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By email: markt-consultation-se@ec.europa.eu

Subject: Public Comment on the modernisation of the Directive 2004/109/EC (Transparency Directive) - Eurosif Response

Information about the respondent

Name of respondent organisation/company/natural person: **Eurosif (European Sustainable Investment Forum)**

Interest Representative Registration ID Number: **70659452143-78**

Contact person and function: **Matt Christensen, Executive Director**

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Field of activity of respondent (e.g. issuer of securities, investor, financial intermediary, financial analyst, national authority, other): **European Association**

Introduction

In the context of the ongoing global financial crisis, the Transparency Directive Modernisation (Directive 2004/109/EC¹) process offers an historic opportunity to improve legislation encouraging longer-term thinking in European financial markets. As outlined in the market study² (hereafter the External Study) carried out by Mazars and serving as a base for the Directive review process, the Transparency Directive is viewed by most financial industry stakeholders as useful for the proper functioning of the market. While the percentage of compliance with the Directive provisions appears high across Europe (as outlined in the External Study), there are a number of emerging issues raised by the stakeholders participating in the External study and which are submitted by the European Commission for review:

- Should the transparency rules laid out in the Directive be specifically adapted to smaller listed companies³ with a view of maintaining and also increasing the attractiveness of regulated markets for this category of issuers? i.e: removing the obligation to disclose quarterly information by listed companies.
- Should large (in particular institutional) investors disclose their voting policies in listed companies?
- Should the disclosure of non-financial information be integrated into the Transparency Directive Regime?
- The possibility of introducing mandatory Environmental, Social and Governance (ESG) data disclosure by listed companies.
- Should the minimum harmonisation character of the Transparency change into a maximum harmonisation one, due to the uneven transposition of the Directive by Member States.
- How "empty-voting"⁴ practices can be limited and the transparency in the stock-lending process increased.
- The need for greater convergence of the rules on disclosure of major holdings of voting rights and of financial instruments giving access to voting rights (including cash settled derivatives).
- The possibility of simplifying the overall reporting requirements for issuers.

¹ Directive 2004/109/EC http://ec.europa.eu/internal_market/securities/transparency/index_en.htm

² Mazars, an international independent audit organisation conducted an external study on the application of the Transparency Directive in behalf of the European Commission which stands at the base of the Directive's modernisation process.

³ The Fourth Company Directive states that "small" companies are companies which, on their balance sheet dates, do not exceed the limits of two of the following three criteria: balance sheet total: EUR 4 400 000; net turnover: EUR 8 800 000; number of employees: 50.

⁴ "Empty voting" is voting without the economic exposure usually attached to shares, such as voting with borrowed shares.

Eurosif (the European Sustainable Investment Forum) is a pan-European network and think-tank of national Sustainable Investment Forums whose mission is to **Develop Sustainability through European Financial Markets**⁵. Current member affiliates of Eurosif include pension funds, financial service providers, academic institutes, research associations and NGO's. The association is a not-for-profit entity that represents assets totalling over €1 trillion through its 80 affiliate members.

While agreeing to the relevance of the many issues raised by the European Commission in the Consultation Questionnaire for the modernisation of the Directive, Eurosif wishes to address those questions which are most consistent with its mission and expertise. **Eurosif believes that relevant, comparable and reliable transparency on material financial, environmental, social and corporate governance (ESG) issues are critical to an effective European financial market.** Therefore, Eurosif strongly advocates that ESG issues should be addressed with this specific Directive as it represents one of the more important legislative instruments to ensure a properly functioning European financial market.

Please find below Eurosif's perspective on the several of the questions in the Consultation Questionnaire as well as our general perspective on the Transparency Directive Modernisation.

Question 7.7: Could you provide a specific reply regarding the disclosure of environmental and social data requested in Article 46(1)(b) of the Fourth Company Law?

Although this question is listed in the Consultation Questionnaire⁶ under the chapter referring to small listed companies, it is important to clarify that Eurosif's position environmental, social and governance (ESG) data disclosure below refers both to small listed companies (explained in footnote n³) and large e corporations⁷

Eurosif proposes that mandatory disclosure of Environmental, Social and Governance (ESG) data by all listed companies should be included in the Transparency Directive.

Environmental, social and governance issues differ from one sector to the next – a pharmaceutical company does not face the same ESG challenges as a utility company for instance. While a detailed prescriptive “one size fits all” reporting approach would not work and would be overloading for companies, Eurosif believes that one **based on principles, flexible and simple enough to work for any listed and large companies, should become mandatory.**⁸

As this area has already attracted significant interest from various stakeholders, Eurosif suggests exploring a number of existing initiatives (Global Reporting Initiative, recent guidelines by the International Corporate Governance Network (ICGN)⁹, the current work of the Climate Disclosure Standards Board¹⁰, for instance) and use them to amend existing regulation.

Eurosif supports work done by the ICGN in 2009 which details principles under which ESG reporting should:

- Be genuinely informative and include forward-looking elements where this will enhance understanding;
- Be material, relevant and timely;

⁵ Please see Appendix for information on Eurosif and its activities.

⁶ The Consultation Questionnaire can be found at the following link:
http://ec.europa.eu/internal_market/securities/docs/transparency/directive/consultation_questions_en.pdf

⁷ The Fourth Company Law Directive defines a large company as a company with a headcount over 250, a net turnover over €35 million and a total balance sheet over €17.5 million.

⁸ A principles-based reporting approach provides a conceptual basis to follow instead of a list of detailed rules. Under a principles-based approach, one starts with laying out the key objectives of good reporting in the subject area and then provides guidance explaining the objective and relating it to some common examples.

⁹ ICGN Statement and Guidance on Non-financial Business Reporting www.icgn.org

¹⁰ The Climate Disclosure Standards Board is developing a global framework for corporate reporting on climate change, which is at a late stage of development (a draft will be launched publicly in May 2009). www.cdsb-global.org

- Describe the company's strategy, and associated risks and opportunities, and explain the board's role in assessing and overseeing strategy and the management of risks and opportunities;
- Be accessible and appropriately integrated with other information that enables investors to obtain a whole picture of the company;
- Use key performance indicators (KPIs) that are linked to strategy and facilitate comparisons;
- Use objective metrics where they apply and evidence-based estimates where they do not;
- Be strengthened where possible by independent assurance that is carried out having regard to established disclosure standards applicable to 'non-financial' business reporting, such as those issued by the IASB.

At the moment, ESG data disclosure is referred to only in the Fourth Company Law in which the Article 46(1)(b) of the Fourth Company Law states that:

"To the extent necessary for an understanding of the company's development, performance or position, the analysis shall include both financial and, where appropriate, non-financial key performance indicators relevant to the particular business, including information relating to environmental and employee matters;"

Nevertheless, at the current time, this requirement has not been readily enforced nor have companies disclosed substantive ESG information that could help investors. **Eurosif believes that European institutions should make reporting on ESG data no longer an option subject to interpretation but a requirement and the Transparency Directive is a good platform for this.**

It is increasingly understood that financial statements capture less than 20% of corporate risks and value creation potential, with the balance deriving from intangible factors such as human capital and resource efficiency. ESG data are relevant, material information that investors should have and increasingly want as a means to better gauge longer-term risks.

The availability of ESG data tracking the sustainability performance of companies could have a beneficial effect on corporate, investment and market performance. Should investors conclude that companies with thoughtful long-term management of ESG issues are better-run companies, a sort of virtuous circle could be created: in this scenario, investors would reward stock prices where sustainability is integrated, and companies would respond by further improving their sustainability performance. Accordingly, a fixation on meeting quarterly earnings estimates and other short-term measures would give way to longer-term thinking as a broader business agenda is recognised and rewarded by investors. The mandatory disclosure of ESG information by publicly listed and large companies could go a long way toward a sustainable economy.

Without such mandatory disclosure, investors will continue to lack the means of assessing substantial numbers of material factors as they arise. Incomplete data makes for inefficient markets and a lack of transparency leads to unstable financial systems. **Investors require reliable, comparable data on a broad range of potential risks.** A purely voluntary disclosure scheme does not guarantee significant, relevant and comparable data from all issuers: information is often provided selectively and very often, with the absence of common standards, the information cannot be compared with other companies, or over time. In addition, adopting a harmonised framework will ease the "questionnaire fatigue" companies sometimes complain about when they receive multiple and diverging information requests from ESG analysts. Finally, the availability of comparable ESG data from European companies will greatly assist the implementation and monitoring of all manner of relevant EU policies and target.

With regards to possible key performance indicators (KPIs), Eurosif believes that most KPIs would need to be sector-specific. A number of existing initiatives have produced interesting results in terms of KPIs (see the European Federation of Financial Analysts Societies (EFFAS)¹¹, the non-financial performance lab by the European Alliance for CSR and the sector additions of the GRI). In particular, EFFAS developed sector-specific KPIs for a limited number of industries, as well as a methodology for defining industry-specific KPIs that any third party can use. **Eurosif would like to see the Commission coordinate further collaboration among different stakeholders and initiatives** to reach a common ground. Eurosif will be happy to bring its expertise and that of its member affiliates into this type of collaboration.

¹¹ EFFAS "KPIs for ESG: A Guideline for the integration of ESG into financial analysis and corporate valuation"

Currently regulators and stock exchanges in numerous jurisdictions around the world – including France (loi NRE, article 116), Brazil, Malaysia, South Africa, Sweden and very recently Denmark – have mandated or encouraged the disclosure of such data.¹² In the United States, mandatory disclosure is currently being promoted by investors to the Obama administration. The EU would retain its leadership on sustainability issues by mandating disclosure of ESG data by publicly traded, large corporations.

Question 15: Which is the best way to make the investment process more transparent (please justify your answer):

- i) requesting investors to disclose their future intentions with holdings;
- ii) requesting investors to disclose their actual voting policies;**
- iii) both;
- iv) none;
- v) other.

Eurosif believes that that the first step in ensuring greater sustainability is for investors to disclose their actual voting policies.

Eurosif considers that the Transparency Directive should foster the development of Responsible Investment among institutional investors. Given the current context of the global financial crisis, Eurosif believes that Transparency Directive should encourage **the disclosure by investors on how they integrate environmental, social and governance issues in their investment policies.**

As discussed previously in the answer to Question 7.7 above, ESG issues do affect the performance of companies. There is a growing consensus in the financial community that **taking ESG issues into consideration is consistent with the fiduciary duty of investors when it impacts profitability**, and is further relevant when there is a consensus to do so by participants /members /stakeholders.¹³ **Ownership and power imply responsibility from investors and trustees.** ESG issues such as climate change, working conditions at suppliers' factories, misaligned executive compensation, corruption and human rights have material impacts on stock values and investment portfolio performance.

Similar transparency regulations have already been adopted in the United Kingdom (2000), France (2001), Germany (2001), Sweden (2001), Belgium (2004), Norway (2004), Austria (2005) and Italy (2004) and were recommended in the 2009 OECD reviewed Guidelines for pension fund governance¹⁴.

This response has been developed as a part of Eurosif's aims to encourage disclosure, transparency and responsible ownership, and to promote the integration of social, environmental and governance issues into financial services. It does not necessarily reflect the views of all of its Member Affiliates.

Yours sincerely,
Matt Christensen
Executive Director, Eurosif (European Sustainable Investment Forum)

A handwritten signature in black ink that reads "Matt Christensen".

¹² For detailed references to case studies, see "Innovations in Social and Environmental Disclosure Outside the United States" by Domini Social Investments http://www.domini.com/common/pdf/Innovations_in_Disclosure.pdf

¹³ UNEP FI, Freshfields, Bruckhaus, Deringer : a legal framework for the integration of environmental, social and governance issues into institutional investment, October 2005.

¹⁴ The 2009 OECD Guidelines for Pension Fund governance can be found here: <http://www.oecd.org/dataoecd/18/52/34799965.pdf>

APPENDIX

About Eurosif

EUROSIF, the European Sustainable Investment Forum, is the pan-European network whose mission is to develop sustainability through European financial markets. Eurosif works as a partnership of the national Sustainable Investment Forums (SIFs) within the EU and with the support and involvement of Member Affiliates. Recognised as the premier European forum for sustainable investment, Eurosif's Member Affiliates are drawn from leading pension funds, asset managers, NGO's, trade unions, academic institutes and research providers, together representing assets totalling over €1 trillion. Eurosif's work includes a focus across asset classes - equity and fixed income markets, microfinance, renewable energy, property, private equity and hedge funds - all centred around the industry trends and future legislation affecting this space. The key benefits that Eurosif affiliate members receive include EU interfacing, SRI information and European wide initiatives that integrate Environmental, Social and Governance (ESG) issues into the financial services sector.

For the full list of Eurosif Member Affiliates, please see www.eurosif.org

Eurosif has two main roles: (1) to provide an international forum that allows members and member affiliates to work together on issues pertaining to Sustainable & Responsible Investment (SRI, see below for definition of SRI and its market size in Europe) and Corporate Governance in the EU financial services sector, and (2) to collect input from members and member affiliates and then communicate their ideas and initiatives to European policy makers, including the European Commission as well as the European Parliament. Therefore, this note is mainly driven from and by the interest and expertise of our membership.

Sustainable and Responsible Investment Definition

Eurosif continues to use the term "SRI" as the most readily acknowledged expression for this field and defines SRI as follows:

SRI, a generic term covering ethical investments, responsible investments, sustainable investments, and any other **investment process that combines investors' financial objectives with their concerns about environmental, social and governance (ESG) issues.**

To do so, different approaches exist:

- Best-In-Class approach: Selection of the best companies in their sector with regard to sustainable development.
- Thematic approach: Selection of the best companies according to a specific sustainable development theme (renewable energies, water, job creation, etc.).
- Norms-Based approach: Selection of companies according to their observance of the main international treaties/conventions (e.g. ILO).
- Exclusion approach: Exclusion of companies involved in controversial activities or issues (alcohol, gambling, animal testing, etc.).
- Engagement: this includes proxy voting, collaborative engagement, direct private dialogue with companies, and public engagement. Engagement is often considered as an extra overlay to other SRI approaches or traditional management.
- Microfinance approach: financing Microfinance institutions (bonds or equity) favoring economic empowerment.

Market Size

In its latest European SRI Study 2008, Eurosif published the latest Sustainable and Responsible Investment (SRI) figures and trends. The 2010 edition of the SRI Study will be published on October 13, 2010. This unique study will highlight the scale of European SRI as well as European and National trends across eighteen countries. Based on a survey of asset managers and self-managed asset owners, Eurosif assessed the total European SRI assets under management (AuMs) to be €2.7 trillion as of December 31, 2007 and represent as much as 17.5% of the asset management industry in Europe.