



February 19, 2019

**Via Online Submission:** [www.esma.europa.eu](http://www.esma.europa.eu)

European Securities and Markets Authority  
CS 60747  
103 rue de Grenelle  
75345 Paris Cedex 07, France

**Re: ESMA Consultation Papers on Integrating Sustainability Risks and Factors**

Dear Sir or Madam,

Managed Funds Association (“**MFA**”)<sup>1</sup> welcomes the opportunity to provide comments to the European Securities and Markets Authority (“**ESMA**”) on its consultation papers on integrating sustainability risks and factors in the UCITS Directive and AIFMD<sup>2</sup> (the “**UCITS/AIFMD Consultation**”)<sup>3</sup> and in MiFID II<sup>4</sup> (the “**MiFID II Consultation**”),<sup>5</sup> each dated 19 December 2018. MFA supports the aims of promoting sustainable finance within the European Union (“**EU**”), and of closing the investment gap required to meet European climate and energy targets. Environmental, social, and governance (“**ESG**”) factors are of increasing importance to many investors both in the EU and in the United States, and we welcome efforts to enable the asset management industry and the finance sector more generally to meet this increasing demand for sustainability – a demand driven approach that MFA strongly supports. However, MFA cautions against overly prescriptive measures that would obligate asset managers to incorporate ESG factors into investments even when underlying investors, such as pension funds, express a different set of priorities.

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<sup>1</sup> MFA represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry’s contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.

<sup>2</sup> Directive 2011/61/EU, available at: <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:174:0001:0073:EN:PDF>.

<sup>3</sup> Available at: [https://www.esma.europa.eu/sites/default/files/library/esma34-45-569\\_consultation\\_paper\\_on\\_integrating\\_sustainability\\_risks\\_and\\_factors\\_in\\_the\\_ucits\\_directive\\_and\\_aifmd.pdf](https://www.esma.europa.eu/sites/default/files/library/esma34-45-569_consultation_paper_on_integrating_sustainability_risks_and_factors_in_the_ucits_directive_and_aifmd.pdf).

<sup>4</sup> Directive 2014/65/EU, available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0065&from=EN>.

<sup>5</sup> Available at: [https://www.esma.europa.eu/sites/default/files/library/2018-esma35-43-1210-ipisc\\_cp\\_mifid\\_ii\\_sustainability.pdf](https://www.esma.europa.eu/sites/default/files/library/2018-esma35-43-1210-ipisc_cp_mifid_ii_sustainability.pdf).

## I. General Support of Consultation Goals

MFA supports the European Commission’s (the “**Commission**”) goal, as expressed in the draft Delegated Regulation,<sup>6</sup> of increasing transparency with respect to sustainability risks and sustainable investment opportunities to enable clients to better assess whether the investment products and services that they purchase meet their sustainability criteria, and should allow alternative investment fund managers to make a more informed assessment of whether their services are meeting client demand.

MFA also strongly supports ESMA’s decision to use a high-level principles-based approach to integrate sustainability risks into the UCITS, AIFMD, and MiFID II frameworks, where applicable.<sup>7</sup> We agree with ESMA that it is important “to avoid being inflexible or overly prescriptive on such a forward-looking topic, as the market has not yet reached maturity.”<sup>8</sup> Since the market for ESG investments is still growing and evolving, it is prudent to ensure that the requirements imposed under the UCITS, AIFMD, and MiFID II frameworks will accommodate the diverse needs and desires of clients.

## II. Concern with Blanket ESG Requirement

Consistent with these views, MFA believes that there should not be a blanket requirement in the delegated acts under UCITS, AIFMD, or MiFID II for all investment managers to incorporate “ESG preferences” or “ESG considerations” (each as defined in the draft Delegated Regulation) into investment strategies or securities trading in every case (*e.g.*, where the potential client has expressed no ESG preference). Rather, asset managers should engage in a discussion with their clients and potential clients regarding whether the manager’s products and services meet the client’s ESG factors and considerations so that the client can make an informed choice about whether to retain the asset manager. This approach will better ensure that asset managers incorporate ESG factors and considerations to the extent they form an investment objective or preference of the client.

With this in mind, MFA believes ESMA should avoid including broad wording in the proposed amendments that would require all investment managers to take into account “sustainability risks and factors” or “ESG preferences” as part of their UCITS, AIFMD, or MiFID II requirements. Rather, we support the more flexible approach that ESMA used in many places in the MiFID II Consultation, which is to require a firm to take into account a client’s ESG preferences “where relevant.” We believe that using identical language for all of ESMA’s proposed amendments under UCITS, AIFMD, and MiFID II would be an appropriate and reasonable solution. We believe this approach also is consistent with the approach taken by the Commission in its draft Delegated Regulation.

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<sup>6</sup> Commission proposed delegated Regulation amending Delegated Regulation (EU) 2017/565 as regards the integration of Environmental, Social and Governance (ESG) considerations and preferences into the investment advice and portfolio management (the “**draft Delegated Regulation**”), available at: [http://ec.europa.eu/finance/docs/level-2-measures/mifid-delegated-act-2018\\_en.pdf](http://ec.europa.eu/finance/docs/level-2-measures/mifid-delegated-act-2018_en.pdf).

<sup>7</sup> See UCITS/AIFMD Consultation at 6, paragraph 12; and MiFID II Consultation at 8, paragraph 4.

<sup>8</sup> UCITS/AIFMD Consultation at 5, paragraph 8; and MiFID II Consultation at 5, paragraph 8.

Such an approach would allow an investment manager to ask a client or potential client whether the client has any particular ESG preferences. If the client has such preferences, the manager can then determine whether any of its products or services meets the client's ESG preferences (or otherwise make adjustments to existing product offerings to take into account such ESG preferences) and provide such products or services to the client accordingly. However, if the client does not have such preferences, then it would permit the investment manager to continue to provide products or services to the client consistent with the client's non-ESG preferences.

### III. Support for Commission Draft ESG Disclosure Regime

MFA notes that the Commission's proposed amendments to MiFID II under the draft Delegated Regulation would *not* require firms to: (1) incorporate ESG considerations into the information they provide to clients or potential clients on investment services, or (2) disclose details of the types of financial instrument that may be included in the client portfolio based on the client's ESG preferences. While a prior draft of the delegated regulation did incorporate both such disclosure requirements, in more recent drafts, the Commission has chosen to eliminate them.<sup>9</sup> We support the disclosure approach in the current draft Delegated Regulation. It may be appropriate to disclose general information to a client or prospective client on the ESG profile of a financial instrument or investment strategy, but requiring firms to take into account the investment objectives and ESG preferences of a potential client when disclosing information about an investment strategy would be problematic in practice. In particular, firms would no longer be able to work from the same set of information for each potential client. Instead, firms would need to request that prospective clients disclose their investment objectives (and ESG preferences) in advance, and tailor any information provided to those objectives. Such a requirement could prove a high bar in practice, since it would require multiple tailored disclosure documents to be produced.

We agree with the draft Delegated Regulation approach because we think it makes sense to allow investment managers to provide a client or prospective client with general information on what the composition of a fund or portfolio managed by that investment manager might look like in practice. This type of disclosure would then lead to a more detailed discussion with the client around whether that investment strategy would meet the prospective client's investment objectives and ESG preferences.

It is also important to bear in mind that, while a client may have certain ESG preferences, it may view risk or overall financial performance as being the more important criteria for assessing whether the portfolio management service meets its needs. In other words, it is important for ESMA to ensure that the proposed amendments to the delegated regulations under UCITS, AIFMD, and MiFID II do not imply that ESG factors should be seen as automatically taking precedence over other investment objectives.

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<sup>9</sup> See prior Commission draft Delegated Regulation, available at: [https://eur-lex.europa.eu/legal-content/EN/TEXT/HTML/?uri=PI\\_COM:Ares\(2018\)2681500&from=EN](https://eur-lex.europa.eu/legal-content/EN/TEXT/HTML/?uri=PI_COM:Ares(2018)2681500&from=EN).

As MFA's members manage alternative investment funds, MFA wishes to make a comment on how ESG could be considered in the investment funds context.<sup>10</sup> In the context of an alternative investment fund, the fund's offering documents would clearly disclose to investors and potential investors the fund's investment objectives. On the basis of such disclosure, investors decide whether they wish to invest in the relevant fund. To the extent that the investment strategy of the relevant fund does not correspond to an investor's ESG preferences, the investor would simply choose not to invest in that fund (unless the investment manager and client contractually agree to come up with a bespoke approach that suits the ESG objectives of the investor). We note that we support many of the specific recommendations in this regard that are part of the responses submitted by the Alternative Investment Management Association ("**AIMA**") to the consultation papers.

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MFA would like to reiterate its thanks to ESMA for the opportunity to engage constructively on the ESG issues raised in the consultation papers. We would welcome the opportunity to discuss our views in greater detail. Please do not hesitate to contact the undersigned at +1 (202) 730-2600 with any questions that ESMA or its staff may have regarding this letter.

Respectfully submitted,

Michael N. Pedroni  
/s/ Michael Pedroni  
Executive Vice-President and Managing  
Director, International Affairs  
Managed Funds Association

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<sup>10</sup> Article 2(1)(i) of MiFID II.