Insurance intermediaries which provide insurance advice with regard to pension products exposed to market fluctuations, [12]
- AIFMs of ELTIFs, [13]
- PEPP providers, [14]

The European Supervisory Authorities (ESAs) are empowered to deliver through the Joint Committee (JC), draft Regulatory Technical Standards (RTS) the content, methodologies and presentation of sustainability-related disclosures. Six of these RTS must be delivered by 30 December 2020 and one must be delivered by 30 December 2021.[15]

The draft regulatory technical standards (RTS) relate to several disclosure obligations under the SFDR regarding the publication of:

- the details of the presentation and content of the information in relation to the principle of 'do not significantly harm' as set out in Article 2(17) of the SFDR consistent with the content, methodologies, and presentation of indicators in relation to adverse impacts referred to in Article 4(6) and (7) SFDR.[16]

- a statement on an entity's website on the due diligence policy regarding the adverse impact of investment decisions on sustainability factors in relation to climate and other environment-related impacts (Article 4(6)) and adverse impacts in the field of social and employee matters, respect for human rights, anti-corruption and anti-bribery matters (Article 4(7)).[17]

- pre-contractual information on how a product with environmental or social characteristics meets those characteristics and if an index has been designated as a reference benchmark, whether and how that index is consistent with those characteristics (Article 8).[18]

- pre-contractual information to show, where a product has sustainable investment objectives and a) has a designated index as a reference benchmark, how that index is aligned with the sustainable investment objective and an explanation as to why and how that designated index aligned with the objective differs from a broad market index (Article 9(1) SFDR); b) if no index has been designated as a reference benchmark, an explanation on how that objective is to be attained (Article 9(2) SFDR).[19]

- Information on an entity's website to describe the environmental or social characteristics of

[11] Ibid.
[12] Ibid.
[13] Ibid.
[14] Ibid.
[15] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R2088&from=EN
[16] Ibid.
[17] Ibid.
[18] Ibid.
[19] Ibid.

financial products or the sustainable investment; the methodologies used; the pre-contractual information referred to in Articles 8 and 9; and the periodic reports referred to in Article 11.[20]

- Information in periodic reports according to sectoral legislation specifying
  - (a) the extent to which products with environmental and/or social characteristics meet those characteristics, and
  - (b) for products with sustainable investment objectives and products which objective is a reduction in carbon emissions:
    - (i) the overall sustainability-related impact of the product by means of relevant sustainability indicators and
    - (ii) where an index has been designated as a reference benchmark, a comparison between the overall impact of the financial product with the designated index and a broad market index through sustainability indicators (Article 11 of the SFDR).[21]

Consultation questions

Please make your introductory comments below, if any:

BETTER FINANCE considers that the *regulation on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU)2016/2341* is extremely important to clarify fiduciary duties and increase the transparency of the disclosure of sustainability risks.[22] However, in order to be effective, the disclosure regulation needs to be harmonised with the taxonomy regulation and the non-financial reporting directive. Considering that one of the major issues is the lack of a common definition of sustainable investments, it necessary to link how asset managers define sustainable investments with the taxonomy-compliant activities in order to avoid any regulatory divergences. In this regard, we advise to strengthen this link in the draft of Regulatory Technical Standards (RTS).

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?

Summary : *The ESAs, taking into account the input received by the JRC and EEA, saw as the best approach to use a mandatory set of indicators to ensure a minimum level of harmonised assessment of principal adverse impacts of investment decisions on sustainability factors. These indicators would always be considered to be leading to principal adverse impacts on the environment and society, irrespective of the value of financial market participant's result for the indicator's metric. In*

[20] Ibid.
[21] Ibid.
[22] https://esas-joint-committee.europa.eu/Publications/Consultations/JC%202020%2016%20-%20Joint%20consultation%20paper%20on%20ESG%20disclosures.pdf

other words, the financial market participants have no choice to determine whether their investments lead to principal adverse impacts for these indicators because any positive value for the assessment of the indicators is classified as having a principal adverse impact.

This set is complemented by additional indicators that are included on an opt-in basis, for financial market participants to use for the assessment of principal adverse impact. Financial market participants have to choose at least one environmental indicator and one social indicator to be included in the principal adverse impact disclosure. Financial market participants may also add other indicators relevant to their investments.

In order to promote comparable disclosures at entity level, the ESAs have proposed a reporting template containing principal adverse impacts in Table 1.

Furthermore, the ESAs saw merit in trying to consult on the indicators for social and employee matters, respect for human rights, anti-corruption and anti-bribery matters at the same time as the environmental indicators, even though SFDR grants the ESAs one more year to deliver that part of the technical standards.

In developing the indicators, the ESAs have taken into account the European Commission's Technical Expert Group (TEG) work on transparency for benchmark administrators. It remains a goal of the ESAs to align the indicators with the forthcoming Delegated Acts.

Finally, the indicators also take into account the determination of the ESAs to consult on disclosure of how financial products comply with the "do not significantly harm" principle enshrined in Article 2(17) of Regulation (EU) 2019/2088, in relation to the principal adverse impact indicators. In practice this means that some indicators are intended to capture different aspects of significant harm to environmental or social factors. For this reason, the ESAs saw merit in including an indicator for exposure to the manufacture and selling of controversial weapons, based on the baseline exclusions for EU climate transition benchmarks (CTB) and EU Paris aligned benchmarks (PAB).

BETTER FINANCE welcomes the introduction of table 1 requiring consistent disclosure of principal adverse impact. However, it is important to ensure that metrics and indicators are aligned with the non-financial reporting directive and i with the taxonomy regulation regarding the definition of economic activities.

Clear definition of principal adverse impact needs to be provided. In addition to indicator and metrics for principal adverse impact a clear definition needs to be included in order to guarantee that financial market participants will use the same language and will have the same understanding of the concept. At the moment the regulation fails to provide such a clear definition.

The concept of materiality needs to be in line with non-financial reporting directive. As previously advocated by BETTER FINANCE in the consultation on the non-financial reporting directive[23] materiality needs to be assessed according to 2 dimensions (**double materiality**):

1. the potential and/or the actual impact of sustainability risks on the **performance, reputation and activities of the companies** over the short and long-term (this includes also the financial materiality of the company)

[23] https://betterfinance.eu/wp-content/uploads/BF-Feedback-on-the-review-of-the-non-financial-reproting-directive.pdf

2. the potential and/or actual impact of sustainability risks **outside the company** (that includes the environment, society, communities etc.,) over the short and long-term.

Therefore, the disclosure process should be based on a double materiality assessment based on a clear definition of these 2 aspects.

In the long term, ESG risks and opportunities can become financially material, and therefore should be integrated in financial decision-making. Public reporting of non-financial information enables investors/shareholders to gather public support for the issues at stake and make their case for engagement with corporate boards/ filing an ESG-related shareholder resolution. Public disclosure of potential impacts of sustainability risks/opportunities allows shareholders to make their own assessment as to their financial materiality. This is why the disclosure regulation needs to be consistent and linked with the non-financial reporting directive in particular regarding the definition of principal adverse impact indicators.

Consistency with the legislation on sustainable finance. As previously mentioned, the proposed legislation needs to be coherent and harmonized with non-financial reporting directive and the taxonomy regulation, in particular for the definition of metrics and indicators. It is important that the same "language" is used across the 3 legislations. The "do not significant harm" (DNSH) principle needs to be coherent with the DNSH indicators under the taxonomy regulation in regard to the environmental objectives in order to avoid contradiction and regulatory inconsistencies.

In addition, Article 4 paragraph 2(e) regarding engagement policies should be aligned with the disclosure requirements in the **shareholder rights directive**.

Regulatory time gaps. There is a considerable time gap between the implementation of the disclosure regulation that will apply from 10 March 2021 and the ongoing works on the review of the Non-financial reporting directive which is fundamental to guide investee companies in providing non-financial information. In addition, the future definition of the Taxonomy will be completed probably in 2025, thus the do not significant principle will come into force in the disclosure regulation without its specifications and definition in the taxonomy.

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?

Summary: *The disclosure requirements in this Regulation are designed to impose fundamental regulatory requirements which are appropriate for all financial market participants and were regarded as necessary to meet the objective of Regulation (EU) 2019/2088. Depending on their size and nature, a significant number of financial market participants fall under the scope of Regulation (EU) 2019/2088. Financial market participants exceeding the number of 500 employees on their own balance sheet or, where they are parent undertakings, on their group balance sheet are subject to the disclosure obligations on principal adverse impacts at entity level set out in this Regulation. Financial market participants below the threshold of 500 employees should at least explain where they do not consider adverse impacts of investments decisions on sustainability factors the reasons to not consider them. Similarly, financial advisers that consider principal adverse impacts on sustainability factors in their advice are subject to the disclosure obligations set out in this Regulation.*

BETTER FINANCE believes that the proposed regulation needs to comply with a high level of standardization across all market participants. In order to better take into account the size and the nature of the market participants, the proposed regulation should have considered the AuM size of the market participants instead of the number of 500 employees. Market participants with a lower number of employees but with a high impact on sustainable financial products would not have d to disclose information on principal adverse impact.

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?

BETTER FINANCE agrees with the quantitative indicators that would allow for a better standardisation and harmonization of the information disclosed.

However, we stress the need to provide understandable information to individual investors. Disclosure for individual investors must be at all times **simple, short and concise, avoiding jargon and comparable.** To be simple, short and concise, it must focus only on key elements that can and should guide the financial decision making of the average investor. To be comparable, it must reach the highest degree of standardisation at a cross-sectoral levels and standardisation concerns not only the type of information to be included, but also the order of sections and format; in other words, it must exhibit the same structure.

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

We believe that the indicators on the reporting template provided in Table 1 of Annex I would need more explanations on the type of information and data they require. It is important that the list of indicators does not end up as a mere tick the box exercise. The indicators should provide an overview of the goal also in relation to the engagement policy. The principle adverse impact should be assessed against targets/goals of the investment portfolio. Therefore, a stronger link between the engagement policy and adverse impact targets should be done.

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)?

Yes, we recommend including forward-looking indicators as for example CPAEX[24] and emission reduction pathways that would help to identify and monitor the progress of the investment portfolio and progress in reaching specific targets.

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?

[24] https://betterfinance.eu/wp-content/uploads/Joint-position-NGOs-ecolabel.pdf

We believe that additional measures relative to the EU 2030 climate and energy targets and measures of carbon emissions relative to the prevailing carbon price would provide additional disclosure on portfolio alignment to science based international climate objectives. As several methodologies currently exist on measuring company and portfolio temperatures, it is necessary to streamline and harmonize the metrics in accordance with the non-financial reporting directive (NFRD) and the Taxonomy regulation.

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?

We agree with this requirement.

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?

Introduction of more advanced indicators or metrics to capture activities by investee companies to reduce GHG emissions needs to be designed according to climate change mitigation and climate change adaptation objectives in the Taxonomy. In addition, the availability of this data depends as well on the information provided by the Non-financial reporting directive. Finalized taxonomy and available ESG data at company level is essential to capture activities by investee company. Therefore, we recommend ensuring that these aspects are consistent across regulatory requirements in order to avoid the disclosure of unrealistic and incomplete information.

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?

BETTER FINANCE supports strongly the approach to deliver indicators for environmental social and governance (ESG) aspects at the same time.

Moreover, social aspects should be coherent also with the future development of social safeguards criteria of the taxonomy. Social indicators should be in line with international standards as **the UN Guiding Principles on Business and Human Rights,** as it has been included in the agreement of the Taxonomy Regulation on minimum social safeguards and it is more prescriptive on what is expected from a company regarding human rights. Additional indicators on governance issues could be developed around other international frameworks as for example **OECD Guidelines for Multinational Enterprises and UN Global Compact.**

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?

Summary:

Article 6 (2): Where the financial market participant has provided a description of adverse impacts on sustainability factors for at least one previous reference period in accordance with paragraph 1, the statement shall contain a historical comparison of the current reference period with the previous reference periods covering at least the shortest of the following periods:
(a) the previous ten years;
(b) from the date on which the financial market participant first considered principal adverse impacts of its investment decisions on sustainability factors; or
(c) from 10 March 2021.

We agree with the proposal that financial market participants should provide historical comparison of principal adverse impact disclosure covering the previous 10 years or from the date on which the financial market participant first considered principal adverse impacts. We believe that this period should not be shorter than 10 years (or since the inception of the financial product if less than 10 yars), as sustainability is a long term issue. However, we would like to point out that Article 6 paragraph 2 is phrased in a way <u>that even if</u> the financial market participant is able to provide a description of the adverse impacts covering the previous ten years, it's still allowed to provide such information only for period from 10 March 2021 (letter c). Therefore, there should be an additional condition that the reference period (C) may be used **only** when it is impossible to provide the 10 years historical comparison due to the lack of historical data.

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?

The best way to discourage potential "window dressing" techniques in the principal adverse impact reporting is by ensuring consistency with the non-financial reporting directive harmonizing methodology of reporting and standardizing the way the information required are collected and processed.

Sustainability reporting needs to reach the same robustness of the financial reporting. Non-financial indicators are extremely relevant to asses if the company is consistent with ESG values and to identify adverse impact factors. Therefore, harmonized methodology and uniform timing of reporting, complying with same guidelines and accuracy of disclosed information are extremely important for corporate sustainability reporting.

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

Summary: *SFDR indicates that information on financial products falling under the scope of Article 8 and Article 9 should be located in pre-contractual information as well as on websites, without further specifying the precise scope of each disclosure. The ESAs have set out a proposal for pre-contractual information requirements in Chapter III of the draft RTS, taking into account the differences of the various financial products and the differences between the types of pre-contractual documentation set out in Article 6(3) SFDR. This proposal tries to strike a balance between comprehensiveness and comprehensibility of information. This pre-contractual information is complemented by website information under Chapter IV of the draft RTS. The periodic product disclosure focuses on the success of the product in achieving its environmental or social characteristic (or combination thereof) or sustainable investment objective.*

BETTER FINANCE draws the attention to the fact that more regulation is not better regulation, and the costs of "retail" investment products cannot be expected to be lowered if compliance with the EU financial regulatory framework, in this particular case disclosure rules to non-professional clients, is heavy and burdensome. The issue BETTER FINANCE highlights is the discrepancy in pre-contractual disclosure between key information documents (PRIIPs and UCITS) and other disclosure documents for "retail" investment products (such as the Prospectus, Annual reports for AIFs and UCITS, or the other disclosure requirements required by IDD etc). As mentioned in the introductory statement/comment, ESG or sustainability disclosures must be concise and clear for non-professional clients, preferably in short documents. To exclude the two main documents made specifically to convey ***key information*** for "retail" investors from the SFDR is not only a mistake, but it creates different disclosure standards for the same investment products, which can also create confusion for non-professional clients. At the same time, BETTER FINANCE wishes to address the inconsistency between Art. 6(3) SFDR and Art. 8(3) PRIIPs Regulation.

In Art. 8(3)(c) of the PRIIPs Regulation, the product manufacturer must disclose "***specific environmental or social objectives targeted by the product***", which is a generally-termed provision, not further detailed by the delegated acts (Level 2 PRIIPs). As such, the SFDR creates[25] different reporting standards on ESG issues between the Prospectus and other disclosures for PRIIPs and the PRIIPs KID.

Therefore, the SFDR should be aligned with the PRIIPs Regulation at least by extending the disclosure rules from SFDR to the PRIIPs KID; similarly, since UCITS are expected to also transition to the PRIIPs KID, until such transition is made, the UCITS KIID disclosure rules should also be amended accordingly to include information required by the SFDR in an appropriate manner.

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[25] Article *6(3) SFDR: Financial market participants shall include descriptions of the following in pre-contractual disclosures:*
(a) the manner in which sustainability risks are integrated into their investment decisions; and
(b) the results of the assessment of the likely impacts of sustainability risks on the returns of the financial products they make available. Where financial market participants deem sustainability risks not to be relevant, the descriptions referred to in the first subparagraph shall include a clear and concise explanation of the reasons therefor.
2. Financial advisers shall include descriptions of the following in pre-contractual disclosures:
(a) the manner in which sustainability risks are integrated into their investment or insurance advice; and
(b) the result of the assessment of the likely impacts of sustainability risks on the returns of the financial products they advise on.

Pre-contractual and periodic templates need to be in line with existing legislative framework in terms of information disclosure for financial products which requires (*Article 44.2 of MiFID II delegated regulation*)[26]:

- "a fair and prominent indication of any relevant risks",
- not to "disguise, diminish or obscure important items, statements or warnings",
- and to present such information "in a way that is likely to be understood by the average member of the group to whom it is directed, or by whom it is likely to be received"

No need to reinvent the wheel: Disclosure for individual investors must be at all times **simple, short and concise, avoiding jargon and comparable**. To be simple, short and concise, it must focus only on key elements that can and should guide the financial decision making of the average investor. To be comparable, it must reach the highest degree of standardisation at a cross-sectoral levels and standardisation concerns not only the type of information to be included, but also the order flow and format; in other words, it must exhibit the same structure.

However, other pre-contractual and execution phase disclosures can be provided by product manufacturers or distributors, where you need to allow a certain degree of freedom to preserve competition and potentially address or present information that is not included in the regulatory formats, i.e. marketing communication materials. These can be brochures, binders, factsheets, specific product reporting etc. In these non-regulatory documents, there are only two rules that must be observed:

1) first, the information must be consistent with the regulatory reporting, i.e. KIDs, Prospectus and/or BS or best execution reports.

2) the presentation must be fair, i.e. highlight both advantages and disadvantages without any subliminal or express biases.

The last category concerns full disclosure documents, in particular the Prospectus (pre-contractual) and the Annual Report (both pre-contractual and execution phase): these documents are for the broad public (all investor types) and should be as granular as know-how and essential business information allows it. These should not aim to answer all questions of any investor (exhaustive disclosure) but to communicate all information necessary for the proper functioning of the market, for financial stability and for investor protection concerns.

In these two documents. It can be recommended to include definitions, glossaries of terms or explanations for all or unusual terms to facilitate comprehension, but as a ground rule disclosure must be in full and correct.

Q13 : If the ESAs develop such pre-contractual and periodic templates, what elements should the ESAs include and how should they be formatted?

Please see answer above

[26] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R0565&from=EN

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.

N/A

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?

Summary*: The ESAs saw merit in providing mandatory disclosure templates for pre-contractual and periodic product disclosure for Article 8 and Article 9 SFDR products, in order to benefit from harmonised disclosures in a comparable way. However, given the uncertainty regarding the granularity of disclosure under Chapter III (pre-contractual disclosure), the ESAs have delayed the drafting of these templates until there is greater certainty regarding what should be disclosed. The ESAs envisage launching a separate process to develop these templates after the consultation paper has been launched.*

Information can be balanced between pre-contractual and website information as long as there are clear rules on which information and how the information is disclosed on the website. Information on website and other market material is not regulated as pre-contractual documents as for example KIIDs and prospectus, therefore additional rules are needed.

At the moment, Article 13 of the Disclosure Regulation requires only that marketing communications do not contradict the information disclosed. The risk is that other channels to can be used to disguise relevant information or mislead individual investors, reason why ESAs should consider developing additional requirements in order to guarantee a balanced and clear information.

In addition, we recommend making a specific warning on greenwashing. The information provided need to be accurate, fair, clear, not misleading in order to avoid any form of greenwashing and miss-selling. A specific reference could be done with the definition of greenwashing on recital 9 of the taxonomy regulation: *"the practice of gaining an unfair competitive advantage by marketing a financial product as environmentally friendly, when in fact it does not meet basic environmental standards".*

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.

No. there is not a clear distinction between "sustainable investment products" in Article 9 and "products that promote environmental social criteria" in Article 8 of the Disclosure regulation. It necessary to provide a clear definition and guidance that will help to qualify the product category. Lack of a clear definition would end up in different interpretation by financial market participants and national supervision. Even if the Article 2(17) SFDR defines "sustainable investments"[27] [28] as *"an investment in an economic activity that contributes to an environmental objective"*. The environmental objectives are not explicitly referred to the 6 environmental objectives of the Taxonomy regulation. This is one of the major problems that could create regulatory divergences and undermine the correct interpretation of sustainable investment products and the use of the Taxonomy. We strongly recommend reinforcing the link between taxonomy and disclosure regulation in particular regarding the definition of sustainable investments.

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

We believe that the current descriptions are sufficient.

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?

We believe that the graphical representation could help individual investors to easily understand the sustainable features of the product as long as the same format of graphical representation (for example pie or bar chart) is used for the same product category. This would enhance comparability across sustainable products facilitating individual investors to understand the characteristics of the product.

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?

[27] Article 2 (17) SFRD: 'sustainable investment' means an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance;

[28] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R2088&from=EN

For the sake of transparency, we believe that the information on exposure to solid-fuel sectors should always be disclosed. As regards nuclear energy BETTER FINANCE believes that the treatment of nuclear energy (including the need for possible disclosures) needs further scientific and factual analysis and assessment (such as measures of risks (probability and magnitude) and environmental impacts of waste disposal).

Q20 : Do the product disclosure rules take sufficient account of the differences between products, such as multi-option products or portfolio management products?

BETTER FINANCE wishes to propose the same solution for Multi-Option Products as the one suggested in the consultations on the PRIIPs KID review as similar issues require similar solutions (*similia similibus curantur*). We believe that the pre-contractual disclosure for multi-option products must disclose, on each occasion and separately, the information for each possible combination of the underlying options. Only as such accurate and not misleading information can be provided to non-professional clients.

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?

According to Article 8 (1): *"Where a financial product promotes, among other characteristics, environmental or social characteristics, or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices…"*

As Article 8 (1) already mention "good governance practices", we believe the requirements in the RTS should capture the same elements presented in Article 2(17) of the disclosure regulation in order to avoid any miss-interpretation of what is considered good governance practices across different products. Once again, this problem is raised due to the creation of two different category: "sustainable investments" and "products that promotes among other characteristics, environmental or social characteristics". We encourage the ESAs to provide a clear definition of the two categories and a clear explanation of why there is a need to have this separation.

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?

According to recital (33): "*the do not significant harm principle is closely linked to the criteria to be developed in the context of the Regulation on the establishment of a framework to facilitate sustainable investment" (taxonomy)*. However, there is a fundamental contradiction with the environmental objectives. In the taxonomy the "do not significant harm" is addressed to the 6 environmental objectives of the taxonomy: (1) climate change mitigation, (2) climate change adaptation, (3) sustainable use and protection of water and marine resources, (4) transition to a circular economy, (5) pollution prevention and control and (6) protection of healthy ecosystem).

Therefore in the disclosure regulation, the six environmental objectives would need to be identified for the do not significant harm approach but they are not taken into consideration in the definition of sustainable investment (Article 2P.17 of the SFRD). This would create incongruences in terms of the information required to assess the sustainability risks and the identification/classification of the sustainable financial products based on their sustainable objectives. In addition, this would increase the complexity for individual investor which will be confronted with too many and unclear information.

In addition in the impact assessment, the ESAs mention that the policy option to be considered for the scope of the DNSH disclosure relate to the level of ambition among the draft principal adverse impact indicators and the environmental objectives in the taxonomy regulation. We recommend also to provide more clarifications on the relation between the principal adverse impact and the DNSH.

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?

Yes. The definition of investment strategies would be extremely important to streamline market practices, improve transparency and avoid mis-selling and greenwashing. These strategies can be defined in relation to the type of methodology the asset manager used to incorporate sustainability in the investment portfolio.

Looking at the vast composition of sustainable investments what makes the major difference is the approach that defines the investment objectives and policy of the fund. The approach used by asset managers will define and design the final product that is addressed to the retail investor.

The techniques applied by asset managers vary in terms of ambitions and on what they attempt to achieve as final investment output. As a start the disclosure regulation could define investment strategies as for example **exclusion-based ESG investing**, **integration-based ESG investing**, **engagement investing and impact investing**[29].

- **Exclusion-based ESG investing:** an exclusionary policy that provide guidelines on which assets or asset classifications need to be excluded from the portfolio.[30]
- **Integration-based ESG investing:** investment policy based on filtering companies based on Environmental social and governance factors. Filtering the universe of securities, the asset manager will integrate securities that have a favourable rating on ESG. The rating is generally produced by research firms or rating agency.[31]
- **Engagement investing:** This approach is based on the interaction between the institutional investor, as a shareholder, and the companies invested in. The institutional

[29] Matthew W. Sherwood Julia Pollard, Responsible Investing, an introduction to environmental, social and governance investments, Routledge, first published 2019
[30] Ibid.
[31] Ibid.

shareholder via dialogue and communication with the companies would act as a catalyst to push the companies that have environmental, social and governance issues to reduce/solve these issues and to improve their performance.

- **Impact investing:** this investment approach combines environmental, social and governance objectives with specific measurement of the non-financial impact in the real economy.

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?

Summary*: Article 39, 1.The section referred to in point (c) of Article 36 shall contain a list, in descending order of size, of the 25 investments constituting on average the greatest proportion of investments of the financial product during the reference period, including the sector and location of those investments.*
2. By way of derogation from paragraph 1, where the number of investments constituting on average 50 percent of the investments of the financial product during the reference period is less than 25, a list of those investments, in descending order of size, including the sector and location of those investments.

We agree with article 39 and 46 of the RTS. However, the information needs to be provided in a simple and understandable manner for individual investors. In addition, in order to guarantee comparability, the information needs to be provided in the same format. And not to overburden non-professional individual investors, it should be communicated via links to websites.

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.

Point (a) and (b) should be included in the pre-contractual documents, for example in a more descriptive document as the prospectus as they represent an important feature of the investment policy. Point (c) might be too technical and complex for the individual investor, therefore it could be foreseen on the website. Point (d) is an important information that need to be disclosed in pre-contractual disclosure for transparency reasons.

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)?

We believe that the information disclosed regarding the use of derivatives needs to follow the already existing rules listed in MIFID II. However, in case derivatives are used to attain the ESG characteristics or objectives it would be preferable to integrate this section with the geographical and narrative explanation of the investment proportion under article 15(2) and 24(2).

Q27 : Do you have any views regarding the preliminary impact assessments? Can you provide more granular examples of costs associated with the policy options?

N/A