European Securities and Markets Authority

EUROPEAN BANKING AUTHORITY

EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY

JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

Response form for the Joint Consultation Paper concerning ESG disclosures

23 April 2020

Date: 23 April 2020
ESMA 34-45-904

JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

Responding to this paper

The European Supervisory Authorities (ESAs) invite comments on all matters in this consultation paper on ESG disclosures under Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial sector (hereinafter "SFDR") and in particular on the specific questions summarised in Section 3 of the consultation paper under "Questions to stakeholders".

Comments are most helpful if they:

- contain a clear rationale; and
- describe any alternatives the ESAs should consider.

When describing alternative approaches the ESAs encourage stakeholders to consider how the approach would achieve the aims of SFDR.

Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

- Insert your responses to the questions in the Consultation Paper in the present response form.
- Please do not remove tags of the type <ESA_QUESTION_ESG_1>. Your response to each question has to be framed by the two tags corresponding to the question.
- If you do not wish to respond to a given question, please do not delete it but simply leave the text "TYPE YOUR TEXT HERE" between the tags.
- When you have drafted your response, name your response form according to the following convention: ESA_ESG_nameofrespondent_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESA_ESG_ABCD_RESPONSEFORM.
- The consultation paper is available on the websites of the three ESAs and the Joint Committee. Comments on this consultation paper can be sent using the response form, via the ESMA website under the heading 'Your input - Consultations' by **1 September 2020**.
- Contributions not provided in the template for comments, or after the deadline will not be processed.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESAs rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESAs Board of Appeal and the European Ombudsman.

Data protection

The protection of individuals with regard to the processing of personal data by the ESAs is based on Regulation (EU) 2018/1725[1]. Further information on data protection can be found under the Legal notice section of the EBA website and under the Legal notice section of the EIOPA website and under the Legal notice section of the ESMA website.

[1] Regulation (EU) 2018/1725 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data, and repealing Regulation (EC) No 45/2001 and Decision No 1247/2002/EC, OJ L 295, 21.11.2018, p. 39.

General information about respondent

Name of the company / organisation	CDP Worldwide (Europe) gGmbH
Activity	Others
Are you representing an association?	☒
Country/Region	Europe

Introduction

Please make your introductory comments below, if any:

<ESA_COMMENT_ESG_1>
CDP Europe is part of the global CDP non-profit network, that drives companies and governments to reduce their greenhouse gas emissions, safeguard water resources and protect forests. Voted number one climate research provider by investors and working with 515 institutional investors with assets of US$106 trillion, we leverage investor and buyer power to motivate companies to disclose and manage their environmental impacts. Globally, over 8.400 companies with over 50% of global market capitalization disclosed environmental data through CDP in 2019, including more than 2.100 European companies representing approximately 76% of the European market capitalization. This is in addition to the over 950 cities, states and regions globally who disclosed – including more than 215 in Europe – making CDP's platform one of the richest sources of information globally on how companies and governments are driving environmental change.
<ESA_COMMENT_ESG_1>

Q1 : Do you agree with the approach proposed in Chapter II and Annex I – where the indicators in Table 1 always lead to principal adverse impacts irrespective of the value of the metrics, requiring consistent disclosure, and the indicators in Table 2 and 3 are subject to an "opt-in" regime for disclosure??

<ESA_QUESTION_ESG_1>
We generally agree that indicators in table 1 reflect principal adverse impacts. However, for data users the absolute values may not mean much if they cannot compare them to the performance of traditional, non-sustainable financial products. Therefore, we believe the disclosure requirement should be extended to all financial products with future revisions of the regulation.

One exception where an indicator does not necessarily lead to principal adverse impacts could be energy consumption intensity. This metric does not reflect the source of energy consumed. Companies who primarily consume renewable energy would not create significant adverse impacts even if their intensity was high.

<ESA_QUESTION_ESG_1>

Q2 : Does the approach laid out in Chapter II and Annex I, take sufficiently into account the size, nature, and scale of financial market participants activities and the type of products they make available?

<ESA_QUESTION_ESG_2>
NA
<ESA_QUESTION_ESG_2>

Q3 : If you do not agree with the approach in Chapter II and Annex I, is there another way to ensure sufficiently comparable disclosure against key indicators?

<ESA_QUESTION_ESG_3>
NA
<ESA_QUESTION_ESG_3>

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

<ESA_QUESTION_ESG_4>
NA
<ESA_QUESTION_ESG_4>

Q5 : Do you agree with the indicators? Would you recommend any other indicators? Do you see merit in including forward-looking indicators such as emission reduction pathways, or scope 4 emissions (saving other companies´ GHG emissions)?

<ESA_QUESTION_ESG_5>
In relation to greenhouse gas emissions, we recommend using the following indicators:

- "GHG emissions Scope 1+2 owned by the fund" in metric tons CO2 equivalent, calculated as per 1f of Annex 1
- "GHG emissions Scope 1+2+3 owned by the fund" in metric tons CO2 equivalent, calculated as per 1f of Annex 1
- "GHG footprint, Scope 1+2", in metric tons CO2 equivalent per 1 million EUR invested; calculated as per 1g of Annex 1

- "GHG footprint, Scope 1+2+3" in metric tons CO2 equivalent per 1 million EUR invested; calculated as per 1g of Annex 1; and
- Weighted average GHG emissions intensity.

We believe the total value chain emissions (Scope 1+2+3) should be separately reported as the uncertainty around scope 3 emissions data is much higher as is mostly modelled / estimated.

We believe the PAI statement should contain a note that disclosers should disclose these indicators in line with the GHG protocol or the ISO 14064-1:2018 standard (see also page 19 of the EC guidelines on non-financial reporting – supplement on reporting climate-related information as a reference).

We strongly agree that forward looking indicators are generally more decision-useful than backward looking indicators such as the carbon footprint. One additional indicator could be:

"Total exposure to companies without any public, medium-term (e.g. 5-15 year timeframe) emissions reduction target covering relevant value chain emissions".

This information is important and valuable to understand a company's forward-looking ambition for reducing GHG emissions in the future. And it is increasingly being disclosed by companies and also recommended in the EC guidelines on non-financial reporting – supplement on reporting climate-related information, see page 21.

A historical pathway related metric could be:

"Weighted average exposure to companies without Scope 1 & 2 emissions reductions over the previous 3 years".

This metric could also be further specified by relating it to annual reduction requirements as laid out in the PAB/CTB Benchmark regulation (i.e. 7% annual reduction).

Scope 4 emissions savings would not relate to adverse impacts but rather positive impacts. There is also not a standard or accepted method for measuring / benchmarking emissions savings and development of such as standard would take a significant amount of time and effort.

The disclosure requirement currently proposed in the draft RTS of exposure to include only 'solid' fossil-fuels is insufficient and inconsistent with the objectives related to climate change as promoted by the Paris Agreement, the SDGs and the EU climate strategy. Exposure to all fossil-fuels including oil & gas must therefore be included.

Regarding the metrics relating to energy performance, it is unclear why there is only a focus on energy consumption. Indicators on energy generation are missing so as to capture a portfolio's exposure to non-renewable energy generation. In the EC guidelines on non-financial reporting – supplement on reporting climate-related information the EC itself recommends companies to disclose energy consumption and / or production data (see page 22 of the guidelines).

Therefore, we suggest the following KPIs:

"Total gross energy generation from non-renewable sources owned by the fund" expressed in MWh.

The proposed indicator #5 on energy consumption could be simplified and aligned as follows:

"Total non-renewable energy consumption owned by the fund" expressed in MWh

The calculation for these two ownership based indicators could follow the same logic of the carbon emissions as described in 1f of Annex I.

A third energy related indicator could be:

“Weighted average share of non-renewable energy production and/or consumption” expressed in %

Our evidence suggests that data on corporate energy consumption and generation is widely available in sufficient quality. For example, 80% of companies in the MSCI Europe index (n = 430) report energy consumption and production data from renewable and non-renewable sources to CDP each year. The breakdown by type of renewable energy source is less frequently disclosed.

The current proposed energy metrics 6, 7 and 8 seem to provide the least value-added and could in our opinion be omitted in an attempt to shorten the list of KPIs.

However, the ESAs could consider introducing a forward-looking indicator such as:

“Weighted average share of companies without any public, medium-term (e.g. 5-15 year timeframe) renewable energy production or consumption target”, expressed in %

This again would align well with the recommended corporate disclosures in the EC guidelines on non-financial reporting – supplement on reporting climate-related information (page 22)

CDP would be happy to assist the ESAs with more evidence about actual GHG emissions and energy disclosure by global and / or European companies.

On the topic of WATER, we ask the ESAs to consider the following:

Water emissions: If the definition of ‘water emissions’ relates to the amount of specific pollutants by weight held withing water discharges, it is unlikely that investee companies would be tracking this and be able to provide data. Very few companies are disclosing this level of granularity neither on an aggregate nor facility level. Therefore the ability of a financial institution being able to disclose this data on a portfolio basis will be extremely limited.
Other indicators for consideration:

“Weighted average share of companies without any active mid-term water pollution reduction targets”, expressed in %

Exposure to areas of high water stress: Take care not to drive divestment from areas of stress!
There is a risk associated with the disclosure of data tied to “areas of high water stress” that must be managed - the risk that it may signal a desire to divest from these areas when in fact, these are the areas where investment and development are often greatly needed. Guidance should be provided with signposts to innovation.

This indicator could be further refined as follows:

“Total water consumption from areas of high water stress owned (i.e. financed) by the fund”, expressed in cubic liters

OR

“Total water withdrawals from non-renewable sources owned (i.e. financed) by the fund”, expressed in cubic liters.

Other indicators for consideration:

“Weighted average exposure to high impact companies without any active mid-term water consumption reduction targets”

“Weighted average exposure to companies that have not achieved reductions in water consumption in the past three years”

Untreated discharged waste water: Note that not all discharge from all industry activities would need to be treated.

Water usage: Total amount of water consumed and reclaimed, broken down per sector where relevant: Need to define “consumed” and “reclaimed”.

Water recycled and reused: There is no standard approach to defining recycling and reuse. Also recycling and recuse activities are not appropriate/technical relevant for all activities; and impossible to benchmark.

Investing in companies without water management initiatives: This term is very broad and would need to be defined or limited to “without freshwater consumption reduction targets”

On the topic of DEFORESTATION, we ask the ESAs to consider the following:

We believe the proposed metrics need to be more specific as companies can have different deforestation-related policies with varying degrees of coverage. For example, policies could just cover illegal deforestation, certain types of forests/geographies or certain products. Policies should also include specific, quantitative targets and milestones to be robust and so that the policies and progress towards them can be objectively evaluated and verified. Therefore, we suggest clarifying the meaning of “a deforestation policy" as per the following:

“Share of investments in entities without a public company-wide no-deforestation policy with timebound milestones and targets.”

“Share of investee companies without a public company-wide no-deforestation policy with timebound milestones and targets.”

It would also be relevant to identify investments in companies that are implementing those policies. Therefore, we suggest the following metrics:

“Share of investments in entities that do not implement deforestation policies.”

“Share of investee companies that do not implement deforestation policies.”

We suggest that any of the implementation related data points (e.g. use of third-party certification, traceability) can be used to understand if a company is implementing their policy or not. This type of underlying data is readily available from corporates.

<ESA_QUESTION_ESG_5>

Q6 : In addition to the proposed indicators on carbon emissions in Annex I, do you see merit in also requesting a) a relative measure of carbon emissions relative to the EU 2030 climate and energy framework target and b) a relative measure of carbon emissions relative to the prevailing carbon price?

<ESA_QUESTION_ESG_6>
Yes, we see merit in requesting an indicator which compares a fund’s GHG emissions trajectory relative to the temperature objectives of the EU 2030 climate framework. We believe the best way to do this is by looking at underlying corporate emission reduction targets (see also our answer to Q5 above) and companies’ progress against those targets. A framework for such an assessment is currently being developed by CDP and WWF for the Science Based Targets Initiative.

This framework will be publicly available as an open-source resource and is currently available at: https://6fefcbb86e61af1b2fc4-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rack-cdn.com/comfy/cms/files/files/000/003/741/original/Temperature_scoring_-_beta_methodology.pdf

This public methodology allows any user to translate publicly reported corporate emission reduction targets into a long-term global warming pathways expressed in °Celsius.

We therefore propose the following principal adverse impact metric which could be phased in over time:

“Weighted average exposure to companies with implied long-term global temperature pathways above 1.5° Celsius.” expressed in percentage points

OR, at a later stage, the indicator could become:

“Temperature mis-alignment of the fund with the objective of keeping long-term global warming at 1.5° Celsius over pre-industrial levels”, expressed in °C.

We also see merit in requesting an indicator which compares a funds energy consumption exposure to EU 2030 renewable energy targets. A potential metric could be:

“Degree of mis-alignment between total renewable energy consumption owned by the fund and the EU 2030 renewable energy target of 32% of final energy consumption” expressed in percentage points.

A mis-alignment of 5 percentage points would mean that the total renewable energy consumption owned by the fund is 27%.

<ESA_QUESTION_ESG_6>

Q7 : The ESAs saw merit in requiring measurement of both (1) the share of the investments in companies without a particular issue required by the indicator and (2) the share of all companies in the investments without that issue. Do you have any feedback on this proposal?

<ESA_QUESTION_ESG_7>
NA
<ESA_QUESTION_ESG_7>

Q8 : Would you see merit in including more advanced indicators or metrics to allow financial market participants to capture activities by investee companies to reduce GHG emissions? If yes, how would such advanced metrics capture adverse impacts?

<ESA_QUESTION_ESG_8>
See Q6 above on our proposal for the inclusion of a forward-looking temperature alignment metric.

<ESA_QUESTION_ESG_8>

Q9 : Do you agree with the goal of trying to deliver indicators for social and employee matters, respect for human rights, anti-corruption and anti-bribery matters at the same time as the environmental indicators?

<ESA_QUESTION_ESG_9>
Yes. Whilst climate change and environmental destruction are the most pressing concerns for humanity, we believe there is merit in requesting data on social indicators to foster better corporate disclosure and a just transition to a climate neutral economy.

The downside of the broader scope is that PAI readers will be faced with normative decisions about which indicator(s) to prioritise when selecting and comparing funds. We believe that most people won't be able to make such normative decisions and weigh up, for example, social versus environmental impacts against each other. Hence, many investors may still end up referring to aggregate, private ESG fund ratings as ready-made solutions.

<ESA_QUESTION_ESG_9>

Q10 : Do you agree with the proposal that financial market participants should provide a historical comparison of principal adverse impact disclosures up to ten years? If not, what timespan would you suggest?

<ESA_QUESTION_ESG_10>
No. This seems unreasonable given the lack of historic data available for many of the proposed indicators. We suggest a maximum of 3 years in relation to the climate and energy indicators. In general, we'd prefer a stronger focus on forward-looking indicators which in our view should have priority over historical time series reporting.

<ESA_QUESTION_ESG_10>

Q11 : Are there any ways to discourage potential "window dressing" techniques in the principal adverse impact reporting? Should the ESAs consider harmonising the methodology and timing of reporting across the reference period, e.g. on what dates the composition of investments must be taken into account? If not, what alternative would you suggest to curtail window dressing techniques?

<ESA_QUESTION_ESG_11>
The risk of "window dressing" could be reduced by requiring reporting entities to disclose information on a 12-month average basis for all indicators at a product level, e.g. a 1-year weighted average GHG intensity of an investment portfolio based on end of month portfolio holdings information.

This approach is currently applied by ESG fund ratings such as Climetrics or Morningstar's sustainability rating for funds.

<ESA_QUESTION_ESG_11>

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

<ESA_QUESTION_ESG_12>
NA
<ESA_QUESTION_ESG_12>

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

<ESA_QUESTION_ESG_13>
NA
<ESA_QUESTION_ESG_13>

Q14 : If you do not agree with harmonised reporting templates for financial products, please suggest what other approach you would propose that would ensure comparability between products.

<ESA_QUESTION_ESG_14>
NA
<ESA_QUESTION_ESG_14>

Q15 : Do you agree with the balance of information between pre-contractual and website information requirements? Apart from the items listed under Questions 25 and 26, is there anything you would add or subtract from these proposals?

<ESA_QUESTION_ESG_15>
NA
<ESA_QUESTION_ESG_15>

Q16 : Do you think the differences between Article 8 and Article 9 products are sufficiently well captured by the proposed provisions? If not, please suggest how the disclosures could be further distinguished.

<ESA_QUESTION_ESG_16>
NA
<ESA_QUESTION_ESG_16>

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

<ESA_QUESTION_ESG_17>
NA
<ESA_QUESTION_ESG_17>

Q18 : The draft RTS require in Article 15(2) that for Article 8 products graphical representations illustrate the proportion of investments screened against the environmental or social characteristics of the financial product. However, as characteristics can widely vary from product to product do you think using the same graphical representation for very different types of products could be misleading to end-investors? If yes, how should such graphic representation be adapted?

<ESA_QUESTION_ESG_18>
NA
<ESA_QUESTION_ESG_18>

Q19 : Do you agree with always disclosing exposure to solid fossil-fuel sectors? Are there other sectors that should be captured in such a way, such as nuclear energy?

<ESA_QUESTION_ESG_19>
No, CDP would agree to a disclosure requirement including exposure to all non-renewable sources of energy and electricity. This must include liquid fossil fuels and, separately, nuclear energy given the adverse impact on waste and social factors of the latter.

<ESA_QUESTION_ESG_19>

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

<ESA_QUESTION_ESG_20>
NA
<ESA_QUESTION_ESG_20>

Q21 : While Article 8 SFDR suggests investee companies should have "good governance practices", Article 2(17) SFDR includes specific details for good governance practices for sustainable investment investee companies including "sound management structures, employee relations, remuneration of staff and tax compliance". Should the requirements in the RTS for good governance practices for Article 8 products also capture these elements, bearing in mind Article 8 products may not be undertaking sustainable investments?

<ESA_QUESTION_ESG_21>
NA
<ESA_QUESTION_ESG_21>

Q22 : What are your views on the preliminary proposals on "do not significantly harm" principle disclosures in line with the new empowerment under the taxonomy regulation, which can be found in Recital (33), Articles 16(2), 25, 34(3), 35(3), 38 and 45 in the draft RTS?

<ESA_QUESTION_ESG_22>
NA
<ESA_QUESTION_ESG_22>

Q23 : Do you see merit in the ESAs defining widely used ESG investment strategies (such as best-in-class, best-in-universe, exclusions, etc.) and giving financial market participants an opportunity to disclose the use of such strategies, where relevant? If yes, how would you define such widely used strategies?

<ESA_QUESTION_ESG_23>
NA
<ESA_QUESTION_ESG_23>

Q24 : Do you agree with the approach on the disclosure of financial products' top investments in periodic disclosures as currently set out in Articles 39 and 46 of the draft RTS?

<ESA_QUESTION_ESG_24>
NA
<ESA_QUESTION_ESG_24>

Q25 : For each of the following four elements, please indicate whether you believe it is better to include the item in the pre-contractual or the website disclosures for financial products? Please explain your reasoning.

a) an indication of any commitment of a minimum reduction rate of the investments (sometimes referred to as the "investable universe") considered prior to the application

of the investment strategy - in the draft RTS below it is in the pre-contractual disclosure Articles 17(b) and 26(b);

b) **a short description of the policy to assess good governance practices of the investee companies - in the draft RTS below it is in pre-contractual disclosure Articles 17(c) and 26(c);**

c) **a description of the limitations to (1) methodologies and (2) data sources and how such limitations do not affect the attainment of any environmental or social characteristics or sustainable investment objective of the financial product - in the draft RTS below it is in the website disclosure under Article 34(1)(k) and Article 35(1)(k); and**

d) **a reference to whether data sources are external or internal and in what proportions - not currently reflected in the draft RTS but could complement the pre-contractual disclosures under Article 17.**

<ESA_QUESTION_ESG_25>
We believe it is better if all of these disclosures are made in precontractual disclosures as those are more widely read than company websites.
<ESA_QUESTION_ESG_25>

Q26 : Is it better to include a separate section on information on how the use of derivatives meets each of the environmental or social characteristics or sustainable investment objectives promoted by the financial product, as in the below draft RTS under Article 19 and article 28, or would it be better to integrate this section with the graphical and narrative explanation of the investment proportions under Article 15(2) and 24(2)?

<ESA_QUESTION_ESG_26>
NA
<ESA_QUESTION_ESG_26>

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

<ESA_QUESTION_ESG_27>
NA
<ESA_QUESTION_ESG_27>