



aba position paper for the trilogue negotiations regarding the Proposal for a Disclosure Regulation

27 February 2019

The **aba Arbeitsgemeinschaft für betriebliche Altersversorgung e.V.** - is the German association representing all matters concerning occupational pensions in the private and public sector. The aba has 1,100 members including corporate sponsors of pension schemes, IORPs, actuaries and consulting firms, employer associations and unions, as well as insurance companies, banks and investment managers. According to our statutes, our mission is to represent existing schemes as well as to expand coverage of occupational pensions independent of vehicle. We are a member of the European Association [PensionsEurope](#).

Main points

In May 2018, the European Commission published three proposals for regulations to strengthen sustainable finance. Generally, we are concerned that the legislation which is currently being discussed is not tailored to IORPs and therefore it will be difficult for IORPs to comply. This paper summarises our main points regarding the proposed disclosure regulation:

- **Scope - financial market participants and financial products:** The proposed regulation should recognise that IORPs have a social purpose and regularly act as users of financial market products. Because of the differences in labour and social law across the EU, the IORP II Directive sets minimum standards only. IORPs should therefore not be included in the definition of financial market participants. Any changes for IORPs should be carried out by amending the IORP II Directive. In contrast to financial products, pension schemes are embedded in national social and labour law and should therefore not be defined as “financial market product”.
- **Subject matter:** The distinction between disclosure rules for the integration of sustainability risks in the investment decision process of *financial market participants* on the one hand and harmonised transparency rules for *financial products* that explicitly aim at sustainable investments on the other as set out in the Commission’s proposal and Council Position is generally adequate. We would also like to emphasise that a *Disclosure Regulation* should truly be about disclosure – such a regulation should not lead to a new interpretation of the prudent person principle (Art. 19 IORP II Directive).
- **Where does a sustainability objective begin?** It should be clearly defined when a financial product becomes a product with a sustainability objective. Compliance with existing legal requirements should not lead to an inclusion in the definition of a financial product with a sustainability objective. In addition, the consideration of ESG factors in certain areas of investment decision-making should not mean that the product will be labelled as a product with a sustainability objective.
- **Definition of sustainability risk:** A broad definition of “sustainability risk” as proposed by the Council seems adequate considering the range of financial market participants covered, even if IORPs shouldn’t be included in the scope.
- **Delegated acts by the Commission and Guidelines by EIOPA:** We support the Council Position which does not introduce delegated acts into the IORP II Directive, because it takes into account the objective of the Directive, which is EU minimum harmonisation.

The transposition of the IORP II Directive is supported by EIOPA through “opinions and reports”. We therefore do not understand why the Council text refers to “guidelines” issued by EIOPA. Recital 13 should be deleted.

If the objective is specifying “how investment decisions and risks assessment by IORPs take into account environmental, social and governance risks under Directive (EU) 2016/2341”, an amendment of Art. 19 IORP II Directive would be necessary to change the existing investment rules. This change then would have to be transposed by the Member States. EIOPA could support this process of transposition by publishing opinions and reports.

- **Amending the IORP II Directive:** Generally, any changes for IORPs should be made by amending the IORP II Directive. If changes to the IORP II Directive are made, we call for an adequate period of time to gather experience before new rules are created. The IORP II Directive provides for 13 January 2023

as the deadline for an evaluation and review.

Despite the urgency to mitigate climate change, things shouldn't be rushed. Regarding IORPs, the implications for the members and beneficiaries should be considered. New ESG regulation for IORPs should build upon the rules introduced by the IORP II Directive and take into account the role of IORPs in the financial markets – as investors and buyers of products they are on the demand side of the market. This way it can be ensured that on the one hand ESG factors will feature more and more in risk management and investment decisions, while on the other hand over 10m members and beneficiaries in Germany and many more across the EU will benefit from reliable occupational pensions now and in the decades to come.

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Introduction

Institutions for occupational retirement provision (IORPs) are pension institutions with a social purpose and ensure together with sponsoring employers the occupational pensions of millions of people across the EU. In Germany, around 8.6m members and 1.5m beneficiaries were covered by a pension plan provided by an IORP in 2017.¹ The given pension promises regularly run over several decades, rendering IORPs long-term investors in the financial markets. The IORP II Directive ([EU 2016/2341](#)), which had to be transposed into national law by 13 January 2019 introduced prudential requirements for IORPs regarding for the first time the treatment of ESG factors and risks.² On this backdrop we support the objective of the European Commission to foster transparency in the area of sustainable investments. Better data on ESG issues which IORPs can use at low cost would help to remove the barriers IORPs currently face when seeking to integrate ESG factors in their risk management and investment decision making processes.

In May 2018, the European Commission published three proposals for regulations to strengthen sustainable finance.³ In August 2018 the aba provided [Feedback](#) on the Proposal by the Commission on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016/2341 (Overview over the relevant EU documents in the [Legislative Observatory](#)). In October, the aba published an [aba position paper](#) on the Draft Report on the Proposal for a Disclosure Regulation by the Committee on Economic and Monetary Affairs of the European Parliament. In February 2019, these two papers were completed with a [position paper](#) on the agreed Council position.⁴

Generally, we are concerned that the legislation which is currently being discussed is not fit for purpose for IORPs and therefore it will be difficult for IORPs to comply. This paper summarises our main points – it contains both recommendations of how to regulate in this area and concerns about specific proposals:

1. Scope: financial market participants and financial products
2. Subject matter
3. Where does sustainability begin?
4. Definition of sustainability risk
5. Delegated acts by the Commission and Guidelines by EIOPA
6. Amending the IORP II Directive

1. Scope: financial market participants and financial products

According to Art. 2a (in all three documents) IORPs fall under the definition of financial market participants and with that under the proposed regulation. According to the Council document, 'financial product' means i.a. a pension scheme; "'pension scheme' means a pension scheme as defined in Article 6(2) of Directive (EU) 2016/2341" (Art. 2 (j) and (l) respectively).

¹ [BaFin-Erstversicherungsstatistik 2017](#); in Germany, Pensionskassen and Pensionsfonds are IORPs according to the IORP II Directive.

² The IORP II Directive includes requirements regarding ESG in the following articles: Art. 19 (Investment rules), Art. 21 (General governance requirements), Art. 25 (Risk management), Art. 28 (Own-risk assessment), Art. 30 (Statement of investment policy principles) and Art. 41 (Information to be given to prospective members).

³ Overview over the [Commission's work on sustainable finance](#)

⁴ Our website [provides](#) an overview of the developments regarding the three Commission Proposals from May 2018 relating to sustainable finance (in German).

This classification does neither respect the social purpose of IORPs⁵ nor takes it into account that IORPs are mostly (end-) investors in financial instruments/products in the financial market. Very few IORPs compete at all, most IORPs neither with each other nor with financial service providers. Transparency rules have to take into account – as for example done in the Shareholder Rights Directive - whether they are directed at (end-) investors in financial instruments/products (e.g. IORPs) or sellers (e.g. asset managers) of financial products.

We disagree with the assessment of the Commission that harmonisation in this area is necessary for all financial market participants covered by the Action Plan on ‘Financing sustainable growth’ because of their regular cross-border activities – this is not the case for IORPs: At the end of 2016, 0.05% of IORPs were cross-border pension funds – 83 IORPs out of 155,000 IORPs in total.⁶

Pension schemes should not be considered financial products – they are embedded in national social and labour law which protects the members and beneficiaries of pension schemes. This is a very different framework to that of financial products; they are embedded in consumer protection legislation.

- The proposed regulation should recognise that IORPs have a social purpose and regularly act as users of financial market products. Because of the differences in labour and social law across the EU, the IORP II Directive sets minimum standards only. IORPs should therefore not be included in the definition of financial market participants. Any changes for IORPs should be carried out by amending the IORP II Directive. In contrast to financial products, pension schemes are embedded in national social and labour law and should therefore not be defined as “financial product”.

2. Subject matter

Both the Commission and the Council documents lay down harmonised rules for financial market participants about the disclosure of the integration of sustainability risks in the investment decision-making process on the one hand and for financial products that have as their objective sustainable investment on the other. In both texts this distinction results in different requirements for the two groups in the following articles. We support this distinction.

The ECON Report seeks to include all financial products, „whether or not they are targeted with a sustainable impact“ under this Regulation. This would mean that all financial market participants and all products are covered, rendering the distinction between the two categories meaningless.

- The distinction between disclosure rules for the integration of sustainability risks in the investment decision process of *financial market participants* on the one hand and harmonised transparency rules for *financial products* that explicitly aim at sustainable investments on the other as set out in the Commission’s proposal and Council Position is generally adequate.
- We would also like to emphasise that a *Disclosure* Regulation should truly be about disclosure – such a regulation should not lead to a new interpretation of the prudent person principle laid down in Art. 19 (Investment rules) IORP II Directive.

While we support the distinction described above, we are concerned about some of the requirements introduced for all financial market participants. The Council Position stipulates in Art. 4 (1) b that pre-contractual disclosure needs to include „the result of the assessment of the likely impacts of sustainability risks on the re-

⁵ See Recital 32 IORP II Directive: “IORPs are pension institutions with a social purpose that provide financial services. (...) such institutions should not be treated as purely financial service providers.”

⁶ EIOPA 2017 Market development report on occupational pensions and cross-border IORPs 30 Jan 2018

turns of the financial products“. This is not relevant in cases where a defined benefit promise is given – in those cases, risks – including ESG risks – are irrelevant for the promised benefit because these risks are borne by the IORP and ultimately by the employer. Information about them would mean additional cost to IORPs without any benefit for the members and beneficiaries, who, to the contrary, might be overwhelmed by information they do not need.

In this regard, the Commission proposal is more adequate, referring to a ‘relevant impact’: „the extent to which sustainability risks are expected to have a relevant impact on the returns of the financial products made available.“ However, we would prefer the introduction of information requirements tailored to the needs of prospective members, while taking into account the related costs for IORPs. This way, defined benefit (and hybrid) promises where members and beneficiaries only bear limited risks could be accommodated. Changing the IORP Directive (Art. 41 addresses information to prospective members) would be the right approach to achieve this.

- Sustainability risks are not always risks to members and beneficiaries of a pension plan offered by an IORP. Any information requirements for IORPs towards prospective members should be tailored to their needs and should follow the principle that information should only be provided if it is relevant and truly adds a value in relation to its costs. This could be achieved by directly amending the IORP II Directive.

3. Where does a sustainability objective begin?

According to the Commission and the Council text, financial products aiming for sustainability have to comply with the requirements laid down in the proposed regulation as well as with the following Level-2-regulation. The key question is how these products are defined, in other words, when a regular financial product becomes a financial product with a sustainability objective.

As stated above, we recommend not including IORPs in the definition of financial market participants. If nevertheless this or a similar requirement is introduced for IORPs, we would like to point out the following: It should be clarified that merely complying with other legal requirements (such as the IORP II Directive or the Shareholder Rights Directive ([\(EU\) 2017/82](#)) cannot lead to a product being labelled as having a sustainability target or objective.⁷ If this was the case, all pension plans would automatically become products with a sustainable objective, which would defy the purpose of making it clear which products do have such an objective and which do not.

If an IORP considered ESG factors in its investment decision making process in some areas (e.g. for shares, but not for other types of investment), this should not lead to the specific pension plan falling under the rules for sustainable investment products either. Only products / pension plans which explicitly have a sustainability objective should be considered to fall in this category, otherwise the category would lose meaning.

- It should be clearly defined when a financial product becomes a product with a sustainability objective.
- To clarify that compliance with legal requirements does not mean that the product will be labelled as a product with a sustainability objective, we propose that the following text is added to Recital 4a (to be inserted after the sentence „As a consequence, as regards the financial products with environmental or social characteristics, financial market participants should disclose whether...“): „Compliance with

⁷ The Commission Proposal refers to a „target“, the Council to an „objective“.

legal requirements regarding ESG only should not mean that the products provided are financial products that have as their objectives sustainable investments.“

- To clarify that a consideration of ESG factors in certain areas of investment decision-making does not mean that the product will be labelled as a product with a sustainability objective, we propose that the following text is added to Recital 4a (after the sentence proposed above): “For a financial product to be labelled as a product with a sustainability objective, all related investment decisions need to be based on a consideration of ESG factors, with the aim to label it as a ESG product. The pure consideration of ESG factors without the aim of a product labelling should not fall within the scope of the disclosure rules. ”

4. Definitions: sustainability risk

In the Commission proposal “sustainability risk” is not defined; the ECON Report includes a definition with the intention to spell it out further through a delegated act⁸ (Art. 2 (sa) of the ECON Report); and the Council agreed on the following brief definition: “‘sustainability risks’ means an environmental, social or governance event or condition that, if it occurs, could cause a material negative impact on the value of investment” (Art. 2 (t) of the Council position).

If sustainability risk is a central concept in the proposed Regulation it seems necessary to define it. Considering the range of financial market participants (and what they offer) covered, however, it seems adequate to choose a broad definition without prescribing too much detail.

- A broad definition of “sustainability risk” as proposed by the Council seems adequate considering the range of financial market participants covered, even if IORPs are not included in the scope.

5. Delegated acts by the Commission and Guidelines by EIOPA

We welcome that the Council position has deleted the delegated acts for IORPs proposed by the Commission in Art. 10 of the draft regulation. We note that the ECON Committee voted with a narrow margin only to keep the delegated acts in the text.

From our perspective delegated acts are not a suitable instrument for the regulation of IORPs: Delegated acts that regularly aim for full EU harmonisation do not fit into any directive that aims for minimum EU standards to accommodate the differences in labour and social law across the EU. Furthermore, delegated acts are limited to amending non-essential elements. The proposed delegated acts would amend the prudent person rule (Art. 19 IORP II), which is an essential requirement for IORPs. It is neither justified nor understandable why the pro-

⁸ (sa) ‘sustainability risks’ mean financial or non-financial risks, material or likely to be materialised, linked to environmental, social and governance risks and factors, where material for a particular investment approach; ‘sustainability risks’ comprise:

(a) short-term and/or long-term risks to the return of a financial or pension product that arise from its exposure to economic activities that can have adverse environmental or social impact, or from the product's exposure to investee entities that exhibit poor governance;

(b) the short-term and/or long-term risk that the economic activities to which a financial or pension product is exposed have negative impacts on the natural environment, on workforces and communities, or on the governance of investee entities, including but not limited to when linked to financial risk referred to in point (a);

Financial market participants should consider the environmental, social and governance factors and indicators listed in Annex Ia of this Regulation.

posed Regulation should make such a fundamental change to the IORP II Directive. Essential changes to the IORP II Directive should always be carried out by amending the Directive itself through the ordinary legislative procedure, because this is the only way which adequately involves the Council and Parliament.

Another argument to reject the proposed delegation of power to the EU Commission is that the coherence the delegated acts are supposed to achieve with the UCITS, AIFM and Solvency II Directives is neither reasonable nor necessary. IORPs are not to be treated as pure financial service providers (see Recital 32 IORP II Directive).

- We support the Council Position which does not introduce delegated acts into the IORPI II Directive, because it takes into account the objective of the Directive, which is EU minimum harmonisation.

The Council position refers to guidelines to be issued by EIOPA (Recital 13) “specifying how investment decisions and risks assessment by IORPs take into account environmental, social and governance risks under Directive (EU) 2016/2341“. We note that this is not reflected in any of the articles that follow.

As stressed above, the objective of the IORP II Directive is EU minimum harmonisation rather than full harmonisation. Consequently, EIOPA’s opinions and reports⁹ focusing on the transposition of the IORP II Directive are based on Art. 29 of the EIOPA Regulation ([EU 1094/2010](#)), which addresses “common supervisory culture“. We therefore do not understand that Recital 13 of the Council text refers to “guidelines“ which are based on Art. 16 of the EIOPA Regulation.

- The transposition of the IORP II Directive is supported by EIOPA through “opinions and reports“. We therefore do not understand why the Council text refers to “guidelines“ issued by EIOPA. Recital 13 should be deleted.
- If the objective is specifying “how investment decisions and risks assessment by IORPs take into account environmental, social and governance risks under Directive (EU) 2016/2341“, an amendment of Art. 19 IORP II Directive would be necessary to change the existing investment rules. This change then would have to be transposed by the Member States. EIOPA could support this process of transposition by publishing opinions and reports.

6. Amending the IORP II Directive

While neither the Commission, the ECON Committee nor the Council call for an amendment of the IORP II Directive, amendments were proposed by [Paul Tang](#) (S&D, NL) in his [Draft Report](#). As we have stated several times above, we agree that this would be an adequate way of changing the existing rules for IORPs. However, a key question in this regard is the timing: the period for transposing the Directive into national law only ended at the beginning of the year (13 January 2019); in Germany the changes to transpose the IORP II Directive came into force precisely on 13 January 2019.¹⁰ This means that it is now up to IORPs to adjust their operations to the new requirements. Changing the IORP II Directive at this point in time would mean that it would not be possible to gain any experience regarding the implementation and effectiveness of the new ESG rules.

The IORP II Directive itself includes the requirement for evaluation and review until 13 January 2023. The current disclosure proposals are not based on any actual experience with the new (ESG) rules. In line with the Better Regulation Agenda these new rules should first be evaluated before they are replaced / supplemented with additional rules.

⁹ [The Revised EIOPA Single Programming Document 2019-2021 with Annual Work Programme 2019](#)

¹⁰ Overview over the transposition process into German law on the [aba website](#) (in German).

- Generally, any changes for IORPs should be made by amending the IORP II Directive. If changes to the IORP II Directive are made, we call for an adequate period of time to gather experience before new rules are created. The IORP II Directive provides for 13 January 2023 as the deadline for an evaluation and review.

Conclusions

Currently the three Commission proposals regarding sustainable finance from May 2018 are going through the legislative process. At the time of writing, two of them were already being negotiated in the trilogue. There is immense political pressure to conclude these legislative acts before the elections to the European Parliament in May 2019. Despite the urgency to mitigate climate change, things shouldn't be rushed. Regarding IORPs, the implications for the members and beneficiaries should be considered. New ESG regulation for IORPs should build upon the rules introduced by the IORP II Directive and take into account the role of IORPs in the financial markets – as investors and buyers of products they are on the demand side of the market. This way it can be ensured that on the one hand ESG factors will feature more and more in risk management and investment decisions, while on the other hand over 10m members and beneficiaries in Germany and many more across the EU will benefit from reliable occupational pensions now and in the decades to come.

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