Response form for the Consultation Paper on the Draft advice to European Commission under Article 8 of the Taxonomy Regulation

5 November 2020

Date: 5 November 2020

Responding to this paper

ESMA invites responses to the questions set out throughout this Consultation Paper and summarised in Annex II. Responses are most helpful if they:

- respond to the question stated and indicate the specific question to which they relate;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by **4 December 2020**.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Instructions

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

- Insert your responses to the consultation questions in the form "Response form_Consultation Paper on TR Article 8 advice", available on ESMA's website alongside the present Consultation Paper (www.esma.europa.eu → 'Your input – Open consultations' → 'Consultation on advice under Taxonomy Regulation Article 8').
- Please do not remove tags of the type <ESMA_QUESTION_TRART8_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: ESMA_TRART8_nameofrespondent_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA_TRART8_ABCD_RESPONSEFORM.
- Upload the form containing your responses, in Word format, to ESMA's website (www.esma.europa.eu under the heading 'Your input – Open consultations' → 'Consultation on advice under Taxonomy Regulation Article 8').

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. If you do not wish for your response to be publicly disclosed, please clearly indicate this by ticking the appropriate box on the website submission page. 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 ESMA's rules on 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 ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Data protection'.

Who should read this paper?

This Consultation Paper may be of particular interest to non-financial undertakings and asset managers covered by Article 8 of Regulation (EU) 2020/852 (the 'Taxonomy Regulation') as well as to investors and other users of non-financial information

General information about respondent

Name of the company / organisation	ISDA
Activity	Other
Are you representing an association?	☒
Country/Region	Europe

Introduction

Please make your introductory comments below, if any:

<ESMA_COMMENT_TRART8_1>
The International Swaps and Derivatives Association (ISDA) welcomes the opportunity to respond to the European Securities and Markets Authority's (ESMA) consultation on draft advice to the European Commission (EC) under Article 8 of the Taxonomy Regulation. Our response is based on responses provided by members of the ISDA Sustainable Finance Working Group; ISDA Commodity Derivatives Working Group; ISDA Energy, Commodities & Developing Products Group and ISDA European Government Relations Working Group;. Not all members responded and not all members of ISDA are members of these working groups. Not all members who provided feedback responded to all of the questions. The views expressed herein may not, therefore, reflect the full range of views held by ISDA's membership or of the working groups in their entirety.

Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 925 member institutions from 75 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org.

In view of our broad membership, we are providing various perspectives to the questions asked that reflect the views of ISDA's different member institutions.

For the purpose of this consultation, ISDA is providing a synthesis of responses either in standalone form and/or in coordination with EFAMA and AIMA (those responses are indicated in red), by endorsing, totally or partially, the Associations' responses to specific questions.

<ESMA_COMMENT_TRART8_1>

Q1 For this KPI, do you agree with the proposed approach to defining turnover (bullet a in the draft advice)?

<ESMA_QUESTION_TRART8_1>
Endorsing EFAMA's response

We welcome the clear definition of turnover based on the Accounting Directive, IFRS Regulation and national GAAP. The Turnover definition in the Accounting Directive should be the reference point for thee wax nonfinancial undertakings definer turnover for the purpose of calculating their turnover KPI under Article 8(2) of the Taxonomy Regulation. We commend that undertakings applying IFRS can use the amount of revenue and income accounted for under IFRS 15 and 16 as their turnover.

.
<ESMA_QUESTION_TRART8_1>

Q2 For this KPI, do you agree with the proposed approach to when turnover can be counted (bullet b in the draft advice)?

<ESMA_QUESTION_TRART8_2>
Partially endorsing EFAMA's response

Asset managers find the proposed approach adequate and consistent with other (forthcoming) elements of sustainable finance legislation, notably on DNSH in Taxonomy DA, minimum safeguards in Article 2 of SFDR and Articles 10-16 of the Taxonomy regulation on activities that substantially contribute to environmental objectives.

ISDA's financial members welcome the focus on turnover/revenues, which is the most widely available metric to assess the exposure of companies to EU taxonomy aligned activities. They are of the view that it should only include third party sales whilst intercompany sales and equity participation sales should be eliminated, to prevent overstating of green revenues.

However, the requirement to publish a plan on a company's website might be difficult to fulfil in practice, especially if a company pursues many investment projects at a time. Additionally, investment plans could include sensitive business information that cannot be published.
<ESMA_QUESTION_TRART8_2>

Q3 For this KPI, do you agree with the proposed approach to defining CapEx (bullet a in the draft advice)?

<ESMA_QUESTION_TRART8_3>
ISDA non-financial members are in agreement with the proposed approach as it follows the IFRS standards. However, the proposed definition is not detailed enough given that it only considers adjusting for depreciation and amortisations. Additionally all non-cash effects have to be eliminated, such as capitalization of addition to provisions or inception of leasing contracts; cf. IAS 7.6. In general, it would be helpful to closely align with the statutory cash flow according to IAS 7.
<ESMA_QUESTION_TRART8_3>

Q4 For this KPI, do you agree with the proposed approach to when CapEx can be counted, including the definition of 'plan' (bullet b in the draft advice)?

<ESMA_QUESTION_TRART8_4>
Partially endorsing EFAMA's response

In general, we agree with point 79, proposing the inclusion of CapEx if the plan to which it relates aims to make the economic activity in question Taxonomy aligned within a certain period. Nevertheless, the requirement for a 'plan' to be published on the company's website may not be practical or suitable, especially if a company has many investment projects at a time. Also, the requirement of a 'five years maximum' necessitates further investigation and clarification of what constitutes the start of a 'plan' i.e. significant initial investigation costs and planning may occur before the final investment decision and the total period of the plan through to becoming an 'activity' may last longer than 5 years, especially for large infrastructure projects when compared to their investment horizons and timeframes for depreciation. For such projects, we suggest extending the period to 10 years in order not to disincentivize from long term investments plans.

In point 80 of the consultation there is a reference to consideration of cases (such as low carbon technologies) that can already be considered to make a substantial contribution without needing to be part of a plan. It is crucial that these exceptional cases are included in the final guidance.

Other ISDA members believe that while CapEx disclosures can be a useful forward looking measure, they should be assessed within a company's context as their degree of applicability will vary significantly depending on the sector of the green economy. It is felt that for infrastructure focused sectors, such as renewable power generation, CapEx disclosures will be highly applicable but less so for more technologically focused sectors. An additional factor for consideration is that CapEx is currently less disclosed than green revenue and whilst mandatory disclosures will be beneficial for European companies, it will prove challenging for generating global consistent figures.
<ESMA_QUESTION_TRART8_4>

Q5 For this KPI, do you agree with the proposed approach to defining OpEx (bullet a in the draft advice)?

<ESMA_QUESTION_TRART8_5>
Partially endorsing EFAMA's response

Asset managers believe the inclusion of mandatory OpEx disclosure is disproportionate to the original taxonomy regulatory text which rightly considered "capex and, <u>if relevant</u>, OpEx". The rationale behind "if relevant" was to allow for accounting operational expenditures inherently linked to a project. In this context, a general requirement to report on all OpEx, albeit well intentioned, would constitute an unsurmountable barrier for companies given the extremely highly accounting difficulties to allocate operational expenditures to NACE codes and to adjust internal accounts to such a classification. In agreement with ESMA, they recognize the complexity of this exercise and believe that OpEx as a financial metric measuring Taxonomy alignment would provide no added value to regulators or institutional investors.

From the perspective of non-financial undertakings, we believe this definition is too vague and further specification on this KPI is needed. In particular, it gives rise to the following questions:
1) would companies need to include or exclude items that are reported as non-operating results (aperiodic and/or non-operating activities such as impairments, results of derivatives or disposal gains)?
2) do we understand it correctly that OpEx would be basically defined as residual between operating result (EBIT) and turnover/revenues?
3) what would apply to income from participations, e.g. Joint Ventures?

<ESMA_QUESTION_TRART8_5>

Q6 For this KPI, do you agree with the proposed approach to when OpEx can be counted, including the definition of 'plan' (bullet b in the draft advice)? With reference to the TEG's inclusion of the words "if relevant" in relation to OpEx, in which situations should it be possible to count OpEx as Taxonomy-aligned?

<ESMA_QUESTION_TRART8_6>
ISDA's non-financial members do not see the benefit of providing plans for OpEx and are of the view that all OpEx related to taxonomy-aligned activities should be counted.
<ESMA_QUESTION_TRART8_6>

Q7 Do you believe that any of the suggested approaches covered in questions 1 to 6 above will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, including whether they are one-off or ongoing, and provide your best quantitative estimate of their size.

<ESMA_QUESTION_TRART8_7>
ISDA's non-financial members believe that identifying the KPIs and relevant taxonomy-aligned and out of scope activities would be a burdensome requirement for companies whereas it is expected to increase personnel costs and IT costs. <ESMA_QUESTION_TRART8_7>

Q8 Do you agree that sectoral specificities should not be addressed in the advice, as proposed in Section 3.2.3?

<ESMA_QUESTION_TRART8_8>
ISDA's non-financial members are of the view that all sectors that are at the heart of the transformation required, would need sector-specific guidance for CapEx as the primary KPI to describe this transition. They consider that the turnover metric will only reflect previous investments and will remain both too small and too gradual to reflect the major investments being made and the importance of those sectors for large-scale taxonomy-alignment.

<ESMA_QUESTION_TRART8_8>

Q9 Do you agree with the requirements for accompanying information which ESMA has proposed for the three KPIs?

<ESMA_QUESTION_TRART8_9>
Endorsing EFAMA's response

Asset managers agree with the proposed requirements for accompanying information, given that contextual and qualitative information is essential for investors to put the Taxonomy KPIs in context. They would also suggest the inclusion of voluntarily disclosed "potentially aligned" activities where the firm has the objective to reach Taxonomy alignment in foreseeable future.

<ESMA_QUESTION_TRART8_9>

Q10 Do you consider that the requirement to refer to the relevant line item(s) in the financial statements for each KPI ensures sufficient integration between the KPIs and the financial statements?

<ESMA_QUESTION_TRART8_10>
ISDA's non-financial members are supportive of this requirement and would continue to ensure that KPIs are consistent with line items in their financial statements.
<ESMA_QUESTION_TRART8_10>

Q11 Do you agree with ESMA's suggestion to permit compliance by reference, so that non-financial undertakings may present the accompanying information elsewhere in the non-financial statement than in the immediate vicinity of the KPIs, as long as they provide a hyperlink to the location of the accompanying information?

<ESMA_QUESTION_TRART8_11>
ISDA's non-financial members are in agreement with this suggestion.
<ESMA_QUESTION_TRART8_11>

Q12 Do you consider there are additional topics that should be considered by ESMA in order to specify the content of the three KPIs? If yes, please elaborate and explain the relevance of these topics.

<ESMA_QUESTION_TRART8_12>
We strongly believe that there is a need for sector-specific guidance. We consider that a re-framing of the turnover metric as a measure of change/delta would be more appropriate for the transitioning sectors than focus on an absolute figure. It should also be noted that there is the potential to use the turnover change metrics in a number of different ways to truly analyse a portfolio's climate risk (such as is being done in carbon where the same data is being used to analyse the overall exposure in carbon intensity, the change in carbon intensity over time and the exposure to high carbon industries). Additionally, more specific guidance on OpEx is needed (please see our response to Q5).
<ESMA_QUESTION_TRART8_12>

Q13 Do you believe that providing the suggested accompanying information will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

<ESMA_QUESTION_TRART8_13>
ISDA's non-financial members are of the view that the suggested accompanying information would result in an increase of personnel costs due to an amplified work load for the organisation on a continuous basis. Additionally, one-off costs for IT landscape and projects would need to be considered.<ESMA_QUESTION_TRART8_13>

Q14 Do you agree that non-financial undertakings should provide the three KPIs per economic activity and also provide a total of the three KPIs at the level of the undertaking / group? If not, please provide your reasons and address the impact of your proposal to financial market participants along the investment chain.

<ESMA_QUESTION_TRART8_14>
Partially endorsing EFAMA's response

Asset managers believe that the economic activity breakdown is important for investors to conduct their own assessments and verify the level of Taxonomy alignment of investee companies.

On the other hand, ISDA's non-financial members believe that the provision of KPIs at each activity level is likely to introduce a level of reporting complexity and reconciliation that would risk outweighing the benefits to investors and give rise to potential information overload. They further believe that the requirement for accompanying information would better serve the need to explain KPI development to investors.
<ESMA_QUESTION_TRART8_14>

Q15 Do you agree that where an economic activity contributes to more than one environmental objective, non-financial undertakings should explain how they allocated the turnover / CapEx / OpEx of that activity across environmental objectives and where relevant the reasons for choosing one objective over another?

<ESMA_QUESTION_TRART8_15>
ISDA's non-financial members are in agreement with this proposal.
<ESMA_QUESTION_TRART8_15>

Q16 Do you agree that non-financial undertakings should provide information on enabling and transitional activities?

<ESMA_QUESTION_TRART8_16>
Partially endorsing EFAMA's response

ISDA's non-financial members are in agreement with this proposal, which would also enable financial market participants to make use of this information for their own disclosure obligations.

However, financial market participants would welcome more guidance on how to distinguish between these types of activities.

<ESMA_QUESTION_TRART8_16>

Q17 Do you agree that the three KPIs should be provided per environmental objective as well as a total at undertaking or group level across all objectives? If not, please provide your reasons and address the impact of your proposal to financial market participants along the investment chain.

<ESMA_QUESTION_TRART8_17>
Partially endorsing EFAMA's response

Asset managers would utilise disclosure per environmental objective especially for impact and thematic funds targeting a specific environmental objective. At the same time, disclosure at group/undertaking level across all objectives would facilitative comparability and Taxonomy integration.

However, ISDA's non-financial members would oppose this proposition as they note that it is very challenging to make the split per environmental objective whereas only the main environmental objective, which has been duly chosen to assess significant contribution towards, should be disclosed.<ESMA_QUESTION_TRART8_17>

Q18 Do you agree that non-financial undertakings should be required to provide the three KPIs for economic activities which are covered by the Taxonomy, economic activities which are covered by the Taxonomy but for which the relevant criteria are not met and therefore are not Taxonomy-aligned as well as for economic activities which are not covered by the Taxonomy?

<ESMA_QUESTION_TRART8_18>
Partially endorsing EFAMA's response

ISDA's non-financial members do not agree with this proposal give that according to Article 8 of the Taxonomy Regulation, undertakings shall only disclose the proportion of their turnover, CapEx and OpEx, which is taxonomy-aligned. Hence, a reporting of activities, that are not taxonomy-aligned is not foreseen in the Regulation. Even so, such a reporting would risk to result in additional administrative burden.

On the other hand, asset managers would encourage this breakdown, as it will help market participants to understand what could potentially align and what not, thereby avoiding misinterpretations. For activities that are not eligible under the Taxonomy, it is very important for asset managers to be able to distinguish between activities that do not meet its criteria and those that are not covered yet. The Taxonomy still covers a limited number of sectors, and companies should not be penalized for investing in uncovered sectors, such as digital or shipping. This would be consistent with the TEG's recognition of "potentially aligned" activities, namely those that are not yet covered or are performed outside of the EU.

For activities that that are eligible but not aligned, investors would also want to understand from firms whether "substantial contribution" or/and "do no significant harm" criteria are not met. Delineating the reasons for non-alignment of eligible activities is felt to be important also for international standardisation policy objectives, given that meeting the criteria will be especially challenging for activities outside the EU.

Highlighting the activities that are eligible for environmental sustainability but not yet meeting the criteria also has an enabling effect for asset managers' engagement, as that can be a powerful lever for investors to influence and stimulate the transition in the companies in their portfolio.

Finally, this breakdown is considered to enable the disclosure by asset managers in terms of aligned and eligible assets.
<ESMA_QUESTION_TRART8_18>

Q19 Do you agree with the proposal not to require retroactive disclosure concerning the four environmental objectives relating to the financial year 2021?

<ESMA_QUESTION_TRART8_19>
Endorsing EFAMA's response

We agree that requiring retrospective disclosures would be unnecessarily burdensome for companies.

In this context, we would like to draw attention to a timeline implementation inconsistency problem. Asset managers will need to report their level of Taxonomy compliance in January 2022, whereas Taxonomy reporting by companies will be available for 2022 only at the end of the financial year. As a result, asset managers will have no extra-financial data on Taxonomy compliance reporting available during the year of 2022.
<ESMA_QUESTION_TRART8_19>

Q20 Do you consider that there are specific elements in ESMA's draft advice which are not in line with the information needed by financial market participants in order to comply with their own obligations under the Taxonomy Regulation and the SFDR? If yes, please specify in your answer.

<ESMA_QUESTION_TRART8_20>
Partially endorsing EFAMA's response

ISDA's non-financial members, believe that the level of detail required such that each KPI is presented at every activity level will lead to a potentially significant explanatory burden where, for example, company A has to explain why its hydro activities are not taxonomy-relevant whereas company B's are. These industry-specific screening criteria are better explained as part of an annual audit and confirmed by auditors, than made available to each investor where sector-specific expertise cannot be expected.

Other ISDA members agree that auditors have an important role to play in terms of verification of disclosures and their breakdown, balanced with the need to manage costs for issuers.

On the other side of the spectrum, asset managers agree with ESMA´s approach in the draft advice, as they believe that the level of detail required such that each KPI is presented at every activity level would be instrumental for asset managers to comply with their obligations under the Taxonomy Regulation and SFDR.
<ESMA_QUESTION_TRART8_20>

Q21 Are there points that should be addressed in ESMA's advice in order to facilitate compliance of financial market participants across the investment chain? If yes, please specify.

<ESMA_QUESTION_TRART8_21>
Endorsing EFAMA's response

For compliance and cost management purposes, asset managers are looking into automating ESG information gathering. This objective could be facilitated by submitting Taxonomy disclosures in a machine-readable format.

They believe that the auditing of Taxonomy related disclosures would strengthen financial market participant compliance by strengthening the credibility of the disclosed information.
<ESMA_QUESTION_TRART8_21>

Q22 Do you believe that ESMA's detailed proposals under Section 3.3 will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

<ESMA_QUESTION_TRART8_22>
Please see our response to Q13.<ESMA_QUESTION_TRART8_22>

Q23 Do you consider there are additional topics that should be considered by ESMA in order to specify the methodology that non-financial undertakings should follow? If yes, please elaborate and explain the relevance of these topics.

<ESMA_QUESTION_TRART8_23>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_TRART8_23>

Q24 Do you agree that in order to ensure the comparability of the information disclosed under Article 8(2) of the Taxonomy Regulation and as such facilitate its usage, ESMA should propose the use of a standardised table?

<ESMA_QUESTION_TRART8_24>
Endorsing EFAMA's response

Please see our response to Q21.

A proposed standardised table may be advised, but it should not hinder innovation amongst reporting firms in developing more user-friendly formats to investors which provide more contextual information in the reporting template.
<ESMA_QUESTION_TRART8_24>

Q25 Do you consider that the standard table provided in Annex III of this Consultation Paper is fit for purpose? Do you think the standard table provides the right information, taking into account the burden on non-financial undertakings of compiling the data versus the benefit to users of receiving the data? If not, please explain and provide alternative suggestions to promote the standardisation of the disclosure obligations pursuant to Article 8 of the Taxonomy Regulation.

<ESMA_QUESTION_TRART8_25>
ISDA's non-financial members agree it would be good to report on an economic activity level but they do not see merit in each environmental objective requiring its own column. In particular, they agree with the first 4 columns and the last 3 columns. Column 5 could read instead "covered by Taxonomy and meets TSC" (for the relevant environmental objective). The remaining columns could become one column for showing whether the DNSH criterion is met or not for the remaining objectives, and one column for minimum safeguards. In addition, activities that are nor taxonomy-aligned or covered by the taxonomy should not be subject to reporting (e.g. derivatives, commodities, commodity derivatives).
<ESMA_QUESTION_TRART8_25>

Q26 Do you agree that the disclosure in the three standard tables should comply with the formatting rules mentioned in Table 5?

<ESMA_QUESTION_TRART8_26>
Partially endorsing EFAMA's response

ISDA's non-financial members are of the view that although some guidance on how to report is good, the table formatting should be in line with the overall design rules of the respective company. Otherwise the taxonomy section will be inconsistent with the formats of the rest of the financial and non-financial reports.

On the other hand, asset managers believe that these formatting rules are important for automated data gathering without the need for data cleansing.
<ESMA_QUESTION_TRART8_26>

Q27 Do you believe that ESMA's detailed proposals under Section 3.4 will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

<ESMA_QUESTION_TRART8_27>
Please see our response to Q13.<ESMA_QUESTION_TRART8_27>

Q28 Do you agree that a share of investments is an appropriate KPI for asset managers? If you do not, what other KPI could be appropriate, please justify.

<ESMA_QUESTION_TRART8_28>
Partially endorsing EFAMA's and AIMA's responses

We agree that a share of investments as a ratio of eligible investments that are Taxonomy aligned is an appropriate indicator. We note that the weighted average indicator is also aligned with recommendations by the TCFD for carbon footprint disclosures.

We would recommend as much consistency as possible with requirements that already apply under the SFDR under Article 8 and 9, but also 7 (principal adverse impact considerations).

We also welcome the fact that ESMA recognizes the current lack of data on ESG indicators on underlying investments. Access to data on private companies or on companies headquartered outside the EU and not subject to the NFRD can be very complex and might not be always available.

Private research shows that globally under 30% of companies have disclosed data on green activities and their revenues. Comparable disclosures across the investment chain are thus important so investors and issuers are focusing on a consistent set of metrics. This would also help comparable assessments of EU taxonomy alignment among different investors. Standardised sector specific disclosures should also be considered as an efficient way to make do no significant harm (DNSH) and minimum social safeguard (MSS) assessments.

We therefore strongly support one of the possibilities mentioned by ESMA in the consultation paper which is to restrict the denominator to Article 8 and 9 funds and to eligible assets in these funds.

<ESMA_QUESTION_TRART8_28>

Q29 This advice focuses on the collective portfolio management activities of asset managers. Should this advice also cover potentially any other activities that asset managers may have a license for, such as individual portfolio management, investment advice, safekeeping and administration or reception and transmission of orders ('RTO')?

<ESMA_QUESTION_TRART8_29>
Endorsing EFAMA's response

Asset managers do not believe that the disclosure of these activities on Taxonomy compliance would be relevant and bring added value to the policy objective. Such requirements would be costly, immaterial and onerous and could therefore be detrimental to the general investment process.

They consider that it may be helpful to align with the scope of SFDR. Under SFDR, asset managers would be covered under the categories of UCITS ManCo, AIFM and MiFID investment firm providing portfolio management.
<ESMA_QUESTION_TRART8_29>

Q30 Do you agree that for the numerator of the KPI the asset manager should consider a weighted average of the investments exposed to investee companies based on the share of turnover derived from Taxonomy-aligned activities of the investee companies? If not please propose and justify an alternative.

<ESMA_QUESTION_TRART8_30>
Partially endorsing EFAMA's response
However, ISDA's non-financial members note that, as also acknowledged by ESMA, CapEx is often the more important metric, especially for sectors in transition. This must be reflected in the disclosure of asset managers as well. Looking mainly at the turnover will lead to a static picture, that doesn't take future plans of companies and their decarbonization potential into account. The use of CapEx will show, which path a company is following and if it is willing to decarbonize. Thus, asset managers should weight their investments based on CapEx, not turnover.

Similarly, asset managers would recommend giving equal weight also to the CapEx indicator compared to the turnover indicator. CapEx is a crucial forward looking metric because it reflects new, incremental green investments in the economy filling the existing investment gap.

<ESMA_QUESTION_TRART8_30>

Q31 Do you agree that in addition to a main turnover-derived Taxonomy-alignment KPI, there is merit in requiring the disclosure of CapEx and OpEx-derived figures for Taxonomy-alignment of an asset managers' investments?

<ESMA_QUESTION_TRART8_31>
Please see our responses to Q5 and Q30 above.

<ESMA_QUESTION_TRART8_31>

Q32 Do you think sovereign exposures, such as sovereign bonds (but excluding green bonds complying with the EU Green Bond Standard) should be considered eligible investments and if so under what methodology?

<ESMA_QUESTION_TRART8_32>
Partially endorsing EFAMA's response

Some ISDA members are of the view that the taxonomy needs to be applicable on a multi-asset basis in order to effectively encourage investment towards a net zero economy including listed equity and sovereign bonds. Sovereign exposures are a key and important part of the transition and there is growing investor interest (e.g. recent launches of climate adjusted sovereign bonds).

On the other hand, asset managers believe that given that the EU GBS, as well as green standards, methodologies or possible certificates (Bruegel, 2020) for conventional sovereign bonds are only being developed, it would be premature to include sovereign bonds at this point. Other asset classes, such as commodities, should also not constitute eligible investments.
<ESMA_QUESTION_TRART8_32>

Q33 Do you agree that the denominator should consist of the value of eligible investments in the funds managed by the asset manager or should it be simply the value of all assets in the funds managed by the asset manager?

<ESMA_QUESTION_TRART8_33>
Endorsing AIMA's and EFAMA's responses

Asset managers believe that the value of eligible investments in the funds is a more insightful and accurate figure than total AuM at entity level.

Given that clients invest in products, asset managers should disclose this KPI at the level of investment products to guide their investment choices between different sustainable product offerings. Furthermore, the level of Taxonomy alignment will be applicable in the current data environment, and for the next several years, only for equity and corporate bond funds, excluding a large proportion of non-eligible asset classes in AuM.

Nonetheless, for transparency purposes, we could also envision including a secondary figure on total AuM (e.g. disclosing what % of their AuM is not Taxonomy eligible).

This approach would at least allow a picture that would be closer to reality than a KPI based on a denominator for which a number of assets, are not related to sustainability due to their investment universe (e.g. sovereign bonds, interest rates derivatives).

<ESMA_QUESTION_TRART8_33>

Q34 Do you support restricting the denominator to funds managed by the asset manager with sustainability characteristics or objectives (i.e. governed by Article 8 or 9 of Regulation (EU) 2019/2088)? What are the benefits and drawbacks of such an approach?

<ESMA_QUESTION_TRART8_34>
Endorsing EFAMA's response

Asset managers are of the view that restricting the denominator to funds with sustainability characteristics could create a disincentive for integrating ESG considerations into other than Article 8 and 9 funds. Many funds managed by large asset managers, are not related to sustainability due to their investment universe (e.g. FX, global macro). Reporting only on Article 8 and 9 products, which may constitute a minority of asset manager´s AuM, may also not provide the full picture of the asset manager´s financing of Taxonomy aligned activities.

They therefore recommend using the application of the Article 8 and 9 funds denominator as an additional indicator, but it should not replace the eligible investments indicator in question 33.

<ESMA_QUESTION_TRART8_34>

Q35 Is it appropriate to combine equity and fixed income investments in the KPI, bearing in mind that these funding tools are used for different purposes by investee companies? If not, what alternative would you propose?

<ESMA_QUESTION_TRART8_35>
Endorsing EFAMA's response

Asset managers do not see the combination of equity and fixed income investments in the KPI as problematic.
<ESMA_QUESTION_TRART8_35>

Q36 Do you believe the proposed advice will impose additional costs on asset managers? Please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

<ESMA_QUESTION_TRART8_36>
Endorsing EFAMA's response

Asset managers believe the highest costs will be related to acquisition of data from data providers and in terms of workload for aggregating, analysing and reporting on the data in non-financial reports. Comparing these two cost segments, we believe that product level disclosure obligations will be more costly than the entity level reporting.
<ESMA_QUESTION_TRART8_36>

Q37 What are the benefits and drawbacks of limiting Taxonomy-aligned activities to those reported by Non-Financial Reporting Directive companies?

<ESMA_QUESTION_TRART8_37>
Please see our response to Q28.
<ESMA_QUESTION_TRART8_37>

Q38 Do you agree with ESMA's recommendation that the Commission develop a methodology to allow a sector-coefficient to be assigned for non-reporting investee companies?

<ESMA_QUESTION_TRART8_38>
Endorsing EFAMA's response

While asset managers agree that the EC should consider the feasibility of developing a methodology to allow KPI calculation to also cover investments in companies not reporting under the Non-Financial Reporting Directive the extent of their Taxonomy-aligned activities, they disagree that the way forward is exclusively by assigning them a coefficient derived on a sector-basis under a common methodology.

They believe that the assignment of a coefficient should be applied to those stocks that lack minimum reporting, given that coefficients could undermine companies that make the effort to disclose on the Taxonomy. But for all those that have a certain level of disclosures, a more thorough customised methodology based on proxies and estimations should apply. This will allow a) for more accurate results; b) will help encourage non-NFRD companies to disclose and will encourage investors to ask for greater transparency; and c) will not undermine those companies that make the effort to disclose. A mixed approach should be allowed. The EC should consider developing specific guidelines and rules for both approaches. The Platform should provide advice to the EC on those.
<ESMA_QUESTION_TRART8_38>

Q39 Should netting be allowed, on the lines of Article 3 of the Short-Selling Regulation?

<ESMA_QUESTION_TRART8_39>
Endorsing AIMA's response

Asset managers agree that netting should be allowed following the lines of Article 3 of the Short Selling Regulation. They would recommend however avoiding the assumption that shorts are only relevant as hedges to corresponding long positions.

Furthermore, they note that the example shows that a short position can reduce the alignment with the Taxonomy. They would also welcome examples on how alignment can be increased by a short exposure, in the case when non-Taxonomy aligned investments are being shorted, and Taxonomy-aligned investments are not.
<ESMA_QUESTION_TRART8_39>

Q40 How should derivatives be treated for the calculation purposes? Should futures be considered as potential Taxonomy-aligned investments?

<ESMA_QUESTION_TRART8_40>
Partially endorsing EFAMA's response

As acknowledged by the JRC in its revised draft Technical Report v3.0 and 3rd Criteria Proposal, *"considering the importance of theses underlying assets for diversifications purposes, it is suggested that such types of underlying assets are excluded as an eligible green asset class. Still, they are included in the calculation of total portfolio value."*

Although ISDA agrees in principle with the inclusion of derivatives in the calculation of total portfolio value, we consider that it is essential that investment managers are not prevented or excessively restricted from using derivatives as the use of derivatives can bring benefits, such as increased liquidity and supply of credit to the market, which may be crucial to the ability of investment managers to realise sustainable investments.

As noted in ISDA's response to the revised draft Technical Report v2.0 with Criteria Proposals on the Development of an EU Ecolabel for 'Financial Products', derivatives have an important role to play in a sustainable finance context as they could contribute to the achievement of the EU's long-term sustainable investment strategy goals by:

- facilitating capital raising of the amounts needed to finance the transition to a low-carbon economy
- helping firms manage financial risks related to ESG issues
- helping firms manage their businesses risk for the long-term by smoothing volatility from a variety of factors that may occur in the short term

Given that derivatives are an efficient low-cost tool for investment firms to manage their portfolio risks and they enable capital to be freed up for investments, investment firms are more likely to make longer-term investments if they are able to efficiently hedge the risks of such investments. From an economic perspective, it is perfectly acceptable and appropriate for a fund manager or asset manager to take on an exposure with derivatives even when there is no underlying risk to hedge. They are sophisticated investors and have the ability to appropriately assess the various risks. This should not be confused with the notions of long-termism / short- termism. Derivatives are a tool that can support both long-term and shorter-term investment strategies, rather than an indicator of the type of strategy undertaken.

At present, ~~the~~ ESG investments generally represent a limited fraction of the bond or stock markets. With the upcoming taxonomy of EU sustainable activities, it is anticipated that this selection could become even more restrictive. As a consequence, institutional and retail investors are expected to opt for portfolio diversification solutions that will allow them to hedge risks and/or limit trading costs through the use of derivatives. It is therefore crucial that investors are not discouraged to invest in green assets without having the opportunity to neutralize common risks.

Moreover, ISDA's non-financial members are of the view that the activities of the wider real economy on the wholesale commodity and commodity derivatives markets should not be in scope of the EU Taxonomy. Non-financial firms use the commodity and commodity derivatives markets to reduce their commodity (price) risks and this risk management activity should not be constrained by an assessment under the EU Taxonomy. Also, a commodity derivative is typically not specifically linked to an underlying specific economic activity of a corporate in scope of the current EU Taxonomy, but rather to the market price of an underlying commodity.

For futures, asset managers recommend against measuring them as this would require look-through. For example, measuring 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.

<ESMA_QUESTION_TRART8_40>

Q41 What are the costs and benefits associated with the different options for non-reported activity coverage, netting and derivatives treatment presented above? Please provide a quantitative estimate for each option, distinguishing between one-off and on-going costs.

<ESMA_QUESTION_TRART8_41>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_TRART8_41>

Q42 Do you have any views on the proposed advice recommending a standardised table for presentation of the KPI for asset managers in Annex IV?

<ESMA_QUESTION_TRART8_42>
Partially endorsing EFAMA's response

Asset managers question the merits of having to break down their AuM by economic activity. There are a total of 21 NACE macro sectors, with 7 of these having been identified as relevant by the TEG for climate mitigation. These 7 macro sectors have been further broken down into over 70 more detailed economic activities. As the remaining four environmental objectives are screened, asset managers are likely to see this list multiply considerably. Given that most asset managers invest across the market, disclosures by economic activity would become extremely cumbersome for them.

It should be added that financial market participants, subject to reporting requirements under articles 5 to 8, should not be obliged to report in line with NACE. Instead, they should continue using sector frameworks aligned with investment guidelines and investment workflows.

Furthermore, the proposed template assumes that for all environmental objectives there are and/or will be transitioning and enabling activities; and that is not the case already for climate adaptation and no decision has been taken regarding the remaining activities.

However, some ISDA members, are of the view asset managers should disclose 'contribution' to relevant economic activities and % of the portfolio that has environmental characteristics (i.e. activities that are potentially aligned with the EU taxonomy) in order to build a more complete and transparent narrative for end investors.
<ESMA_QUESTION_TRART8_42>

Q43 Do you agree with presenting accompanying information in the vicinity of the standard table?

<ESMA_QUESTION_TRART8_43>
Endorsing EFAMA's response

Asset managers agree that information should be provided within the vicinity of the main KPIs.
<ESMA_QUESTION_TRART8_43>

Q44 Do you agree that there would be merit in including in the accompanying information a link, if relevant, to an asset managers' entity-level disclosures on principal adverse impacts of investment decisions on sustainability factors?

<ESMA_QUESTION_TRART8_44>
Endorsing EFAMA's response

Asset managers believe that the same formatting criteria would be conducive to automating and structuring of ESG data.
<ESMA_QUESTION_TRART8_44>

Q45 Do you agree with adopting the same formatting criteria as presented in Section 3.4.2 for the asset manager KPI disclosure?

<ESMA_QUESTION_TRART8_45>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_TRART8_45>

Q46 What are the one-off and on-going costs of setting up the reporting and disclosure under this obligation? Please clarify the type of costs incurred and provide a quantitative estimation where possible.

<ESMA_QUESTION_TRART8_46>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_TRART8_46>