Fondbolagens förening
SWEDISH INVESTMENT FUND ASSOCIATION

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# Response to the ESA Consultation on ESG Disclosures

## General comments

The Swedish Investment Fund Association (SIFA) is supportive of the European Commission's aim to create a strong framework for sustainable investment that supports the green transition. The ESAs' current work on the Disclosure regulation level 2 rules will be instrumental in providing financial market participants with an effective framework and investors with useful disclosures. SIFA recognises that this is a formidable task and welcomes the opportunity to provide comments on the proposed level 2 regulation. Providing investors with clear and comparable disclosures in the field of sustainability has been a priority for SIFA during the last couple of years as Swedish fund legislation has mandated sustainability disclosures since 2018.

SIFA agrees with the ESAs' analysis that although a stronger link between the Disclosure regulation and the Taxonomy regulation could have been favourable in terms of clarity, the definition of sustainable investments in article 2(17) of the Disclosure regulation does not feature a link to the taxonomy regulation. Although this may lack practical implications, it means that the definition of environmentally sustainable investments for the purpose of the disclosure regulation could differ from how environmentally sustainable investments are defined in the taxonomy regulation. The links between the two regulations are complex and additional clarity would be welcome.

As a general comment, SIFA believes that the sequencing of the Disclosure regulation, the Taxonomy regulation and the revision of the NFRD is unfortunate and should have been better coordinated at level 1 in order to achieve a more coherent regulatory framework and better prospects of reaching Union objectives of the European green deal. Therefore, we urge legislators, going forward, to ensure that requirements in the Disclosure regulation are adequately matched by provision of data under the NFRD. SIFA strongly supports the ESAs recommendation to the Commission to revise the level 1 application date of Disclosure regulation given the challenges faced by the industry. An extension of the application date to the 1 January 2022 would give market participants a more manageable timeline and would provide for a better alignment and coherence with other sustainable finance rules like the Taxonomy regulation and the imminent changes to the UCITS and AIFMD frameworks.

On the subject of timing, the application dates are rather unclear. It is our understanding that in respect of adverse impacts, everything related to policies and summaries (meaning all information referred to in articles 5 to 10 of the draft RTS not related to the reference period), should be published in the first year (by 30 June 2021 at the latest). Everything related to the reference period, which includes indicators and the table in articles 6, 8 and part of article 9 (policies to reduce the impacts), should be disclosed in the subsequent year (by 30 June 2022 at the latest). By 30 June 2023, the third report should include the historical comparison, as at least two reference periods are needed. If our understanding is correct, we fail to understand the purpose of article 53 of the draft RTS. Further clarity in this regard would be welcome.

As regards the timing of the first annual reports complying with the new obligations, it is our understanding that recital 32 of the Disclosure regulation clearly points to the importance of reporting on an *entire* financial year. Therefore, annual reports complying with the new obligations should be issued for the first time in 2023, regarding the year 2022. If the ESAs don't share this interpretation of the level 1 text, we would welcome an explanation as to the purpose of recital 32.

SIFA welcomes the proposal that the focus in the periodic disclosure should be on the success of the product in attaining its environmental or social characteristic or sustainable investment objective. However, we believe it is important to refrain from providing investors with information on the presumed sustainability impact, except in the few cases when this can be backed up by a causal link. Disclosure of assumptions of sustainability impacts without proper scientific backing risks serious damage to investors' trust. Additionally, such disclosure could be in conflict with marketing legislation. As a result we are concerned with the wording of the proposed articles 8 and 9 of the draft RTS where an "explanation of the reduction in principle adverse impacts achieved by the actions taken" should be provided. SIFA believes this risks encouraging financial market participants to take credit for positive changes where this in most cases will be very difficult to prove and may in fact be contrary to marketing legislation. SIFA would welcome a clarification regarding the meaning of "reduction in principle adverse impacts" and the difference between the "explanation of the reduction in principal adverse impacts achieved by the actions taken during the reference period" that should be provided according to articles 8(b) and 9 of the draft RTS.

SIFA notes that the ESAs are of the opinion that the possibility to address proportionality issues in the RTS is limited. The cost of implementing the proposed framework is in reality out of reach for most smaller asset managers and would in effect prohibit smaller firms from entering and competing in the market. The proposal would not only create an unlevel playing field between smaller and larger financial market participants but would also lessen competition and give the end-investor a more limited choice of suppliers. Less competition is not in the end-investors' interest. To prevent this SIFA would welcome any clarification, including in Q and As developed by the ESAs, on how the principle of proportionality can be applicable in relation to the Disclosure regulation.

## Adverse impacts

As currently drafted the rules on disclosure of adverse sustainability impacts at entity level will for financial market participants that offer a wide spectre of investment strategies lead to vast amount of information being disclosed. SIFA believes that the volume and detail of information means that it is unlikely to be useful to retail investors. If it is to be of any use to retail investors it will need to be simplified considerably. For comparison between financial market participants to be possible the data would need to be weighted and benchmarked. SIFA believes that the information at the level of the financial market participant can be useful to assess, over time, whether the industry is making sufficient progress in the area of sustainability. As such, the information should primarily be of interest to regulators and legislators. However, no such objective can be found in the level 1 text. Therefore, SIFA believes that the information should be shortened and simplified considerably in order to be useful to retail investors. Disclosure should be relevant, material and comparable. SIFA is therefore recommending that only six indicators be mandatory, while the remaining indicators should be voluntary and be disclosed based on materiality. However, we would recommend that the issue be revisited in the next couple of years, as this is a fast evolving area.

The main challenge in relation to adverse impacts will be the lack of available data. Further clarity is needed in relation to the steps financial market participants are required to take according to the proposed article 7(2) of the draft RTS. In practice it may be very difficult to obtain information directly from investee companies. SIFA would therefore suggest that the obligation in (a) and (b) be alternative, rather than cumulative. SIFA believes that the obligation under article 7(2)(a) of the draft RTS should be to use *reasonable efforts* to obtain the information. SIFA questions the usefulness in regulating the manner in which data should be collected. Additionally, we fail to see that such rules are required according to the level 1 mandate.

## Product disclosure

SIFA notes that the ESAs believe that the broad concept of 'ESG integration' should not be enough to justify that a product promotes environmental or social characteristics as this is now a requirement in the disclosure regulation (page 11). It is the interpretation of SIFA that the obligation for financial market participants to take ESG-risks into account will be enshrined in the foreseen changes to delegated acts in UCITS-, AIFMD-, MiFID-, IDD- and Solvency frameworks, rather than the Disclosure regulation, which is limited to the obligation to make sustainability-related disclosures. SIFA recognises that the practical implementation of ESG-integration as a method varies considerably from a bare minimum of taking ESG-risks into account to a method where ESG-risks and opportunities permeates the entire investment process and has a profound impact of the financial product. SIFA is of the opinion that only the basic taking account of ESG-risks will be regulated by the changes to delegated acts to the above mentioned frameworks, while more sophisticated ESG-integration methods must still be available to managers when managing products that promote environmental or social characteristics, provided these characteristics are binding on the financial market participant. The requirements to explain the binding elements of the strategy and obligation to disclose results is likely to prevent green-washing in this area.

In recital 24 it is stated that some exclusion strategies while showcased as material, actually lead to exclusion of only a limited number of investments. This pinpoints an important issue: which is more important – the amount of effort put in by the financial market participant in making sustainability related decisions or the level of sustainability of the end product? From our experience of ESG-disclosures in the Swedish market, SIFA would argue that the investor will probably focus on the latter. Investors in a product with an exclusion strategy will expect the product to be 'free' from the investments claimed by the financial market participant to be excluded. The amount of effort put in by the financial market participant or the number of actual excluded companies will in all likelihood be of less interest to the investor. In certain markets you may only have to exclude a handful of companies while in other markets many more exclusions are needed to achieve the same degree of sustainability. For example, for an actively managed equity fund with a Nordic focus and a 10 % global mandate, it would involve a disproportionate amount of work to carry out global screening for coal in order to disclose a minimum reduction rate. SIFA does not believe that the disclosure of a minimum reduction rate is appropriate. Such disclosure may only be relevant for index funds (but for which other performance indicators are more relevant when measuring deviation from index). Consequently, we believe that recital 24 should be deleted, as well as articles 17(c) and 26(c) of the draft RTS. At the same time, it is equally important that investors don't pay a premium or are misled regarding a specific sustainability strategy, where in fact that strategy does not entail any significant effort on part of the financial market participant. SIFA recognises that it is not an easy balance between the effort put in by a financial market participant and the actual sustainability level of the end-product. SIFA would like to draw the ESAs' attention to this issue as it is something that SIFA has grappled with in the process of developing the SIFA template for sustainability disclosures (attached for information). It is the view of SIFA that the focus here should be on accurate disclosure so that investors have appropriate expectations on the fund that they invest in.

SIFA questions the purpose of the far-reaching disclosure obligations regarding the control mechanisms put in place to monitor compliance (recital 25, articles 34(1)(f) and 35(1)(f) of the draft RTS). It is unclear to us why sustainability related compliance should be singled out in this way. A financial market participant should naturally ensure compliance in this field in the same way as for other issues such as risk-level and investment strategy.

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## Questions

**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?**

On a theoretical level SIFA is supportive of the proposed approach. There should be a balance between mandatory and voluntary indicators. The mandatory indicators are adequately linked to the taxonomy and these two regulations need to be considered in conjunction with one another. Mandatory indicators are good as they increase comparability of disclosures. However, the proposed approach entails insurmountable practical problems. Many of the proposed indicators are not yet developed enough to be used in the way proposed here, in disclosures to retail investors. And there will initially be a severe lack of available data which will lead to incomplete and possibly misleading disclosures.

We would suggest initially limiting the number of mandatory indicators to a smaller subset of more generic metrics that are meaningful, relevant across a large number of sectors and asset classes and measurable with available data. We would recommend the following indicators:

<u>**Environmental indicators:**</u>

- **KPI 1 (carbon emissions, broken down by scope 1 and 2):** Generally considered relevant for all assets. Data for scope 3 emissions is generally 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 investors. Moreover, the issue of double-counting within scope 3 and between scope 2 and scope 3 emissions is not yet sufficiently addressed.

- **KPI 2 (carbon footprint for scope 1 and 2 emissions):** Generally considered relevant for all assets. Calculation methodologies for scope 1 and 2 are established in the market, but are asset class specific. The suggested methodology is based on the investee company's enterprise value which is not fully adequate for direct equity investments.
- **KPI 5 (total energy consumption from non-renewable sources and share of non-renewable energy consumption):** 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.
- **KPI 7 (energy consumption intensity):** 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.

**Social and employee, respect for human rights, anti-corruption and anti-bribery indicators:**
All indicators proposed in this section are generally only applicable to investments in companies and are too granular to be assessed based on ESG data as currently available. Therefore, as an alternative we suggest using the following high-level mandatory KPIs in order to report on the relevant aspects of portfolio investments in companies:

- **No signatories to UN Global Compact** (share of investments in investee companies that are not committed to the UNGC principles)
- **Severe controversies/breaches of UN Global Compact** (share of investments in investee companies that are involved in severe violations of the UNGC principles)

Adherence to and severe violations of UNGC is already measured by a number of ESG data providers since many years. Data on these aspects is therefore readily available to the market, even though the interpretation of severe violations is not fully aligned.

It should be noted that although we would recommend the mandatory indicators above, disclosure will not be straightforward. There will not be complete data. And, unfortunately, it is unlikely that investors will understand the limitations of this type of disclosures (for example, investments in manufacturers of solar panels will generate a principle adverse impact in terms of Co2 emissions but may still be a positive investment from a sustainability point of view). We would welcome clarity on how the indicators should be disclosed for asset classes other than equity, such as sovereign investments and short positions. And further clarification is also needed on for example whether a look through principle should be applied for certain instruments. For example, do investments in the banking sector require an analysis of the respective banks' lending? This would be very difficult; as key performance indicators are often lacking.

We would also encourage the ESAs to clearly motivate their choice of each individual indicator, in order to better understand the logic behind it. As this area is developing quickly, we would recommend the question be revisited in a couple of years in order to add and possible adjust the list of mandatory indicators.

Financial market participants should be free to disclose additional indicators based on materiality. As it is currently drafted, the logic behind the choice of voluntary indicators is unclear. Would there not be an incentive to include a less serious adverse impact? And also, there may not necessarily be additional relevant and material adverse impacts. We would recommend that it be clarified that additional, voluntary indicators should be disclosed based on materiality.

**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?**

No. All financial market participants do not have the same capacity and ability to perform a full due diligence on investee companies and will have to rely on data providers. The cost of buying data and amount of work needed for the disclosure will be unproportionate, in particular for smaller financial market participants, and in relation to the deemed usefulness of the disclosure for end-investors. Also, for a smaller manager, a single fund will impact the manager's result more significantly than for a larger manager with hundreds of funds. Therefore, the suggested approach favours larger financial market participants which SIFA believes was not the ESAs' intention . SIFA would welcome any clarification, including in Q and As developed by the ESAs, on how the principle of proportionality can be applicable in relation to the disclosure regulation. Please also see our response to question 27.

Additionally, many of the proposed indicators are not relevant for other assets apart from equities and corporate bonds and it is therefore unclear how the proposed rules should apply for some types of products.

**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?**

Please see our response to question 1.

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

Please see our response to question 1 for which indicators we recommend be mandatory. For each indicator we would recommend additional information on:

- the proportion of investment for which the indicator is relevant,
- the proportion of the investment for which there is data,
  (a) the proportion of data reported,
  (b) the proportion of data that is estimated.

On the basis of that information a result can then be disclosed for each mandatory indicator.

**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)?**

Please see our response to question 1 for a list of mandatory indicators that we recommend.

*Guiding principles for disclosure of indicators*
Ideally, the principles of materiality (for different industries) and comparability (between asset managers) should be decisive in the choice of indicators. One industry might have very energy-consuming processes, but the asset manager can choose to invest in companies within the industry that has low energy use compared to peers. However, this will lead to worse results compared to a manager only invested in other sectors. Unfavourable results don't necessarily mean that the manager has less ESG-focus. The indicators seem to reward investments in certain industries. This will specifically benefit managers that only have a few focused funds and can avoid certain sectors. Thereby the comparability across asset managers is difficult, if only looking at the indicators provided in the templates.

There should ideally be more focus on outcome-based indicators to the extent such information is available. The information that a policy is in place is not necessarily useful since the policy could be very vague, unambitious, or not even adhered to. The absence of a certain policy in an investee company does not automatically mean that adverse impact is caused. It does not even necessarily mean that the risk of adverse impacts is greater – that could depend on other factors such as type of sector, geographical location and judiciary system of a country.

We therefore recommend a short list of mandatory indicators and that other indicators should be disclosed by the financial market participant based on materiality. Overall, and to the extent possible, we would also recommend trying to simplify, as the information is unlikely to be understood by retail investors. In general, we believe that information aggregated at the level of the financial market participant is unlikely to be particularly useful to investors but we acknowledge this is enshrined in level 1 of the Disclosure regulation. We encourage the ESAs to provide a clear rationale for why a particular indicator should be mandatory.

*Forward looking-indicators*
Unfortunately, the proposed indicators fail to capture investments that have an appropriate plan for transition. It is difficult to measure and prove future plans, but from an ESG perspective it's preferable to invest in for example an energy company with a good transition plan, but that might not be visible in the current indicators. However, we believe it is too early to include CCS and percentage of investments adhering to Paris-aligned pathways as methodologies are not yet sufficient advanced. Scope 4 emissions should not be included. There is not sufficient data on scope 3 emissions, let alone scope 4. We would recommend that the issue be revisited in the future. An option that may be worth considering is adding an indicator on whether an investee company has a policy on carbon neutrality (bearing in mind that such indicator would not be 'adverse').

*Practical problems*
The biggest problem is currently the lack of data from investee companies, in particular in emerging markets. This is likely to improve over time. However, clarification is needed regarding what to do in the meantime. For example, what information should be disclosed when data is only available for 10 % of the investments? There is also the problem of how the indicators should be disclosed in relation to asset classes other than equity and corporate bonds. How should the short side in hedge funds be reported? SIFA would encourage the ESAs to provide examples in this regard. An unintended and unfortunate consequence of pressure from financial market participants on investee companies to present policies on topics that are not relevant to them is it risks undermining financial market participants' shareholder engagement.

**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?**

a) Yes, if this metric is also used in the taxonomy it is relevant.
b) No, there is not sufficient data.

**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?**

SIFA is supportive of this proposal.

**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?**

No, such indicators are not yet sufficiently developed. Additionally, it would appear that such metrics would be positive rather than "adverse".

**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?**

Yes. Please see our response to question 1 for which indicators we recommend should be mandatory. Remaining indicators should be voluntary.

**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?**

SIFA believes that ten years is too long. In all likelihood the metrics will have evolved in that time, making ten-year-old information irrelevant and impossible to compare. As the information is for end investors five years is a more appropriate historical comparison. If the ESAs maintain their position that ten years is appropriate, we would welcome an explanation as to how this is consistent with the mandate in level 1.

**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?**

Reference period and methodology should be harmonised. SIFA would suggest that calculations are based on the overall portfolio composition at every twelve, or at most six, months' interval. We don't believe that the risk for "window dressing" should be exaggerated as any (financially unmotivated) reallocation of portfolio holdings entails transaction costs and risks reducing the net performance of financial products.

We would welcome clarification on how long an indicator should be disclosed. For example, for how long should a particular case of severe human rights violation be disclosed, only for the particular year that it occurred?

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

Yes.

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

Templates should include both environmental and social data. Templates should be limited in length and detail and discretion should, where appropriate, be left to financial market participants. Information on the strategy used to promote ESG characteristics or to pursue sustainable investment objectives should be included (i.e. whether products make use of ESG-integration, exclusions, best-in-class strategies, etc.) Consumer testing should be carried out to ensure that disclosure is useful to investors.

Swedish fund legislation has included mandatory sustainability disclosures since 2018. In order to increase comparability and promote simplicity in retail disclosures SIFA has developed a template[1] (please see attached) for sustainability disclosures, mandatory for all SIFA members but also used more widely in the Swedish market. The template is simple, in particular in comparison to what is proposed in chapter iii. However, when Finansinspektionen (the Swedish financial supervisory authority) carried out consumer testing on how well the template was understood the results showed that the information was still perceived as complex by consumers. As a result, SIFA has tried to make adjustments to the template to improve its consumer friendliness. SIFA is not suggesting that the template be used here in this context but it can serve as an interesting reference point when it comes to the level of complexity that is appropriate for retail clients.

**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.**

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**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?**

Generally, we believe the information should be on the website to avoid overburdening the prospectus. According to our understanding investors to a greater extent absorb information by visiting websites than by reading the prospectus. The information will therefore most likely reach a greater audience if published on the website.

SIFA recommends that the disclosures according to article 33 of the draft RTS can be made available directly to investors in case of portfolios managed on a discretionary basis in order to avoid a breach of bank secrecy. Please see our reply to question 20.

**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, this is unclear. It is unclear in the level 1 text and sufficient guidance is not provided in the draft RTS. Unfortunately, the draft delegated regulations on the integration of sustainability considerations under MiFID II and IDD has added to the confusion.

*"Warning" may be misleading*
According to the proposed articles 16(1) and 34(3) of the draft RTS the following statement should be provided for article 8 products: "This product does not have as its objective sustainable investment". This statement will most likely confuse investors. In particular as the difference between article 8 and article 9 products is not very clear either in the level 1 text or in the draft RTS. It is likely that investors will have trouble separating article 8 and article 9 products. SIFA therefore proposes that the statement is replaced by the

[1] The template is based on the SWESIF's template for sustainability disclosures.

following standard statement: ”This product promotes environmental and/or social characteristics ”. As an alternative the statements can be combined: “This product promotes environmental and/or social characteristics but does not have as its objective sustainable investment.”
It is also unclear if the characteristics need to be on the individual investee company level, or if it’s sufficient that it’s on the fund level. For example, a fund could strive to have a good key figure on the portfolio level (e.g. low carbon or good gender balance) without all of the investee companies necessarily having activities promoting these targets, but on the portfolio level they could still be fulfilled.

*Passively managed products*
SIFA believes that a clarification of the proposed articles 21(2) and 34(4) of the draft RTS is needed. It is SIFA’s understanding that these articles are only applicable where a benchmark has been chosen to achieve the environmental or social characteristic, i.e. “passive” strategies. Therefore, the second paragraph of article 21 appears superfluous. We fail to understand how a passively managed product, that hasn’t intentionally chosen an ESG-screened index could be classified as an article 8 or 9 product. Is it the ESAs’ interpretation of article 8(1)(b) of the Disclosure regulation that it is applicable to other strategies than passively managed products? Article 21(2) of the draft RTS seems to imply this. As a consequence, it is also unclear in which situations articles 36(d) and 40 of the draft RTS would apply.
In relation hereto, articles 30 and 35(4) of the draft RTS are applicable to products referred to in article 9(1) in the Disclosure regulation. It is SIFA’s understanding that these articles are only applicable where a benchmark has been chosen to achieve the sustainable investment objective, since the information required according to the articles is only relevant for passively managed products. Since this is not entirely clear in the level 1 text, SIFA would like clarification that articles 30 and 35(4) of the draft RTS are only applicable to passively managed products.

In relation to recital 29, products that pursue a low-carbon investment objective since before the union climate-related benchmark were in place could use certain exclusion criteria that are not covered by the EU Paris aligned or the EU Climate transition benchmarks. In order not to violate the promise to the clients it is important that these products may continue using these exclusion criteria even though it could lead to that the product deviates from the union benchmarks.

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

No. SIFA would welcome an explanation of “direct holdings”, and whether this encompasses anything besides shares and corporate bonds? Does use of the term “entity” in recital 3 imply that also sovereign debt instruments are to be regarded as direct holdings? We also note article 15(2)(b)(ii) of the draft RTS where money market instruments are mentioned – should these always be regarded as the “remainder of the investment”?

SIFA believes that more clarity is needed regarding “the purpose of the planned remainder of the investments” in article 15(2)(b)(ii) and recitals 20 and 30 of the draft RTS. For example, an index manager may, for a limited period and to handle the issue and redemptions in a fund, need to gain exposure to a particular market through index futures where a sustainability screened index is not available (e.g. emerging markets). Such exposure is clearly an indirect holding according to article 15(2)(b)(i). However, such exposure is not required to be explicitly disclosed according to article 15(2)(b)(ii) as only hedging, money market instruments and instrument for which there is insufficient data are mentioned in (ii). This appears contradictory. SIFA would suggest rephrasing the list in article 15(2)(b)(ii) so that it is non-exhaustive and thus, also covers liquidity issues.

**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?**

Yes, this could be misleading. In many cases multiple characteristics as well as multiple methods will be used in the same financial product. Mixing different characteristics and methods in the same graphic representation may be challenging and may be difficult for investors to understand. If integration or best in class strategies are used, it may well be that 100 % of the portfolio is screened. This may be misleading and possibly make it difficult for investors to see the difference between article 8 and 9 products.

There needs to be more guidance regarding how shorted instruments should be treated.

**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?**

Yes, we agree. SIFA welcomes a definition of 'fossil fuel sectors' but unfortunately as currently drafted it is very unclear. Are liquid and gas fossil fuels intentionally excluded? The scope of 'distribution' may need further clarification and also how fossil fuels can be disclosed in relation to sovereign debt investments. SIFA would also like some more clarity on the relevance of the exception of investments related to clean vehicles. Moreover, should disclosure refer to any turnover (meaning that the threshold is "0") or to investee companies that meet a certain level of turnover (% threshold). We welcome that the definition does not include services in relation to solid fossil fuels. Services companies can often contribute to decreasing the adverse environmental impacts in the fossil fuel sector.

No other sectors should be included.

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

No, unfortunately the rules do not take sufficient account of differences between products. In fact, SIFA would argue that the proposed rules don't even take sufficient account of difference between types of funds.

The classification of portfolio management as a product, rather than a service, in the level 1 of the Disclosure regulation entails a number of challenges. It necessitates that the level 2 rules adequately accommodate for the specificities of portfolio management. In particular, SIFA is concerned with the requirement to publish information on clients' portfolios on the website. In our view this publication could constitute a breach of bank secrecy rules as there is a risk that the identity of the client could be exposed. In the case of model portfolios, the disclosure obligations as currently drafted would lead to massive repetition of information that is likely to deter clients from accessing information on the website. SIFA urges the ESAs to attempt to find a more practical solution within the constraints of the level 1 text. SIFA would recommend that disclosure should be limited to representative model portfolios only. And to note that the requirements regarding engagement policies are difficult to fulfil since a portfolio manager is not entitled to vote on behalf of the client unless this has been specifically agreed with the client – which is not standard practice.

Additionally, the focus is clearly on products distributed in the retail market and the proposed disclosures may be inappropriate for professional investors.

**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?**

Yes, two different 'levels' of good governance practices would be confusing. The standard required in article 2(17) of the Disclosure regulation is reasonable also for article 8 products.

**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?**

From a retail investor perspective this is much too complicated. In particular in relation to article 8 products, that may include a limited proportion of sustainable investments. The mandate to the ESAs to develop detailed rules on the "do no significant harm" (DNSH) principle is in relation to article 9 products, not article 8 products. It is the ESAs' proposal to categorise the investments of article 8 products that has resulted in a perceived need to extend the DNSH principle also to article 8 products (or at least the part of the product that can be classified as sustainable investments). It is unlikely that the extension of the DNSH principle to article 8 products was anticipated at level 1. SIFA therefore proposes that the requirements in articles 16(2)(a), 34(3) and 38 of the draft RTS are removed.

Additionally, in order to determine whether the DNSH principle has been fulfilled, thresholds in relation to the indicators are necessary.

We are concerned that the DNSH principle in the Disclosure regulation may be inconsistent with the same principle in the Taxonomy regulation. The principle in the draft RTS will apply at the investee company level. This differs from the Taxonomy regulation where the consideration is at the level of the economic activity. We recommend that the consequences of this inconsistency should by carefully analysed.

**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, this would be useful for investors. Easily comprehendible and well established definitions can be found in the Global Sustainable Investment Review. We would welcome common definitions of the most widely used strategies but definitions should not be in the format of an exhaustive list. It is important that innovation is not stifled in any way.

**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?**

Yes.

**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.**

Generally, we believe that investors prefer website disclosures and it would have the added benefit of not overburdening the prospectus. Website disclosure could perhaps be coupled with a brief note in the prospectus, directing the reader to more information on the website.

As regards a) SIFA believes that disclosing on a minimum reduction rate is not appropriate and that this requirement should be deleted. The actual number of excluded companies depends on in which market the product invests. In certain markets you may only have to exclude a handful of companies while in other markets many more exclusions are needed to achieve the same degree of sustainability. For example, for an actively managed equity fund with a Nordic focus and a 10 % global mandate, it would be disproportionate to carry out global screening for coal in order to disclose a minimum reduction rate. Disclosure on a minimum reduction rate may only be relevant for index funds (but for which other performance indicators are more relevant when measuring deviation from index). Please see our introductory comment regarding recital 24.

We would recommend that b) and d) be disclosed on the website instead. A financial market participant's policy is likely to apply to a number of products and is therefore more appropriate on the website. Information on data sources may need frequent updating and is therefore more appropriate as website disclosure.

**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)?**

It would be better to integrate derivatives with the graphical (if possible) and narrative explanation of the investment proportions. At least those derivatives that are used to achieve the investment strategy (as opposed to those used for liquidity purposes) should be included. It would be preferable if smaller derivatives positions used for efficient portfolio management purposes could be held temporarily, without needing to fulfil all the ESG-disclosure requirements of it.

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

The implementation of the framework will require massive resources, and include a large number of people. Systems will need to be developed. It's likely that some firms may need to ten-fold their budget when it comes to buying ESG-data. Some firms will need to hire new competence. The costs associated with disclosing adverse impacts at entity level seems unproportionate in relation to its likely usefulness to investors.

The cost of implementing the proposed framework is in reality out of reach for most smaller asset managers and would in effect prohibit smaller firms from entering and competing in the market. The proposal would not only create an unlevel playing field between smaller and larger financial market participants but would also lessen competition and give the end-investors a more limited choice of suppliers. Less competition is not in the end-investors' interest.

# SIFA Standard for sustainability information

[The sustainability information included in the fund's prospectus and annual report shall be presented in the following manner:]

### *Sustainability information*

☐ Sustainability aspects are taken into account in the management of the fund.
☐ Sustainability aspects are not taken into account in the management of the fund.

[If the first option is checked, the fund management company shall also provide information under the following headings. If the second option is checked, the remaining headings shall not be included in the sustainability information. However, where sustainability aspects are not taken into consideration in the management of a fund but where the fund's investment policy nonetheless means that the fund is free from certain products and services, information about this can be provided under the heading 'negative screening'. The purpose of this is to facilitate for consumers wishing to use the search function.]

Fund management company's comments:

[In this comment the fund management company can provide general information that facilitates an assessment of the fund in respect of sustainability. The comment can, for example, include the following information:

- If the fund is sustainable for reasons other than that sustainability work is carried out in respect of the fund, e.g. if the fund is to be regarded as sustainable on account of its investment strategy (debt instruments issued by the Swedish government is one example).
- For funds, e.g. mixed/balanced funds, where the investment strategy entails an inability to carry out sustainability work for part of the portfolio, this comment should specify the portion of holdings for which sustainability work can be carried out.
- For funds of funds this comment should specify whether the sustainability work refers to the *selection of underlying funds* or if the fund of funds adopts a *look-through approach to its underlying funds* and selects funds whose holdings corresponds to the fund of funds' sustainability principles.

Other clarification that the fund management company wishes to make can also be made here.]

### *Sustainability aspects taken into account in the management of the fund*

[The following check options shall be presented under this heading and applicable options checked.]

☐ Environmental aspects (e.g. the companies' environmental and climate impact).
☐ Social aspects (e.g. human rights, employee rights and equal opportunity).

☐ Corporate governance aspects (e.g. shareholders' rights, issues relating to remuneration for senior executives, and anti-corruption work).
☐ Other sustainability aspects.
[Specify any other sustainability aspects taken into account.]

*Methods used for the sustainability work*

☐ **Positive screening**
[If this method is used, all check options shall be shown and applicable options checked. For both options full information shall be provided regarding the fund management company's methods. The information shall be provided on the fund management company's website and shall enable readers to understand the reasons behind the standardised options checked below.]

☐ Sustainability aspects are critical in the manager's choice of companies.

The fund has specific and explicit criteria for positive selection of companies, based on environmental, social and business ethics issues. An analysis of the companies' sustainability work is critical to the selection of the companies in the fund.

This option also refers to funds that select companies on the basis of a specified sustainability-related theme, such as climate, water, ecotechnology, or social sustainability, and to funds that only invest in projects or operations with quantifiable social or environmental benefits.

[If sustainability aspects are critical in the manager's choice of companies, the method used should be summarised in the comment. This applies to both fundamental and quant based strategies that use sustainability as their basis.]

Fund management company's comments:

☐ The manager of the fund take sustainability issues into account.

Sustainability issues are taken into account in the context of corporate economic analyses and investment decisions and play a part, but not necessarily a crucial one, in determining which companies are selected for inclusion in the fund.

This option refers to funds which explicitly and systematically integrate sustainability aspects into their economic analyses and investment decisions. Sustainability aspects are explicitly part of the investment process, are continuously analysed, and affect the fund's investments.

Fund management company's comments:

Other

☐ Other method of positive screening used by the fund.

Fund management company's comments:
[Specify the method used by the fund.]

☐ **Negative screening**

[If this method is used, applicable check options only shall be shown.]

The fund does not invest in companies that are involved in the following products and services. A maximum of 5% of the turnover in the company in which the investment is made may entail operations attributable to the specified product or service.

Products and services

The following check options can be used where sustainability aspects are not taken into account in the management of a fund but where certain products and services are not included in the fund as a result of its investment policy.

☐ Cluster bombs, landmines

Fund management company's comments:

☐ Chemical and biological weapons

Fund management company's comments:

☐ Nuclear weapons

Fund management company's comments:

☐ Weapons and/or munitions

Fund management company's comments:

☐ Alcohol

Fund management company's comments:

☐ Tobacco

Fund management company's comments:

☐ Commercial gambling operations

Fund management company's comments:

☐ Pornography

Fund management company's comments:

☐ Fossil fuels (oil, gas, coal)

Fund management company's comments:

☐ Coal

Fund management company's comments:

[This option refers to funds that exclude coal, but not other fossil fuels.]

☐ Uranium

Fund management company's comments:

☐ Genetically modified organisms (GMO)

Fund management company's comments:

☐ Other

Fund management company's comments:

[Specify any other products or services excluded.]

International norms

International norms refer to international conventions, laws and agreements such as the UN Global Compact and OECD guidelines for multinational companies that relate to issues concerning the environment, human rights, labour practices, and business ethics.

[This option refers to funds that apply reactive sustainability analysis and exclude companies because they violate international norms. Select one of the two options below, depending on how comprehensive the exclusions made due to violations of international norms are. Merely a review with regard to norm violations – but where the violations do not result in exclusions – are insufficient grounds for checking either of these options.]

☐ The fund does not invest in companies that violate international norms. The assessment is carried out either by the fund management company or a third party.

[If the fund also excludes companies suspected of and investigated with regard to breaches, this should be specified in a separate comment.]

Fund management company's comments:

☐ The fund does not invest in companies which do not address identified problems or where the fund makes the assessment that the company will not address the problems within a time frame deemed reasonable in that specific case.

This option refers to funds that draw up an action plan for questionable companies which are excluded if the specified conditions are not met within a specified period of time.

Fund management company's comments:

Countries

☐ For sustainability reasons, the fund does not invest in companies involved in certain countries/interest-bearing securities issued by certain states.

This option refers to funds that carry out a country-specific sustainability analysis that results in the exclusion of companies involved in certain countries or of interest-bearing securities issued by certain states. [Specify which countries are excluded and the reasons for the decision. Please note that this option refers solely to sustainability-related country analysis against explicit sustainability criteria. Geographic restrictions applied for other reasons, such as the fund's investment objective, do not constitute grounds for checking this option.]

Fund management company's comments:

Other

☐ Other

Fund management company's comments:

[Specify any other exclusionary criteria.]

☐ **The fund management company influences**

[If this method is used, applicable check options only shall be shown.]

The fund management company exercises its investor influence to influence companies on sustainability issues.

[Note that if the fund management company is to check this option, the exertion of influence must be relevant to the fund in question.]

The fund management company engages with companies with a view to influencing them to adopt a more sustainable approach.

☐ In-house investor influence

Fund management company's comments:

☐ Investor influence in cooperation with other investors

Fund management company's comments:

☐ Investor influence through external suppliers/consultants

Fund management company's comments:

☐ Voting at General Meetings

Fund management company's comments:

☐ Participation in nomination procedures in order to influence the composition of the Board

Fund management company's comments:

☐ Other forms of investor influence

Fund management company’s comments:

[Specify]