European Fund and Asset Management Association

EFAMA REPLY TO ESA's CONSULTATION PAPER CONCERNING TAXONOMY-RELATED SUSTAINABILITY DISCLOSURES

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INTRODUCTION

The European Find and Asset Management Association appreciates the opportunity to submit its views to the European Supervisory Authorities (ESAs) on the Joint Consultation Paper (CP) regarding draft regulatory technical standards (RTS) for Taxonomy-related sustainability disclosures pursuant to Article 8(4), 9(6) and 11(5) of Regulation (EU) 2019/2088 (Taxonomy Regulation or TR).

EFAMA is a pan-European organisation representing the full diversity European investment management industry towards European policymakers, as well as international public bodies. At the end of Q2 2020, assets managed by European asset managers as investment funds and discretionary mandates amounted to an estimated EUR 24.9 trillion. Our members include 28 national associations, which bring their country-specific expertise and viewpoints to our committees. Our 58 corporate and 24 associate members add multinational company perspectives to our work.

EXECUTIVE SUMMARY

i. Timeline-related implementation challenges

EFAMA points out that if the taxonomy-related amendments to the SFDR RTS are finalised only after the Commission endorsed the SFDR RTS submitted by the ESAs in February, the technical standards would not be endorsed as a single rulebook. On the contrary, it would **result in two sets of RTS coming into force at different times, resulting in confusing interpretation by the market**. If the amended RTS are adopted in Q3 2021, the timeline will not allow sufficient time to meet the new disclosure requirements ahead of 1 January 2022 and it will cause double implementation efforts. Therefore, we would urge the European Commission to allow in the first year of the Taxonomy's application (1 January to 31 December 2022) a best-effort, transitional implementation for financial undertakings' taxonomy Level 2 disclosures on the provisions in Articles 5, 6 and 8. A best-effort application of the taxonomy-related RTS amendments would also limit the number of times pre-contractual documents will need to be updated and lead to less confusion by end-investors.

ii. Key performance indicators

We underline that the amended RTS should seek consistency with the KPI specifications provided under the forthcoming Delegated Act under Article 8 of the Taxonomy Regulation. In principle, **financial undertakings should be allowed the choice of either indicator (Turnover or CapEx), depending on which indicator is more relevant to a particular sector or company**. This flexibility is essential for CapEx-based sectors, such as real-estate, and for the objective of climate adaptation, since turnover cannot be recognised for adapted activities, as outlined by the Technical Expert Group[1]. We recognise that the most significant advantage of the “either Turnover, or CapEx method” at product-level (option preferred by ESAs) is standardisation, comparability and clarity for end-investors. However, we also see merits in a blend of both CapEx and Turnover indicators at the product level. Such a method would be more relevant for investment strategies focusing on both highly green and transitioning companies and be more consistent with the proposed approach in the EU Ecolabel for retail financial products Technical Report 4.0[2].

[1] TEG Final Technical Report on the Taxonomy (p.30, 2020).
[2] EU Ecolabel for retail financial products Technical Report 4.0 (p.25, 2021)

iii. Derivatives

Given the complexity of derivative financial instruments, we believe their mandatory inclusion could raise several technical questions and lead to disproportionate reporting requirements. For the time being, **derivatives should be included only on an optional discretionary basis**, depending on the deemed relevance in the context of the exposure to taxonomy-compliant activities of the portfolio. For example, we would consider it reasonable to include it in the calculation of the so-called participation certificates, i.e. derivatives or structured notes that strictly track the performance of their respective underlying asset.

iv. Assets not covered by the Taxonomy

The Commissions' approach to non-assessable assets, such as sovereign bonds, cash or commodities, needs to find a balance between the principles of comparability, conciseness, and relevance. While a mandatory inclusion of all assets might boost comparability, it will also significantly dilute the taxonomy alignment ratio and unduly penalise funds with high exposure to assets that have no chance of becoming taxonomy aligned. **We recommend that the proportion of non-assessable assets be disclosed in the template as a secondary indicator in a pie chart or the accompanying narrative**. At the same time, we recognise that the draft delegated Regulation under Art. 8 of the Taxonomy Regulation published on 7 May 2021 explicitly excludes any exposures to central governments and central banks from both the numerator and the denominator of taxonomy-related KPIs. We insist that the Commission should fully align the treatment of sovereign bonds for the purpose of KPI calculations under both Level 2 measures.

v. Assessment of statements on compliance by external or third parties

We do not see a need for these statements to be audited by external or third parties, as the market and standards are not mature enough to include third-party assessments. Regular auditing firms have, so far, no practical experience with the application of the EU Taxonomy. Therefore, the added value of an external verification would be somewhat limited and would only produce additional costs that the end-investors would ultimately bear. Such auditing expenses could deter asset managers, particularly smaller ones, from making taxonomy investments. Financial Market Participants are already confirming whether products are aligned with the Taxonomy and are taking responsibility for these statements. Therefore, third-party opinions on alignment should be optional and the focus should be on auditing the underlying ESG company information at its source.

vi. Periodic disclosures

As companies begin to report their taxonomy alignment only in 2022, the periodic disclosures Level 2 requirements should enter into application in 2023 (for reference periods starting on or after 1 January 2022), given that investors will not have the data available for periodic disclosures yet in 2022. In a joint supervisory statement published in February 2021, the ESAs recommended that the Commission specifies that the RTS applies to periodic reports with reference periods starting from 1 January 2022 in case the RTS are not adopted early enough to allow at least six months to enable financial market participants to gather the necessary information. As the amendments proposed in this consultation will be adopted only in Q3 2021, thereby not providing at least six months for information gathering, we urge the ESA's to reiterate this recommendation.

vii. Templates for products with social objectives

While waiting for a complete taxonomy, **a product should be able to positively claim a social objective, and not only in opposition to the climate taxonomy**. Otherwise, products with a social objective would be required to mark the box "not aligned with the EU Taxonomy", which could negatively affect the products' distribution. Therefore, we suggest offering product developers the opportunity to indicate whether products pursue social or environmental objectives. The taxonomy alignment boxes should only be ticked for funds with environmental objectives/ characteristics.

viii. Data costs

A high burden placed on the Financial Market Participants to comply with the SFDR and taxonomy disclosures requirements when accurate, consistent and comparable data on taxonomy alignment is not available. One should be careful not to create a kind of indirect tax or license to operate, whereby investors would be obliged to buy data from external providers. Due to the market concentration amongst ESG data, research and rating providers, there is a risk for exorbitant fees being charged by taxonomy data providers, leading to increased costs for end-investors. **Higher costs would be detrimental for smaller asset managers and create barriers to entry for new players.** As it is crucial to preserve the competitiveness of the European players, a balance must be found between transparency and the reporting burden.

QUESTIONS TO STAKEHOLDERS

Question 1: 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?

EFAMA supports the "single rulebook" approach. Consistency is needed in the methods, definitions and template-based use of the Taxonomy alignment KPI under Article 8 of the Taxonomy Regulation and SFDR RTS. In our view, this approach is entirely consistent with the ESAs' empowerments under Art. 25 of Taxonomy Regulation and helps create a coherent and comprehensive set of rules for ESG-related product disclosures.

However, we are concerned that the ESA's report under Taxonomy-related product disclosures, amending the existing SFDR RTS, will be finalised only after the Commission' endorsement of SFDR RTS submitted by the ESAs in February. This would mean that the **technical standards would not be endorsed as a single rulebook, but in two separate sets of RTS coming into force at a different time, resulting in confusing interpretation by the market**.

The operationalisation of the disclosure templates will be a significant undertaking requiring sufficient time. The industry needs the final, adopted RTS to begin preparing effectively for the roll-out of the templates. Therefore, i**f the amended RTS on Taxonomy-related product disclosures are adopted only in October/November 2021, the timeframe for implementing the pre-contractual templates will be inconceivable.** Such a timeline would not allow sufficient time to meet the new disclosure requirements ahead of the 1 January 2022 compliance deadline, thereby aggravating the readiness challenge it presents to implementing firms.

We wish to emphasise that such timing and sequencing of the taxonomy-related disclosures **risks causing a double implementation effort**, with additional costs and challenges for Financial Market Participants (FMPs). It is of utmost importance that financial market participants are not obliged to start applying the templates based on the first RTS of SFDR and then must change the template based on the taxonomy-related amendments. This would also create an unjustified burden, and IT costs.

Should the amended Taxonomy-related RTS templates be adopted only after the SFDR RTS are endorsed by the EC based on ESA's Final Report of February 2021, we would urge the European Commission to provide in the first year of the Taxonomy's application (1 January to 31 December 2022) **a best-effort, transitional implementation for financial undertakings' Taxonomy Level 2 disclosures on the provisions in Articles 5, 6 and 8**. A best-effort application of the Taxonomy-related RTS amendments would also limit the number of times pre-contractual documents will need to be updated and thereby also lead to less confusion by end-investors.

This approach would also be consistent with the Level 1 approach to compliance the Commission took to the 10 March 2021 deadline due to implementation and timing challenges. The ESAs have taken a similar approach regarding the phasing in the reporting of the principal adverse impact indicators under the SFDR Principal Adverse Impact Statement template. It would also be beneficial in terms of the Better Regulation Agenda in potentially aligning the effective date of the Taxonomy-related SFDR RTS amendments with the application date of product level principle adverse impact (PAI) disclosures under Article 7 of SFDR.

In a joint supervisory statement published in February 2021, the ESAs recommended that the Commission specifies that the RTS applies to periodic reports with reference periods starting from 1 January 2022 in case the RTS are not adopted sufficiently early to allow at least six months to enable financial market participants to gather the necessary information. We understand that with the Commission endorsing in May or June the RTS submitted by the ESAs in February, financial market participants will have more than six months to gather the necessary information to make the required disclosures. However, **we believe that this recommendation should still apply. These RTS will still be subject to amendments as required under the Taxonomy Regulation and the amendments proposed in the consultation are not minor amendments and will require sufficient time to implement properly**. We urge the ESAs to reiterate this recommendation given that financial market participants will not yet have the data available to disclose this information in periodic reports issued in 2022 as investee companies will only begin to report their Taxonomy alignment in 2022.

In the context of the **operational implementation challenges relating to the Article 8 Taxonomy alignment KPI** disclosures by financial undertakings, a best-effort transitional period in the first year of application is essential. It would help investors address the uncertainties related to the calculation of Taxonomy alignment KPI stemming from the lacking availability of ESG data necessary for assessing their holdings against the EU Taxonomy. Even though there is a clear interest among asset managers and investors to invest in line with the EU Taxonomy criteria, investment strategies based on the EU Taxonomy are still not operational on a broader scale. This is mainly due to the early stage of the development of technical criteria that cover only a few sectors and are not relevant to the broader economy. Moreover, due to the late publication of the delegated acts with technical criteria for environmentally sustainable economic activities contributing to either climate change mitigation or adaptation, it should be clear that even those companies covered by technical criteria will not be able to report reliable data on Taxonomy-alignment of their activities until end 2021 or shortly afterwards.

Question 2: 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 agree that a share of investments as a ratio of eligible assets that are Taxonomy aligned is an appropriate indicator. The choice of indicators should be **aligned with the forthcoming Delegated Act under Article 8 of the Taxonomy Regulation**, which will determine the calculation methods, eligible assets in the denominators, and the role of CapEx in deriving the Taxonomy alignment KPI of financial undertakings.

In choosing between the three options of (i) Turnover as the only primary indicator; (ii) the ESA's preferred method of using either Turnover, or CapEx at product level; (iii) blend of both indicators at the product level, our members recognise that each approach comes with its specific advantages and disadvantages. **In principle, financial undertakings should be allowed the choice of either indicator (Turnover or CapEx), depending on which indicator is more relevant.** As both options ii and iii have very specific methodologic and practical advantages and disadvantages, EFAMA's objective is to provide the ESA's reflections on how these options compare to one another, without explicitly recommending either of the two approach.

The most significant advantage of the either/or product-level method (option ii) is **standardisation, comparability and clarity for end-investors at the product level**. In comparison, the blending of CapEx and Turnover at the product level (option iii) could introduce heterogeneity issues to the data summed in the ratio's numerator. This challenge would need to be addressed by a calculation based on the ultimate market value, as in the EU Ecolabel proposal, and thereby introducing further complexity to the formula.

We also **acknowledge arguments favouring a blend of CapEx and Turnover at the product level** (option iii). Most importantly, it would be more relevant for investment strategies whose underlying companies are made of a combination of highly green (indicated by high Turnover) and companies driving the transition (indicated by high CapEx). Furthermore, Turnover-based products would cease to be relevant for CapEx based sectors, such as real-estate or climate adaptation, thereby inciting segregation of the sectors based on the product-level prevalent KPI. We also emphasise that reporting only one single indicator at the product level could present an inaccurate percentage of Taxonomy alignment within the portfolio, as both Turnover and CapEx may be equally valid, depending on the specifics of the company. We also note that the recent recommendations of the Platform on Sustainable Finance on forward-looking metrics, that product developers could choose whether to weigh a company in a fund portfolio based on either the share of Taxonomy-aligned Turnover, or the Taxonomy-aligned CapEx. Therefore, while EFAMA members' majority preference is for using the either/or calculation (option ii), some of our members would encourage the ESA's to reflect on the aforementioned challenges and give due consideration to option iii.

Furthermore, a blend of CapEx and Turnover calculation method would by consistent with the proposed approach of the JRC for calculating the Taxonomy-relevant portfolio shares under **the Technical Report 4.0 of EU Ecolabel criteria for retail financial products**. Both portfolio greenness methodologies need to be consistent and not create an additional administrative burden producing different percentages – one for SFDR Article 8/9 Taxonomy-related disclosures and another for the EU Ecolabel.

Furthermore, these indicators may not be relevant for alternative assets. For example, Special Purpose Vehicles typically do not report Turnover or CapEx. Investors in securitization would need to use an alternative measure that should probably be detailed by asset type (consumer assets, auto loans, RMBS and etc.). Furthermore, it is key to be able to use different methodology in line with the specificities of the assets, in order to be able to report on the assets that composed the Mutual Funds. This applies also to real estate funds where these KPIs are less applicable as the investments are into the assets themselves, rather than into investee companies.

We also wish to highlight **several clarifications needed from the ESA'**s:

First, it should be specified when calculations regarding the percentage of taxonomy aligned investments are to be made (i.e. at a **point in time or a weighted average over a period of time,** such as the quarterly collection data).

Second, it needs to be clarified whether Taxonomy-alignment should only cover the environmental objective to which the product directly contributes, or whether the KPI is designed to cover all Taxonomy-aligned investments. For example, should a fund that targets only climate change be reporting only on the extent to which the underlying investments meet the Taxonomy criteria for climate change mitigation or adaptation, or should it be reporting a total number of Taxonomy-alignment across all six environmental objectives? We would suggest that only Taxonomy-aligned investments that contribute to the environmental objective of the product should be included, but this needs to be clarified in the RTS.

Third, the consultation document **does not indicate the appropriate database** that could be used to calculate the Taxonomy quota. This is in contrast to the final advice on reporting by asset managers under Article 8 of Taxonomy Regulation where ESMA proposes a decision tree hierarchy concerning prioritisation of different types of data. We would welcome a similar clarification for the purpose of calculations at the product level. In particular, **it should be clear that product providers must not rely solely on data directly reported by companies, but can use other sources of information, including the services by ESG data vendors,** to obtain the data necessary to reasonably establish the proportion of Taxonomy-aligned investments. In this context, we fully support ESMA's suggestion in the final report under Article 8 of Taxonomy Regulation for considering the development of a common methodology for estimating the share of Taxonomy-aligned activities in different economic sectors.

We note, however, that the Commission did not follow ESMA's suggestion in the draft delegated Regulation under Art. 8 of Taxonomy-Regulation published on 7 May 2021. On the contrary, it seems that the proposal allows only calculation of Taxonomy quota based on information reported directly by EU companies and that voluntary disclosures by non-EU undertakings could be taken into account from 2025 on at the earliest. This approach will further narrow down the proportion of portfolio assets that could be disclosed as Taxonomy-aligned due to the lack of reported data and impossibility to account for Taxonomy-aligned activities in investments outside the EU. In a global ESG portfolio, the share of Taxonomy-aligned assets will thus remain negligible in the following years.

Question 3: 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?

The disclosure and availability of the OpEx indicator by economic activities is not uniform and comes with several accounting challenges for non-financial undertakings. The inclusion of mandatory OpEx disclosure would be disproportionate also to the original Taxonomy regulatory text, which rightly considered "CapEx and, if relevant, OpEx". The rationale behind "if relevant" was to include operational expenditures inherently linked to a project or its sustainability-related maintenance (e.g. real estate). A general requirement to report on all OpEx, albeit well-intentioned, would constitute an insurmountable barrier for companies caused by accounting difficulties relating to allocating operational expenditures across NACE codes and adjusting internal accounts to such a classification.

We, therefore, recommend reverting to the original text: "CapEx and, if/when relevant Opex" which will ensure its inclusion at the project financing level where and when it is appropriate and meaningful. If OpEx is to be disclosed separately for investments, it should provide only supplementary information on the extent of the running expenses spent in the context of environmentally sustainable activities that could be disclosed as an additional KPI on a voluntary basis.

Question 4: 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?

Considering the large scope of derivatives (future, forwards, options, Total Return Swaps, convertible bonds etc.), the nature of their underlying (indices, interest rates, securities, currencies, cash etc.), purpose (strategic vs. tactical) and their potential usage (exposure, hedging, arbitrage), answering this question is not straightforward. The market would need guidance on how to treat derivatives before including it in the KPIs.

Given the complexity of derivative financial instruments**, their mandatory inclusion could raise several technical questions and lead to disproportionate reporting requirements** (leverage or short positions, full exposure or residual exposure or delta equivalent exposure, collateral received or posted, etc.). The relevance of derivatives in KPI calculation must be assessed instrument by instrument. For example, for futures, calculation of the MSCI ACWI would require decomposing it into 3,000 constituents, measuring each one at the respective weighting, and building it back up again. Logistically, this would be very difficult for market participants and overly complicated, especially with regards to estimating the underlying data.

The following two examples give an idea of some of the issues around derivatives and other practices that need to be considered:

- *Total return swaps (TRS)*: May be used to manage climate risk in a portfolio. For example, asset managers can enter into a TRS which may provide a return over a basket of securities which are net carbon neutral. It should be further considered whether such as TRS can be reported as: i) a taxonomy aligned investment; or ii) a risk management technique which provides the investor with taxonomy aligned exposure.

- *Stock-lending*: Based on a combination of the security being lent, the counterparty to whom the security is being lent and the use to which it is put, it would be possible to analyse the extent to which revenue earned from stock-lending is taxonomy compliant.

Therefore, we believe it would be better not to require mandatory inclusion of derivatives for the time being, as further assessment is required to develop shared guidelines. Derivatives should be included on a discretionary basis only, depending on the deemed relevance in the exposure to taxonomy-compliant activities of the portfolio. For example, we would consider it reasonable to include in the calculation the so-called participation certificates, i.e. derivatives or structured notes that strictly track the performance of their respective underlying asset. Such underlying assets can be indexes or baskets, but also shares of individual companies. In some emerging markets without sufficient liquidity, such participation certificates are the primary way of investing for European asset managers. Of course, eligibility of participation certificates should depend on the underlying assets and should be considered only for derivatives that track the performance of equity (or debt) instruments issued by financial or non-financial undertakings or real estate assets.

The draft delegated Regulation under Art. 8 of Taxonomy-Regulation published on 7 May 2021 explicitly excludes derivatives from the numerator of any KPI that shall be reported by financial undertakings under the EU Taxonomy. While not supporting not entirely supporting this exclusion, we believe that the calculation methodology for the proportion of Taxonomy-aligned investments must be fully consistent at both product and entity level. In the end, therefore, a uniform approach to the treatment of derivatives should be adopted under both Level 2 measures.

Finally, we highlight that Contracts for Difference (CFDs) should not be included as derivatives. In many geographies, notably the UK, investors commonly use CFDs to simply avoid stamp duty.

Question 5: 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?

The use of "equities" and "debt instruments" seems sufficiently clear to capture relevant instruments issued by investee companies.

However, we would recommend adding the list of instruments under the scope to each relevant category to avoid any misinterpretation. For example, do we consider rights and warrants as equities even though they are optional instruments? Should loans be included under debt? A complete classification would be beneficial in that regard.

We would also welcome more clarity on multilateral development bank bonds treatment – particularly if the earmarked projects in bonds contribute to sustainable objectives.

Asset-Backed Securities should also be taken into account. ABS are typically issued by special purpose vehicles which merely hold the underlying assets. As such, there would need to be a 'look through' approach to the basket of underlying assets to determine whether the ABS in question is taxonomy compliant. This would involve assessing the attributes of the underlying assets. For example, if an ABS is backed by car purchase loans, are they loans for environmentally sustainable vehicles or not?

We understand a consultation is planned by the European Banking Authority to insert sustainability factors analysis into the securitization regulation. We hence expect the amendments of the securitization regulation to be mirrored within the Taxonomy and SFDR regulations, and to allow investors including Mutual Funds and clients under mandates in securitization to report taxonomy-alignment according to KPI adapted to the specificities of securitized assets, hence enabling securitization investors to qualify their financial products as article 8 or 9 using dedicated and relevant KPI.

Concerning valuation criteria, the term “market value” is widely understood and applied consistently in the industry and we would not suggest imposing alternative valuation methods. It makes sense for firms to use their own internal valuation criteria rather than having a specific valuation model specified. Firms investing in private market currently use own valuation models for determining the valuations of their investments and it would be confusing to impose alternative methods.

Furthermore, we note that in debt instruments categories, we will face difficulties accessing the required data. In the case of sovereign bonds, the three KPIs will not be disclosed, and as a result, it will not be possible to disclose their alignment with taxonomy whilst these instruments can represent a very significant proportion of some products.

Question 6: 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?

Considering that the main objective of these indicators is to offer investors a concise, high-level and comparable figure, we believe **it would be appropriate to include all investments in the denominator**. Exclusion of particular assets could lead to unnecessary confusion and hinder comparability between funds with different proportions of exposure to sovereign bonds. It could also lead to opportunities for overstating the proportion of Taxonomy-aligned investments in a product.

On the other hand, **mandatory inclusion of general sovereign exposures will significantly dilute the Taxonomy alignment ratio and unduly penalise funds with high exposure to this asset class**.

It will also create an urgent need to develop universal methodologies for assessing the Taxonomy alignment of sovereign bonds under the forthcoming EU GBS proposal, which may take several years under the ordinary co-legislative procedure. Sovereign green bond issues for earmarked projects aligned with the Taxonomy should also apply, even if not compliant with the EU GBS. We believe this would also encourage the participation of sovereigns in green bond issuance.

To further address the challenge of non-assessable assets (these also include cash, emerging market instruments, securitised assets or commodities), **we recommend that the proportion of non-assessable assets can be disclosed** in the template as a secondary indicator, either as a portion of the pie chart or in an accompanying narrative.

As a result, the client could compare the primary number showing the percentage of Taxonomy aligned asset against total assets, and the proportion of Taxonomy-aligned and not aligned activities compared with non-assessable activities. This would ensure that investors can understand to what extent the Taxonomy-alignment KPI relates to assets that can be assessed against the Taxonomy.

We also recommend that alongside the KPI, there should be a blank explanation field, where the FMPs can describe the product's investments and the investments' relation to the EU taxonomy in more detail. This is particularly important as investments can be sustainable in social terms (aligned with the SFDR art. 2(17)) without being taxonomy-aligned. It should be possible to communicate this to the customer clearly.

We also note that the draft delegated **Regulation under Art. 8 of Taxonomy-Regulation** published on 7 May 2021 explicitly excludes any exposures to central governments and central banks from both the numerator and the denominator of Taxonomy-related KPIs. For the sake of consistency regarding disclosures of Taxonomy-aligned proportions of investments at both, company and product level, the **treatment of sovereign bonds for KPI calculations should be fully aligned under both Level 2 measures.**

Question 7: 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?

We agree with the proposed statement of Taxonomy compliance, but we do not see a need for these statements to be supervised or audited by external or third parties. **In our view, the market and standards are not mature enough to include third-party assessments.**

The EU Taxonomy framework is a very complex piece of regulation that will require substantial research and/or purchase of data from commercial vendors to become applicable to an investment portfolio. It is questionable whether external verifiers are better placed for assessing or reviewing the Taxonomy-based calculations than the product provider itself, who needs to work with the Taxonomy criteria daily to meet and monitor the respective commitments in terms of the share of Taxonomy-aligned investments. The regular auditing firms have so far no practical experience with the application of the EU Taxonomy. Therefore, the added value of an external verification would be somewhat limited and would only produce additional costs that the end-investors would ultimately bear. Such auditing expenses could deter asset managers, particularly smaller ones, from making taxonomy investments. In addition, in-depth verification of the underlying calculation would require access to the same data sources that would raise significant licencing issues and render external assurance hardly practicable.

FMPs are already confirming whether products are aligned with the taxonomy and are taking responsibility for these statements. They may decide to request an external/third party opinion on alignment, but this should be only on an optional basis, as it will add additional cost, have timing implications and would not necessarily ensure that such products are aligned (the third party will be basing their opinion on information provided by the FMP).

Furthermore, based on ESMA's final technical advice on Article 8 of Taxonomy Regulation, it was stated that less than 3% of EU fund portfolios have an estimated Taxonomy alignment of 5% or higher and that, on average, funds with at least some exposure to EU have an estimated Taxonomy alignment of 0.9%. Given this context and the materiality of the percentages that will be disclosed, we believe it is unjustified to require financial market participants to verify this statement externally.

We believe it makes more sense to audit the information at its source - the underlying investee company ESG information. Much of the data used to develop the Taxonomy alignment KPI will be derived from company reporting based on ESG information submitted in line with the forthcoming mandatory European sustainability reporting standard. In its recent CSRD proposal, the EC introduces limited assurance requirements for disclosure and suggests a progressive movement towards reasonable assurance. Therefore, should the information subjected to CSRD come with more robust audit requirements, and financial market participants use the data published by non-financial investee companies in their non-financial reporting under Art. 8 of the Taxonomy Regulation, the information collected will benefit from better assurance. In turn, this will result in increased data quality and more trustworthy disclosures by financial undertakings as users of this information.

Question 8: Do you have any views on the proposed periodic disclosures which mirror the proposals for pre-contractual amendments?

As companies begin to report their taxonomy alignment only in 2022, the periodic disclosures level 2 requirements should enter into application in 2023 (for reference periods starting on or after 1 January 2022) , given that investors will not have the data available for periodic disclosures yet in 2022.

We agree that it makes sense to mirror the pre-contractual disclosures as laid down in the proposed RTS for the periodic disclosures, as it is essential to ensure coherence with the structure of the SFDR RTS. However, certain sections of the reporting documents could be simplified so that they are not a mere a duplication of the content of the pre-contractual document.

Question 9: Do you have any views on the amended pre-contractual and periodic templates?

The main areas where clarity is urgently needed are linked to interpretations as to the disclosure of underlying information. In relation to the disclosed Taxonomy alignment KPI, should this be seen as a minimum proportion of the underlying investment or an expected average? We also see a challenge in how to disclose the underlying data from the investors if the Taxonomy alignment is based on Turnover, OpEx or CapEx.

We are concerned that including the proposed level of information regarding the Taxonomy alignment KPI in pre-contractual documents could be potentially misleading to consumers by giving the impression that the disclosed Taxonomy alignment KPI is a 'target' set by the financial market participants, whereas it is just a snapshot of what the Taxonomy alignment KPI is at the time of preparation of the document.

Our preference is for Taxonomy-related disclosures in pre-contractual documents to be more qualitative as opposed to quantitative indicators. For "existing" products such as mutual and pension funds, the Taxonomy alignment KPI can represent a "snapshot" of the exposures of the portfolio at a certain point in time and could be relatively easily calculated and relevant for the investor. However, the same would not apply to financial products such as institutional mandates. For such bespoke mandates, client may not find the disclosures meaningful particularly if the investments are, for example, in private markets or illiquid assets. While in the pre-contractual disclosure for this type of products, the identification of certain E/S characteristics that will be promoted can be part of an investment policy and strategy, the ex-ante identification of a quantitative percentage of the KPI would be too restrictive and go beyond what is envisaged in the Level 1 Regulation.

For this reason, we would find it more appropriate to allow for **a qualitative disclosure of the alignment with the Taxonomy**, also in consideration of the continuously evolving nature of the latter. The narrative disclosures would explain **how and to what extent was the Taxonomy used in determining the sustainability of the underlying investments**, as suggested in TEG's Final Report. As part of this qualitative disclosure, financial market participants could choose to include an alignment percentage clarifying whether this is a commitment or an alignment at the time of the preparation of the document. This will provide context regarding the Taxonomy alignment KPI.

Question 10: 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?

We support the proposal for unified pre-contractual and periodic reporting templates applicable to all Article 8 and 9 SFDR products (including Article 5 and 6 Taxonomy Regulation products which are a sub-set of Article 8 and 9 SFDR products).

However, flexibility should be given in its implementations regarding the omission of some sections that are not relevant. Otherwise, some Article 8 and 9 products that are not in scope of Article 5 and 6 of the Taxonomy Regulation (in particular Article 8 products promoting only social characteristics) would be disadvantaged by disclosing a very low or zero Taxonomy alignment KPI.

Therefore, the section specifying the share of sustainable investments aligned/not aligned with the EU Taxonomy should be included only if relevant for the specific product. This could be facilitated by a reasoning tree. Ticking the appropriate box at the beginning of the template would allow the FMP not to answer questions that are not relevant.

Question 11: 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?

The suggested templates are based on the current state of the EU Taxonomy, which is largely a Taxonomy covering a limited scope of environmental objectives.

We insist that while waiting for a more complete Taxonomy (remaining objectives and a potential social taxonomy), a product should positively claim a social objective, and not only in opposition to the climate

Taxonomy. Otherwise, products with a social objective would be required to mark the box "not aligned with the EU taxonomy", which could negatively affect the products' distribution. Therefore, we suggest offering product developers the opportunity to indicate whether products pursue social or environmental objectives. The Taxonomy alignment boxes should only be ticked for funds with environmental objectives/ characteristics.

Furthermore, a fund that doesn't comply with the EU Taxonomy alignment should be able to fully and extensively explain it in these templates.

Question 12: Do you have any views regarding the preliminary impact assessments? Can you provide more granular examples of costs associated with the policy options?

We would like to reiterate the high burden placed on the Financial Market Participants to comply with the SFDR and Taxonomy disclosures requirements when accurate, consistent and comparable data on Taxonomy alignment is not available. One should be careful not to create a kind of indirect tax or a license to operate, whereby investors would be obliged to buy data from external providers. Due to the market concentration amongst ESG data providers, there is a risk for exorbitant fees being charged by Taxonomy data providers, leading to increased costs for end-investors. **Higher costs would be detrimental for smaller asset managers and create barriers to entry for new players**. It is crucial to preserve the competitiveness of the European players and a balance must be found between transparency and reporting burden.

Furthermore, we find that the **draft delegated Regulation under Art. 8 of Taxonomy Regulation published on 7 May 2021 further aggravates this situation**. First, it delays the reporting of specific Taxonomy-related KPIs that could be used for identification of Taxonomy-aligned investments to 2023. Second, it doesn't admit the consideration of Taxonomy-aligned investments in non-EU companies or effectively any companies not subject to NFRD reporting until 2025. In the meantime, the share of Taxonomy-aligned assets that could be identified in a global ESG portfolio will remain negligible. Moreover, before 2023, no product will be able to assess the likely share of Taxonomy-aligned investments that are in line with its investment strategy in order to make firm commitments as regards their minimum proportion to investors. This also means that by the expected time of entry into force of the new provisions on sustainability preferences under MiFID II and IDD, there will be no products that offer investors a minimum proportion of investments in line with the EU Taxonomy in line with Art. 2 (7)(a) of MiFID II Delegated Regulation and Art. 2 (4)(a) of IDD Delegated Regulation to be amended in line with the Commission's proposal from 21 April 2021.

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About EFAMA

EFAMA, the voice of the European investment management industry, represents 28 Member Associations, 58 Corporate Members and 24 Associate Members. At end Q4 2020, total net assets of European investment funds reached EUR 18.8 trillion. These assets were managed by more than 34,350 UCITS (Undertakings for Collective Investments in Transferable Securities) and almost 29,650 AIFs (Alternative Investment Funds). At the end of Q2 2020, assets managed by European asset managers as investment funds and discretionary mandates amounted to an estimated EUR 24.9 trillion.

More information is available at www.efama.org.

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ANNEX

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