Finance Watch response to the public consultation on the proposal for a regulation amending Regulation (EU) 2016/1011[1]

Brussels, 3rd August 2018

Finance Watch is an independent non-profit Members' association set up in 2011 to act as a public interest counterweight to the powerful financial lobby. Our mission is to strengthen the voice of society in the reform of financial regulation by conducting advocacy and presenting public interest arguments to lawmakers and citizens. Our Members are civil society organisations and expert individuals, supported by a full-time secretariat.

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We agree to the publication of this response.

Finance Watch is glad to provide the following contribution to the public consultation on the EC proposal for a regulation amending Regulation (EU) 2016/1011 aimed at defining low carbon benchmarks and positive carbon impact benchmarks.

- First and foremost, we consider that the proposed review of the Regulation (EU) 2016/1011 cannot support the transition to low carbon economy, because the indices are used only to measure the financial performance of an investment theme and not broader environmental goals. For this reason, we consider the contribution of this proposal to the objectives of the sustainable finance agenda to be highly questionable. Moreover, the current proposal fails to include any definition of ESG benchmark.

Notwithstanding this,

- With regard to the following article (23a) on low-carbon benchmarks:

"(23a) 'low-carbon benchmark' means a benchmark where the underlying assets, for the purposes of point 1(b)(ii) of this paragraph, are selected so that the resulting benchmark portfolio has less carbon emissions when compared to the assets that comprise a standard capital-weighted benchmark and which is constructed in accordance with the standards laid down in the delegated acts referred to in Article 19a(2);"

The wording in the article 23(a) is not more ambitious than index providers' current approach[2] and therefore simply confirms current industry practices.

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[1] REGULATION (EU) 2016/1011 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014

[2] https://www.msci.com/low-carbon-indexes
http://www.ftse.com/products/downloads/ftse-global-climate-index-series.pdf

Moreover, the wording in the article 23(a) should clarify what "less" means and what emissions are considered. At the very least the article should specify that the resulting benchmark portfolio should have significantly less carbon emissions when compared to a standard capital-weighted benchmark and that when calculating carbon emissions, it is critical to consider a life-cycle perspective. In any case whether an index has less carbon emissions than the parent index says nothing about constituents' alignment with Paris Agreement goals.

Finally, it is important to remember that many companies doing green activities (like reforestation) are not listed.

- With regard to article (23,b):

  "'positive carbon impact benchmark' means a benchmark where the underlying assets, for the purposes of point 1(b)(ii) of this paragraph, are selected on the basis that their carbon emissions savings exceed the asset's carbon footprint and which is constructed in accordance with the standards laid down in the delegated acts referred to in Article 19 a (2)".

  We would like to highlight that the legislator should consider the real life-cycle reductions in emissions and not the virtual emission savings.

- We are particularly concerned with the following definition of: *'emission saving'* included in the point (iv), of the paragraph (h) of the Article 1 of the Annex to the proposed Regulation:

  "emissions which would continue to exist if the company's products or services would be replaced by more carbon emitting substitutes ('emission savings')'.

  The estimation of emission saving implies the construction of the counterfactual scenario and this might be a major source of uncertainty, given that the counterfactual scenario might be modelled in such a way to show the highest possible virtual savings with the sole objective achieving a carbon impact ratio higher than 1. Moreover, the legislator should create as many as possible incentives for supporting the transition to the low carbon economy instead of asking companies to assess which products are more polluting. In this sense, the proposed definition is – in our view - fully inconsistent with the sustainable finance agenda objectives.

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https://www.euronext.com/en/indices/index-factsheets