

**MEMO# 32484**

May 26, 2020

# **EU Disclosure Regulation: Adverse Sustainability Impact Disclosure - Preliminary Analysis of the 500 Employee Threshold Requirement**

[32484]

May 26, 2020 TO: ESG Task Force

ICI Global Regulated Funds Committee RE: EU Disclosure Regulation: Adverse Sustainability Impact Disclosure - Preliminary Analysis of the 500 Employee Threshold Requirement

The EU Disclosure Regulation<sup>[1]</sup> mandates website disclosure of “principal adverse impacts of investment decisions on sustainability factors” for “financial market participants”<sup>[2]</sup> with more than 500 employees.<sup>[3]</sup> Financial market participants with fewer than 500 employees are subject to this requirement on a comply-or-explain basis.<sup>[4]</sup> We received a number of questions regarding how to apply the 500-employee requirement to global businesses with EU-based subsidiaries.

As background, the Disclosure Regulation outlines the following two scenarios in which a financial market participant will exceed the 500-employee threshold and therefore be subject to mandatory disclosure of principal adverse impacts:

- A financial market participant that exceeds on its balance sheet the average number of 500 employees during the financial year,<sup>[5]</sup> or
- A financial market participant that is a parent undertaking of a “large group” as referred to in Article 3(7) of Directive 2013/34/EU<sup>[6]</sup> (Accounting Directive), exceeding on the balance sheet date of the group, on a consolidated basis, the average number of 500 employees during the financial year.<sup>[7]</sup>

While each firm should make their own determinations based on their own facts and circumstances,<sup>[8]</sup> we share below the initial high-level legal analysis from our outside counsel, who concluded that—

- Where a group parent is an (unregulated) holding company with multiple financial market participants as its subsidiaries, the counsel does not consider that Article 4(3) should apply to the group. As such, there would be no need to aggregate the number of employees across the group. Therefore, the requirement to consider adverse impacts of investment decisions on sustainability factors would apply to such

subsidiaries on an individual basis and only on a comply-or-explain basis as provided for by Article 4(1) of the Disclosure Regulation.

- However, for any financial market participants within such a group that are themselves parent companies (and which, with their subsidiaries, have 500+ employees), then an accounting analysis may be needed to determine whether this “sub-group” qualifies as a “large group” under the Accounting Directive. Under Article 3(7) of the Accounting Directive, a “large group” is a group consisting of a parent and its subsidiary undertakings that are included in a consolidation and which, on a consolidated basis, exceed two of the three following criteria: (i) balance sheet total: EUR 20 000 000; (ii) net turnover: EUR 40 000 000; (iii) average number of employees during the financial year: 250. For example, a global investment management group could have a European entity which is a financial market participant and which consolidates its subsidiaries onto its balance sheet.

We hope this is helpful.

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#### **endnotes**

[1] See REGULATION (EU) 2019/2088 (Disclosure Regulation), *available at* <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R2088&from=EN>. For a detailed summary of the new ESG-related disclosure requirements that the Disclosure Regulation will impose on asset managers and funds, please see ICI memo no. 32229, *available at* <https://www.iciglobal.org/iciglobal/pubs/memos/ci.memo32229.global>. The European Supervisory Authorities recently launched a consultation on draft regulatory technical standards for the Disclosure Regulation, including details on adverse impact disclosure. See ICI memo no. 32441, *available at* <https://www.iciglobal.org/iciglobal/pubs/memos/ci.memo32441.global>.

[2] As relevant to this memorandum, the definition of “financial market participant” includes a management company of an undertaking for collective investment in transferable securities, and it also includes, among other definitions, an investment firm which provides portfolio management; an institution for occupational retirement provision (IORP); a manufacturer of a pension product; an alternative investment fund manager (AIFM); and a pan-European personal pension product (PEPP) provider. For a complete definition, see Article 2 of the Disclosure Regulation.

[3] See Disclosure Regulation, Article 4.

[4] *Id.*

[5] See *id.*, at Article 4(3).

[6] See Directive 2013/34/EU (Accounting Directive), *available*

at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L:2013:182:FULL&from=EN>.

[7] See Disclosure Regulation, Article 4(4).

[8] This memorandum does not constitute legal advice.

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