

MEMO# 30987

December 19, 2017

European Commission Consultation on Asset Managers' Use of ESG Factors

[30987]

December 19, 2017 TO: ICI Members

Investment Company Directors

ICI Global Members SUBJECTS: Disclosure

Fund Governance

International/Global

Investment Advisers RE: European Commission Consultation on Asset Managers' Use of ESG Factors

The European Commission (EC) published a consultation and an impact assessment that consider whether institutional investors and asset managers should be required to take into account and disclose material sustainability factors.^[1] The consultation and impact statement respond to an interim report of the EC-appointed High-Level Expert Group that recommends, among other things, that the EC clarify in legislation or regulatory reviews that the fiduciary duties of institutional investors and asset managers explicitly integrate material sustainability (*i.e.*, environmental, social, and governance (ESG)) factors with a view toward long-term performance.^[2]

The Impact Assessment outlines four policy options for evaluation as follows:

1. **Disclosure.** Imposing disclosure rules to document how institutional investors and asset managers are taking into account sustainability factors.
2. **Investment policy and asset allocation.** Enhancing the consideration of material sustainability factors in investment strategy/asset allocation.
3. **Risk management.** Improving the consideration of sustainability risks as part of risk management processes.
4. **Governance arrangements.** Adapting governance arrangements to ensure appropriate decision-making capabilities.

The EC is concerned that institutional investors and asset managers do not sufficiently consider material sustainability risks and that existing fiduciary duty requirements do not clearly require assessment of these risks. The EC also believes that institutional investors and asset managers generally understand their fiduciary duties to require “a focus on maximizing short-term financial returns,” which may cause them to disregard long-term effects on performance due to sustainability factors and risks. The EC also points to

concerns about lack of transparency in how institutional investors and asset managers consider sustainability factors in their decision-making.

Concurrently, the EC released the Consultation Paper to gather feedback on ways to improve how institutional investors and asset managers assess and integrate sustainability factors in their decision-making process.^[3] The Consultation Paper asks a number of questions around whether and how investment managers consider or should consider sustainability factors in their investment decisions. Among other things, the Consultation Paper also asks whether existing corporate disclosures provide investment managers with adequate sustainability risk information. The deadline to respond to this consultation is January 22, 2018.

The EC intends the responses to this consultation to inform the High-Level Expert Group's final recommendation on fiduciary duty and sustainability. We understand that the EC may publish an Action Plan on sustainable finance in March 2018.

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endnotes

[1] European Commission, *Consultation: Institutional investors and asset managers' duties regarding sustainability*, available at https://ec.europa.eu/info/sites/info/files/2017-investors-duties-sustainability-consultation-document_en.pdf (Consultation Paper); European Commission, *Inception Impact Assessment: Institutional investors and asset managers' duties regarding sustainability*, available at http://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017-5524115_en (Impact Assessment).

[2] EU High-Level Expert Group on Sustainable Finance, *Interim Report: Financing a Sustainable European Economy*, at p. 57, (July 2017), available at https://ec.europa.eu/info/sites/info/files/170713-sustainable-finance-report_en.pdf (Expert Group Report). The EC appointed the Expert Group to develop a comprehensive EU strategy on "sustainable finance" that aligns with the Paris Agreement on climate change and the UN 2030 Agenda for Sustainable Development. The Expert Group Report also recommends strengthening financial disclosure of material information on sustainability (i.e., ESG) issues.

[3] European Commission, *Consultation: Institutional investors and asset managers' duties regarding sustainability*, available at https://ec.europa.eu/info/sites/info/files/2017-investors-duties-sustainability-consultation-document_en.pdf.

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