FESE response to joint consultation on taxonomy related sustainability disclosures

Brussels 12th May 2021

Introductory comments

FESE welcomes the opportunity to provide a response to the ESAs' consultation on taxonomy related sustainability disclosures.

We support the approach of having only one set of RTS. We have observed some issues in the incoming regulations regarding discrepancies and overlapping requirements. Consolidating the SFDR and the Taxonomy Regulation RTS into one would therefore be very helpful to improve consistency.

We welcome the KPIs selected to measure taxonomy-alignment and believe that the approach proposed by the ESAs should grant enough flexibility for financial intermediaries to apply their calculation of KPIs and evaluate the taxonomy-alignment of investee companies. However, we are concerned that limiting financial intermediaries to the same approach for all investees of a given product/fund could prevent them from selecting the most material KPIs based on the nature of investee companies' businesses. While turnover is more indicative of the status quo, CapEx and OpEx are future-oriented and give investors the ability to label investments in companies which are in the process of becoming taxonomy aligned. Given the current lack of data on CapEx and OpEx, we anticipate that turnover will be chosen, which would hamper efforts to use the taxonomy as a tool to facilitate the transition.

Q1 - Do you have any views regarding the ESAs' proposed approach to amend the existing SFDR RTS instead of drafting a new set of draft RTS?

We welcome the approach of having only one set of RTS. We have observed issues in the incoming regulations regarding discrepancies and overlapping requirements (both minor and major ones). Consolidating the provisions from SFDR and the Taxonomy into one RTS would provide more consistency which would be very helpful.

Q2 - Do you have any views on the KPI for the disclosure of the extent to which investments are aligned with the taxonomy, which is based on the share of the taxonomy-aligned turnover, capital expenditure or operational expenditure of all underlying non-financial investee companies? Do you agree with that the same approach should apply to all investments made by a given financial product?

We welcome the KPIs selected to measure taxonomy-alignment. We believe that the approach proposed by the ESAs should grant enough flexibility for financial intermediaries to apply their calculation of KPIs and evaluate the taxonomy-alignment of investee companies. However, we are concerned that limiting financial intermediaries to the same approach for all investees of a given product/fund could prevent them from selecting the most material KPIs based on the nature of investee companies' businesses. Ultimately this could affect the performance assessment of investee companies, disregarding the diversity of business models and operations held within a fund.

Requiring investors to choose one KPI for all investments makes mixed strategies difficult to display. While turnover is more indicative of the status quo, CapEx and OpEx are future-oriented and give investors the ability to label investments in companies which are transitioning into being taxonomy aligned. Given the current lack of data on CapEx and OpEx, we would anticipate that turnover will be chosen, which would hamper efforts to use the taxonomy as a tool to facilitate the transition. While data availability will improve as reporting requirements for companies become applicable, for most portfolios this will only resolve the issue for a sub-set of companies, meaning that, if the same KPI has to be chosen for all investee companies, using CapEx and OpEx will likely still not be a feasible option.

Q3 - Do you have any views on the benefits and drawbacks of including specifically operational expenditure of underlying non-financial investee companies as one of the possible ways to calculate the KPI referred to in question 2?

N/A

Q4 - The proposed KPI includes equity and debt instruments issued by financial and non-financial undertakings and real estate assets, do you agree that this could also be extended to derivatives such as contracts for differences?

We consider that, if extended, it could become more difficult to calculate and may be difficult to determine which assets to include.

However, as more and more asset owners incorporate ESG approaches into their portfolios, asset managers have the duty and challenge of presenting strategies and products that meet their clients' criteria. In this context, ESG indices are key for enhancing access to ESG strategies with liquidity and appropriate portfolio diversification. Over the last few years, customer demand for listed ESG derivatives has emerged, with mainly the asset-management industry seeking flexible solutions to align their ESG investment mandates, trade longer-dated maturities and manage the granularity of clients' risk exposure while reducing trading costs.

We therefore believe that the proposed KPI for disclosure of the extent to which investments are aligned with the taxonomy should also include derivatives, as ESG derivatives are increasingly playing a role in channelling more capital into sustainable investments. In some instances it might, however, make sense to differentiate between short and long positions. In the case of ESG index futures, for example, long positions are used to manage exposure to the benchmark index, as well as to manage efficiently the cash flows in a portfolio. Long positions should therefore be added to the ESAs' KPI. However, short positions could be treated equally to long position but only when they are used to better manage the risk of the portfolio, and not for speculative purposes.

Q5 - Is the use of "equities" and "debt instruments" sufficiently clear to capture relevant instruments issued by investee companies? If not, how could that be clarified? Are any specific valuation criteria necessary to ensure that the disclosures are comparable?

N/A

Q6 - Do you have any views about including all investments, including sovereign bonds and other assets that cannot be assessed for taxonomy-alignment, of the financial product in the denominator for the KPI?

We would be in favour of including all investments in order to have a more true-to-life picture. The objective of the taxonomy is to channel financing towards the types of activities which we need to achieve environmental objectives. In displaying only those assets that can be assessed for taxonomy-alignment, there would be a risk of misrepresentation.

At the same time, we believe it is important to consider that a large number of green bonds have been issued in recent years prior to the establishment of an EU Green Bond Standard and the finalisation of the taxonomy. It would be important not to disregard companies or public entities which have taken the lead in issuing green instruments based on criteria different to those now included in the EU taxonomy framework, which was not previously available to them. Further consideration of how this can be reflected in the product information would be welcome This would provide a positive signal to all actors who engaged in green sustainable activities prior to the elaboration of the EU taxonomy framework.

Q7 - Do you have any views on the statement of taxonomy compliance of the activities the financial product invests in and whether those statements should be subject to assessment by external or third parties?

Regarding the statement of taxonomy compliance, we understand that these statements will be written by financial intermediaries and that they will be subject to an assurance provided by an auditor or third party review. We would support this approach provided it were implemented at product level and not extended to the underlying investments, in particular SMEs. We would be concerned if the requirement proposed in the RTS would inadvertently increase SMEs' funding costs for financial intermediaries to comply with their mandatory assurances.

The goal of the taxonomy is to create a common understanding of what counts as sustainable. If there is no external verification of these statements, we could see divergence in outcomes depending on how different parties determine taxonomy alignment, with a resulting high risk of greenwashing. To prevent this, not only third-party verification is needed but also clarification that all the criteria developed and set out by the legislative text need to be adhered to in the assessment of taxonomy alignment. This needs to be put in place both for companies reporting on their alignment as well as financial market participants making assessments in the absence of company-reported data. Without such clarification, we will continue to see broadly diverging approaches whereby some financial market participants check whether companies actually have in place the relevant measures required by the DNSH criteria and while others perform only a controversy check to assess DNSH compliance, or even only use sector-based standard coefficients without applying the substantial contribution criteria, the DNSH and the social safeguards.

External verification should look at the methodology applied, including which data was used, which assessment stages were applied and how they respond to the taxonomy requirements. This would make it possible to identify strong vs weak approaches and act accordingly.

The requirements for external assurance at the issuer level will be further discussed and negotiated in the context of the CSRD proposal and any potential requirements regarding assurance should be set following a proportional approach that considers the increased costs for SMEs.

Q8 - Do you have any views on the proposed periodic disclosures which mirror the proposals for pre-contractual amendments?

N/A

Q9 - Do you have any views on the amended pre-contractual and periodic templates?

N/A

Q10 - The draft RTS propose unified pre-contractual and periodic templates applicable to all Article 8 and 9 SFDR products (including Article 5 and 6 TR products which are a sub-set of Article 8 and 9 SFDR products). Do you believe it would be preferable to have separate pre-contractual and periodic templates for Article 5-6 TR products, instead of using the same template for all Article 8-9 SFDR products?

N/A

Q11 - The draft RTS propose in the amended templates to identify whether products making sustainable investments do so according to the EU taxonomy. While this is done to clearly indicate whether Article 5 and 6 TR products (that make sustainable investments with environmental objectives) use the taxonomy, arguably this would have the effect of requiring Article 8 and 9 SFDR products making sustainable investments with social objectives to indicate that too. Do you agree with this proposal?

N/A

Q12 - 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