

ICI Global Response to ESAs' Survey¹ on Environmental/and or Social Financial Product Templates

(submitted 16 October 2020)

[Please note that the below response is re-formatted from Survey format that utilises a template with each question followed by a text box for the response].

We are responding to this consultation on behalf of the members of ICI Global, which carries out the international work of the Investment Company Institute, the leading association representing regulated funds globally. ICI's membership includes regulated funds publicly offered to investors in jurisdictions worldwide, with total assets of US\$34.7 trillion. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of regulated investment funds, their managers, and investors. ICI Global has offices in London, Hong Kong, and Washington, DC.

We appreciate the opportunity to respond to the ESAs' Survey on Environmental/and or Social Financial Product Templates, and our response supplements our response to the ESAs' consultation on the proposed regulatory technical standards (RTS) for the Sustainable Finance Disclosure Regulation (SFDR RTS Response) (submitted on 1st September 2020).

High level comments

Proposed templates illustrate the over-detailed nature of the RTS proposal

We re-emphasise our key theme from our SFDR RTS Response on the product-level disclosure. ***The ESAs must streamline pre-contractual disclosures to make them meaningful to end investors, i.e., they must focus on information that will help investors make investment decisions***, while reserving technical details for a website, non-prospectus disclosure. Our SFDR response recommended removing some proposed disclosure elements from the pre-contractual disclosure in their entirety and shifting many of the other elements to a website disclosure that is not part of the prospectus. We continue to advocate for this approach, and the 6-page long proposed templates (also referred to as mock-ups), focused only on one topic, illustrate the density of the new disclosure requirements.

The ESAs must allow for flexibility in incorporating the SFDR disclosures into the regulatory documents – to be included in the regulatory documents themselves or via a separate document incorporated by reference

We explain this point in response to Question 1.

Survey Questions:

1. How useful is the highly standardised presentation of the information in this format?

- Useless
- Fairly useless
- Neither useless nor useful
- Fairly useful
- Very useful

¹ See <https://ec.europa.eu/eusurvey/runner/ESGtemplatesSFDR>.

There are two types of standardisation: (1) the type of information to be disclosed, and (2) the presentation. The SFDR already mandates the first. Our comments in this response relate only to the proposed standardisation of the layout.

Our view is that templates should not be mandatory. The SFDR does not require mandatory templates, and we strongly recommend providing asset managers with the flexibility to determine whether it is more effective to provide this disclosure to investors (1) within the regulatory documents themselves (the UCITS prospectus and annual report (see SFDR Art. 6(3)(g) and 11(2)(g)), or (2) in a separate document (i.e., a fact sheet) that can be incorporated by reference into the regulatory document (subjecting it to all the applicable prospectus requirements). We also ask the ESAs to confirm that the latter scenario will allow for posting this fact sheet on a web site, separate from the prospectus.

Instead of mandating templates, we recommend that the ESAs suggest sample language to be incorporated in the UCITS prospectus and annual reports ('sample language approach'). This would allow templates to provide helpful illustrations for how the ESAs interpret the SFDR language. The sample language must be for *illustration purposes only* and *non-mandatory* so that it can accommodate the diversity of products. In this regard, the SFDR explicitly states that 'When developing the draft [RTS], the ESA shall take into account the various types of financial products, their characteristics and the differences between them, as well as the objective that disclosures are to be accurate, fair, not misleading, simple and concise.' SFDR Art. 8(3), and similarly, Art. 9(5) and Art. 11(4).

For the SFDR disclosures to be most helpful to investors, asset managers must also have flexibility to include this information in the most appropriate part of the prospectus or annual report. For example, asset managers should have the flexibility to incorporate the description of the environmental/social or sustainable investment aspects of the strategy into the section in the prospectus which describes the investment strategy.

Asset managers must also have discretion to use the style and format that is consistent throughout the underlying documents. UCITS prospectuses and annual reports are multi-page legal documents, typically without icons, graphs or colour, covering many topics as required by the UCITS Directive and additional Member State requirements. Although nothing prevents the use of the template's icons or graphs in these documents, their use to illustrate only one topic (sustainable investments (SI) or ESG) may be inconsistent with the rest of the document and may also over-emphasise the SI/ESG disclosure. Thus, we advise against mandating any use of icons or graphs or colour for the SFDR disclosure.

2. More specifically, how useful is the presentation of the information with the use of icons as visual aids?

- Useless
- Fairly useless
- Neither useless nor useful
- Fairly useful
- Very useful

See response to Question 1. Our answer relates to the sample language approach we propose. UCITS prospectuses and annual reports are multi-page legal documents, typically without icons, graphs or colour, covering many topics as required by the UCITS Directive and Member State requirements. Although nothing prevents the use of icons or graphs in these documents, their use to illustrate only one topic (sustainable investments or ESG) may be inconsistent with the rest of the documents.

We are interested in seeing the consumer testing results regarding the use of these icons in the standalone documents.

3. More specifically, how useful is the presentation of the information with the use of graphs as visual aids?

- Useless _____
- Fairly useless _____
- Neither useless nor useful _____
- Fairly useful _____
- Very useful _____

See response to Question 1. Our answer relates to the sample language approach we propose. UCITS prospectuses and annual reports are multi-page legal documents, typically without icons, graphs or colour, covering many topics as required by the UCITS Directive and additional Member State requirements. Although nothing prevents the use of icons or graphs in these documents, their use to illustrate only one topic (sustainable investments or ESG) may be inconsistent with the rest of the documents.

We are interested in seeing the consumer testing results regarding the use of these graphs in the standalone documents.

4. More specifically, how useful is the presentation of the information with the use of explanatory notes, in the column at the right side of the document, which are presented on a grey background?

- Useless _____
- Fairly useless _____
- Neither useless nor useful _____
- Fairly useful _____
- Very useful _____

See response to Question 1. Our answer relates to the sample language approach we propose.

The typical approach to providing formal definitions in a fund prospectus is to include them in the 'Definitions' section or in a 'Glossary'. Thus, any call-out boxes or the explanatory notes only for the section on 'sustainable investments/ESG' disclosures would look out of place and possibly confuse investors. A better approach would be to allow asset managers the discretion to decide if the further explanation is needed and, if so, where it is most appropriate to include it in the fund prospectus.

As a further note, we found the presentation of the explanatory notes in this format to be confusing. We are interested in seeing the consumer testing results regarding the use of these explanatory notes in the standalone documents.

5. Are there presentation aspects that might make it hard to understand the sustainability aspects of the product? For example, with regards to the distinction between the sub-categories of investments, namely between 1A, Classified as sustainable: environmental and 1B, Other investments aligned with E/S characteristics: Environmental?

- Yes
- No
- Other

The complexity and the confusing nature of the graphs on Page 3 of templates 1 and 2 illustrate the unnecessarily over-complicated nature of the product-level disclosure in the SFDR RTS proposal, as we detailed in our SFDR RTS Response (e.g., Article 8 products should not be subject to disclosing information about 'sustainable investments' but should only disclose information about their environmental/social characteristics).

We are very interested in hearing the results of the consumer testing on this graph; in particular whether individuals can actually interpret the differences between 1A and 1B, and the significance of the distinction for the purpose of their investment decisions. We believe this graph is confusing and unreadable. Moreover, it attempts to illustrate an underlying rule that should not apply to Article 8 products.

For example, the template includes a pie chart with the following headings:

- **#1 aligned with E/S characteristics [showing 95% of this investment]**
 - **#1A Classified as sustainable: environmental [showing 5% of the 95%]**
 - **#1B other investments aligned with E/S characteristics: Environmental [showing 60% of the 95%]**
- **#1B Other investments aligned with E/S characteristics: Social**

At least two headings – 1A and 1B both identify investments as 'environmental' – and they denote completely different segments on the pie chart. We highly question whether an investor can understand what the differences are.

The templates include the following definition in the callout box, and we do not think they are meaningful to help end investor understand their investments:

The **Subcategory #1A** covers investments that are qualified as sustainable. A sustainable investment means an investment in an economic activity that contributes to an environmental objective, measured for example by key resource efficiency indicators such as CO2 emissions, or the use of water, or an investment that contributes to a social objective, such as tackling inequality or that fosters social cohesion.

The subcategory **#1B Other E/S characteristics** covers investments aligned with the environmental or social characteristics that **do not** meet the criteria of ‘sustainable investment.’

This pie chart could be much clearer if it only had explanations about alignment with E/S characteristics.

6. Do you have any other suggestions or comments to improve the presentation of these disclosure documents?

Additional comments on the templates

Consistency of templates with RTS. Templates should not create any new substantive requirements, and they must be consistent with the SFDR and the SFDR RTS. For example, the draft RTS would require only a narrative description of investments in different sectors and sub-sectors (see RTS Art. 15(2)(b)(iii)), while templates 1 and 2 illustrate this as a graph, making it look like that the graph is required rather than a narrative.

Template language is inconsistent with the SFDR terminology. There are two check-boxes at the top of each template with text next to it – ‘ESG objective’ or ‘ESG characteristics.’ It is not clear what these check boxes intend to do and they do not track Article 8 or Article 9 terminology (i.e., ‘promoting environmental or social characteristics’ or ‘an objective of sustainable investments’). The templates must reflect the SFDR and must not introduce any new terminology. These boxes should be deleted.

Recognition that templates cannot cover all product variations. The ESAs’ reference to templates as ‘mandatory’ templates is concerning in that there are many product features that these templates do not cover. As mandated by the SFDR Art. 8(3), and similarly, Art. 9(5) and Art. 11(4), the ESAs must recognise that information will vary depending on the underlying features of the product.

Our members also will find it helpful to see an illustration for an active fund, as the templates only illustrate a tracker ETF.

Further, the templates signal focus on specific ESG investing strategies (i.e., exclusions), whereas the ESAs stated in the SFDR consultation that ‘It is neither the intention nor the mandate of the ESAs to reduce the choice of ESG strategies for companies.’ Therefore, any template will need to be clear that it is for illustration purposes only.

Benchmark question. The question about the benchmark in templates 1 and 2 seems to contain an error, as the question asks about whether an index is designated as a reference benchmark to determine whether this product is ‘sustainable’, while the answer is about the reference benchmark not being aligned with ‘all of the environmental or social characteristics.’

Consumer testing. The ESAs indicated that the proposed templates are ‘subject to the outcome of the concurrent consumer testing exercise.’ We are concerned that the testing was done only on the

standalone documents. Testing must also be done to see how investors comprehend this information when incorporated into a UCITS prospectus or annual report.

7. When the templates are presented via digital media, can you foresee any particular challenges? Can you suggest how these particular challenges could be overcome while retaining the core aspects of the standardized template format?

We are pleased to see that the ESAs contemplate the presentation of this information via digital media. One of the challenges we foresee is the ESAs mandating disclosures based on the existing technology and formats, which would be detrimental to investors, as it will deprive investors of the benefits that new technology can offer. New technology can lead to new ways of presenting information that in turn can lead to better investor comprehension and engagement with the information.

As we advocated in our SFDR RTS Response, the ESAs should future-proof the format of disclosures by not specifying a format that relies on the use of the existing technology or envisions paper-based disclosures. For example, the templates look like paper documents in a pdf format. These documents can already be much more consumer-friendly if they were allowed to be layered and interactive.

As technology evolves constantly, changing how we consume information and interact with it, any proposed templates or disclosure principles should be flexible enough to allow for the use of the new technology. This will be consistent with the aim of the European Commission's Digital Strategy Plan that calls for technology to make EU citizens' lives easier in all aspects, which we believe should translate into how they receive and consume information about investments.