afme/ Finance for Europe

ISDA Safe, Efficient Markets

Consultation response

EBA Consultation on Draft Implementing Standards on prudential disclosures on ESG risks in accordance with Article 449a CRR.

1 June 2021

The Association for Financial Markets in Europe (AFME) and the International Swaps and Derivatives Association (ISDA) welcome the opportunity to respond to the EBA's consultation on draft ITS on the prudential disclosure of ESG risks.

About AFME

AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors, and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society. AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia. AFME is listed on the EU Register of Interest Representatives, registration number 65110063986-76. Information about AFME and its activities is available on the Association's website: www.afme.eu.

About ISDA

Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 950 member institutions from 76 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter, LinkedIn, Facebook and YouTube.

Overarching and general comments

AFME and ISDA's members are supportive of the development of a Pillar 3 framework for the disclosure of ESG risks to allow investors and stakeholders to compare the sustainability performance of banks and their business activities. We agree in principle that this should support institutions in the public disclosure of meaningful and comparable information on ESG related risks and vulnerabilities, including transition and physical risks. In addition, the framework should support banks in providing transparency on how they are mitigating these risks, including information on how they are supporting their customers and counterparties in the process of adapting to climate change risk and in the transition towards a more sustainable economy.

This needs to be considered, however, in the context of a regulatory landscape for ESG disclosures which is inherently complex and which is far from complete at a global level. The levels of granularity of the ESG disclosures proposed in Europe at this stage is therefore surprising, and banks' ability to provide such levels of detail will depend heavily upon information being available from counterparties, companies being able to disclose emissions using common methodologies, and industry capacity to collect this data in the timescales envisaged.

Banks rely on Companies' disclosures to produce their own disclosures. The issue is that the first reporting by corporates under CSRD is expected by 2024, one year after the first Pillar 3 report by banks. For listed SMEs, the first reporting under CSRD is due by 2027. <u>For the type of information to be provided by corporates on a mandatory basis under CSRD (such as the physical risks, sub code NACE, scope 1-2-3, split of revenues by carbon intensive sectors … for instance), the application timeline of the Pillar 3 requirements should be aligned with the CSRD application timeline.</u>

In addition, <u>we would note that the reporting and disclosure of very detailed information in Europe before global standards are developed is likely to lead to fragmentation across large banking groups and potential disadvantages for European corporates</u>. There would also be distortions in markets and competition in jurisdictions outside the EU, where EU banks will need to request information from clients that other credit institutions located in the same jurisdiction, and which are not as advanced as those from the EU, will not. Accordingly, we do not consider mandatory public disclosures should be required for non-EU counterparts where there are not equivalent standards in force in the relevant jurisdiction. The BCBS is going to publish soon a consultation on the ESG Risk Management Framework at international level. In that context, we recommend EBA not to require a too granular Pillar 3 reporting, but to define it in a progressive way in order to be able to take into account international developments, and not to require banks to change in 2-3 years the whole Pillar 3 disclosure.

We recognise and appreciate the EBA's intention to apply the NACE framework for consistency and the practical suggestions concerning the use of proxies and estimates while the disclosure framework becomes more established. However, an excessive granularity would introduce additional complexity with higher operational risks in the calculation of banks' exposures and metrics, exacerbate the operational challenge related to the absence of mirroring information from corporate clients but also preempt the nature and granularity of information that corporates will be required to disclose under the forthcoming Corporate Sustainability Reporting Directive (CSRD). Also, it will be very important that a realistic timetable is provided in relation to the use of proxies where relevant for non-EU exposures given the significant challenges that are envisaged in obtaining data. We would note in addition that disclosures based mainly on proxies may have little comparability and therefore very limited usability for stakeholders as there is no common or standard methodology to deal with the lack of information from non-financial corporate clients in the initial years. There is a separate concern that the presentation of potentially misleading information due to a significant reliance on proxies could expose banks to legal risk and challenge. Over time, it should be appreciated also that as more precise information becomes available this could lead to the emergence of different situations being presented and of diverging assessments of levels of climate change risk. In order to avoid proxies as much as possible, we recommend first the alignment of the Pillar 3 disclosure requirements to the scope of the CSRD, and secondly to allow a one-year gap between the disclosure by corporates under CSRD and the disclosure for banks. We would even recommend allowing banks to rely on the most recent data that they are able to collect. For example, it will not be possible for banks' pillar 3 report published in the first quarter of a given year to rely on data published by corporates in the fourth quarter of the year before. Indeed, certain corporates close their books in the first half of the year while others do in the second half of the year.

At a more operational level, the benefits of requiring semi-annual disclosure are not clear, particularly when considered in the light of the annual requirement only provided for corporate disclosures, and it appears possible that banks may be expected to undertake three Pillar 3 reports over the course of a 12 month period.

We would recommend therefore that policymakers adjust the CRR Article 449a Level 1 text in this area to require an annual disclosure only. In this respect we would also note the current 'disconnect' between the reporting requirements under Article 8 of the Taxonomy Regulation and the forthcoming Pillar 3 regulatory disclosures on ESG risks, specifically where information under the Taxonomy will be required to be reported on an annual basis, including by respective counterparties in scope of NFRD, whilst the Pillar 3 disclosures will need to be produced bi-annually meaning that most of such bi-annual disclosures are likely to be produced based on estimates (in the absence of update information from counterparties).

In terms of timing, we welcome the clarification the EBA has provided that the publication of banks' first Pillar 3 report will be due in Q1 2023 based on banks' data collected ending December 2022. It is important to note though that banks will face great challenges if they are required to collect data from companies closing their books in the second half of the year. Additionally, we would welcome clarity in relation to the interaction of the reporting requirements under the Taxonomy Regulation and the forthcoming Pillar 3 regulatory disclosures on ESG risks, specifically where information under the Taxonomy will be required to be reported on an annual basis, including by respective counterparties in scope of NFRD, whilst the Pillar 3 disclosures will need to be produced bi-annually meaning that most of such bi-annual disclosures are likely to be produced based on estimates (in the absence of update information from counterparties).

The third pillar of the Basel regulation was initially intended to foster market discipline through public disclosures about banks' capital structure, capital adequacy, and risk management. The Pillar 3 disclosures were built over time in order to reach an adequate level of data reliability, consistency and comparability across Banks, and indeed significantly improved the ability of financial markets participants to assess banks' risks management processes, capital structure, risk exposures and capital adequacy.

We also acknowledge the need to consider reporting on how ESG factors impact market risk, but this must be implemented through pertinent and useful indicators both for clients and investors, and for banks' risk management purposes. Indeed, the Taxonomy aligned KPIs are not suitable for ESG Risk purposes, as they do not embed any risk criteria. Being 'environmentally sustainable' may mean less transition risk but cannot obviously go with less credit, market, operational or liquidity risks. Also, several neutral activities excluded from the taxonomy may not necessarily be vulnerable to any transition risks. (and in any case it will be subject to separate legislation through the Delegated Act).

We further note that uncertainty also exists with regards to the revision of the Trading book boundary expected later this year as part of the CRR3 proposal from the European Commission. This will significantly impact the scope of positions to be included across various KPIs. Thus we recommend a phased approach where the inclusion of the Trading book for Pillar 3 disclosure will be incorporated at a later stage.

The inclusion of quantitative information about ESG risk factors and their impacts on common risks categories into the Pillar 3 disclosure is premature. As of today, the conceptual and the regulatory frameworks, and the associated methodologies to set a systematic, robust and quantitative link between ESG risk factors and credit risk does not exist. Consequently, templates should not mix up ESG non-financial data and risk parameters, the link with risk parameters (PD/Performing/non-performing/ Stage 2/ Accumulated impairment, accumulated negative changes in fair value due to credit risk and provisions) does not seem to be justified and we find it is premature to publicly disclose this information. We believe it should be disclosed under supervisory reporting only, and if needed.

We understand that EBA wants to overcome, in the Pillar 3 report, the fact that no 'Harmful taxonomy" has been defined in the European regulation so far. This requirement goes beyond Pillar 3 purpose and Art.449a of the CRR2 mandate. In addition, we struggle to understand the definitions proposed by EBA; the link with the Low Carbon Benchmark Regulation introduces a complexity and requires information that we are not sure can be obtained from our members' customers. This excessive granularity paves the way for misinterpretation, all the more that the cross articulation between the lines granularity and the columns

granularity is not clear at all. We believe this type of reporting is premature. We propose to wait for the definition of the 'Harmful Taxonomy' and the CSRD implementation.

We would also like to highlight also that robust methodologies on physical risks or scope 3 are not finalized yet and need to be harmonized in order to ensure comparability among banks. We propose that, for the time being, physical risk should be reported only in a qualitative manner. Regarding scope 3, we propose to postpone its inclusion in the Pillar 3 till the finalization of common agreed methodologies and till CSRD implementation.

Clarification is needed also on the detail and rationale for the information requested on some templates and we would note a duplication of requirements across some of the templates. To improve clarity, the instructions could where relevant include references or links to data points from other reporting and disclosure templates, for example from the COREP and FINREP frameworks. We would also question the value to the market of recording splits between government and non-government exposures.

There is scope for explicit clarification also on the extent to which templates cover EU and non-EU exposures. For instance, Template 3 refers to the energy efficiency of loan collateral, based on the EPC label. This label was introduced in Europe through the Energy Performance of Buildings Directive and there should not therefore be an expectation that non-EU countries have EPC labels. In this sense it is necessary to clarify whether the request to 'disclose separately those exposures for which there is no EPC information of the collateral' refers also to exposures in non-EU countries.

Our more detailed observations on specific templates and tables are set out in the sections below.

In summary, we recommend a building block approach, a high data quality Pillar 3 framework and a gradual adaptation of the level of granularity with the gradual implementation of the CSRD until the end of the phase-in period and the development of international standards.

Quantitative disclosure templates

Template 1: Banking Book – Quality of exposures by sector

- The template requires banks to disclose information on exposures to carbon intensive sectors, including probabilities of default. It is not clear how this information might be interpreted by stakeholders and we note the ECB's recent thinking in relation to the risks surrounding changes in perceived credit risk owing to climate change[1].

  In particular, the decline in the creditworthiness of certain firms and sectors could incentivise banks to adjust the composition of their portfolios, shifting their investments towards less risky groups of firms. Those changes in bank exposures could trigger second-round effects on the real economy, for example through investment demand.
- The interaction between the rows and columns is not entirely clear, for instance sectors are presented in rows, while 'carbon intensive sectors' are required also in the columns to the table.
- We note that exposures are reported by sector but that columns I to K then require a breakdown of companies excluded which introduces a risk of confusion.
- As mentioned, we consider the public disclosure of possible links with credit risk parameters, including probability of default and performing/ non-performing status, to be premature for the time being. In the meantime, the connection between 'green' and 'less risky' is still under consideration,

[1] Shining a light on climate risks: the ECB's economy-wide climate stress test
Post by Luis de Guindos, Vice-President of the ECB, 18 March 2021.

with an EBA assessment scheduled for 2025. We would therefore propose that in the meantime, the EBA avoids making these connections in the ITS and removes these disclosure requirements from the templates.

- Additional clarity is needed also around the disclosure of Stage 2 non-performing exposures as such exposures would usually be classified Stage 3.
- In terms of columns y and z, we would note that significantly different methodologies might be applied to the calculation of GHG emissions which may be misleading. We would note also that scope 3 emissions are difficult to compare across reporting entities.
- The inclusion of SMEs in the template pre-empts NFRD revisions and significantly increases the operational complexity of obtaining the necessary information. In due course, the inclusion of SMEs should be limited to those subject to the CSRD and those that disclose the green asset ratio on a voluntary basis. We would note in addition that there will not be a mandatory requirement for corporates to provide information on non-green assets that would be necessary for the completion of this template.
- In terms of non-EU counterparties, in many jurisdictions there are no binding disclosure standards and banks will therefore have to request information from clients or use proxies, which will place them at a disadvantage.
- That is why we propose to disclose for the 2023 and 2024 reports, which apply before the implementation of the CSRD, a simplified template 1 with the gross carrying amounts by NACE code at the sectoral level only and per geography.

<u>Template 4: Climate change transition risk – Alignment metrics for the banking book</u>

- We would note that carbon intensity is not provided for some sectors, which is covered by some methodologies but not for all sectors. The ability to provide this information will depend on how methodologies evolve, and whether these methodologies will be able to cover all sectors and segments and it is not possible to foresee how this will evolve over the next three years. The use of the proxy through company turnover could lead to volatility in the metric.
- The majority of our members would propose that Template 4 remains flexible: for the rows, banks should be allowed to fill report on the sectors and code NACE sectors on which it has performed the analysis of the alignment of its credit portfolio on a 2 degrees scenario; for the columns, banks should be allowed to disclose the alignment metrics they have defined in their methodologies. EBA should not be prescriptive in terms of sectors and KPIs. We consider Template 4 of the consultation as an example but not as a mandatory common template.

- Finally, it would be useful to have more information on the type of information expected with regard to the distance to IEA scenario. Also, if the IAE scenario seems to be relevant namely in terms of governance of the scenario and regular update, it is not clear to us which 2 degree scenario the template refers to (i.e. whether the SDS scenario or not). It would be necessary to give more clarity on the scenario that should be the basis for the reporting during a certain period (three years for instance). This will avoid volatility in banks' disclosure not resulting from exposure changes.

- Now, we note that the taxonomy as well as the CSRD proposal are referring to a 1.5 degree scenario. We therefore recommend as much consistency as possible in the proposed scenarios amongst the different legislations.

Template 5: Exposures in the banking book to top carbon-intensive firms

- We observe that the EBA intends to require disclosure of carbon-intensive firms on a 'named' basis and that this may raise legal and reputational questions as to the publication of customer specific information. We would be more supportive, therefore, of the possibility the EBA mentions of the ability to disclose data on an **aggregate only basis**, provided that one single official list of polluting companies should be provided by EBA or EU authorities.
- In addition, we would note that Template 5 aims to show institutions' exposures towards the top carbon-intensive companies. The EBA has suggested that there is evidence that top polluting companies would be more exposed to any policy action to reduce companies' emissions which could jeopardise their creditworthiness, and make them more exposed to reputational risks. If this disclosure materialised, the information released to the market (on a 'named' basis) could speed up some of the risks the EBA points out in its Consultation Paper (reputational risk for instance).
- There are further reasons why the currently proposed Template 5 would not achieve the goal of reducing the asymmetry of information to the market:
    - As the list of top polluting companies would mainly include corporate (and possibly some of largest corporates worldwide), global banks/larger banks would be those providing them funding and hence reporting under this Template 5. The release of this Template could result in a distorted vision of the risks faced by the banking industry. For instance, smaller banks would likely not fill in this template, as their exposures (mainly SMEs) would be out of the scope of the Top-emitting lists; this could wrongly be understood as them being 'less exposed' to polluting companies.
    - Since the data sources used by the institutions to identify the top carbon-emitting companies could differ among banks (each bank could use any source of publicly available information), the information disclosed would not be comparable.

Template 6: Trading book portfolio:

- We would like to understand more fully the objective of the requirement to disclose trading book activities. The value it would provide to the market and wider stakeholders is not clear and the complexity of the subject matter and data could bear burdensome implementation challenges and may lead to incorrect interpretations and conclusions.
- As noted further above, we acknowledge the need to report on ESG factors impacting market risk, but this must be implemented with useful indicators for both clients and investors, and for banks' risk management. Given the very early stages for inclusion of quantitative information about ESG risks as well as the inconsistent associated methodologies for the calculation of KPIs, more time is needed to establish relevant trading book disclosures related to climate risks, based on a robust conceptual framework that appropriately reflects the quantitative link between climate risk factors and market risk. Indeed, the three proposed indicators within the template 6 of the consultation, namely (i) gross exposures by sector, (ii) the sum of absolute purchases and sales by sector, with the respective proportion of alignment with the Taxonomy Regulation, and (iii) gains and losses by sector, do not provide relevant information on *climate risk impact* on the market risk of the trading book.

- Moreover, fair-value information on "brown" exposures in template 6, namely (i) companies excluded from EU Paris-aligned Benchmarks, in each sector, and (ii) carbon-intensive sectors, would only render disclosures more complex, without any robust value-added to clients and investors, as they do not convey any clear market risk information. They pre-empt the future "brown taxonomy" and would create additional unwarranted instability in disclosures, further hindering their usefulness.
- We wish to remind the EBA that the Trading book boundary definition is expected to be revised as part of the CRR3 publication (expected later this year) and the impact has yet to be fully understood,
- We recommend a more gradual approach is needed for reflecting on trading portfolio reporting. This would allow the industry to first concentrate on the implementation of the most relevant indicators, i.e. on the banking book, and built upon this already very challenging experience, to define adequate trading book indicators that appropriately reflect market risk, and are pertinent and useful to clients and investors.
- In addition, to ensure consistency between all credit institutions' trading portfolio disclosures under Article 8 of the Taxonomy Regulation, we believe that the trading portfolio of all institutions, irrespective its size, should be taken into consideration to the extent trading book activities are reported. Otherwise, disclosures would not be comparable among entities (with a trading book above and under certain threshold) and may lead to incorrect interpretations and conclusions by stakeholders and market participants.
- Notwithstanding the above, we would furthermore re-iterate our recommendation of an International approach where global standards are developed to help alleviate fragmented outcomes across jurisdictions.

Template 7 – Banking book exposures subject to physical risk

- In addition to noting the granularity of the template, the interpretation of the information disclosed will be difficult without more standardised measurements and instructions.
- The requirements of this template may create a dependency for banks on external data providers which will not have the same types and levels of data or risk coverage. It is likely to be necessary that these third parties will therefore need to apply broad and differing proxies in their methodologies. This would undermine the consistency and meaningfulness of information disclosed.
- We would also appreciate clarification regarding how to treat exposures that are prone to impact from both chronic and acute climate change events in order to avoid double counting of acute and chronic events.
- In addition, it should be avoided to disclose in the same template information related to historical PD and stages regarding future physical risks. Establishing this relationship would be misleading. In case the EBA needs this information for developing studies about the connection of being green and less risky, our members could provide it on a bilateral way, via reporting.
- We propose that physical risk should be reported on a **qualitative manner only.**

Template 8 and 9– Assets for the calculation of the Green Asset Ratio (GAR)

- Please refer to the **AFME/ISDA comments to the European Commission's proposal for a delegated act specifying disclosure requirements under the EU Taxonomy for entities in the scope of EU**

NFRD for our full position in respect of the calculation of the Green Asset Ratio (i.e. information required to be disclosed under Template 8 and 9).

- In respect of derivatives, the EBA's advice[2] to the European Commission on Disclosures under Article 8 Taxonomy Regulation issued on 1 March 2021 suggests that derivatives should be left out of the GAR calculation for credit institutions in the absence of disclosures or methodologies to assess their taxonomy alignment. Conversely, the draft delegated Regulation for NFRD-entity reporting under Art. 8 of Taxonomy-Regulation published on 7 May 2021[3] is understood to propose the exclusion of derivatives from the numerator of the GAR for credit institutions but their inclusion in its denominator.
- Derivatives perform a critical role in economic activity by facilitating the raising and allocation of capital for green finance, enabling, and helping businesses and investors better manage the risks to which they are exposed, and to more effectively align their exposures with risk tolerance and risk management requirements. The derivatives market also plays a major role in enhancing transparency through providing information on the underlying commodities, securities or assets, which can ultimately contribute to long-term sustainability objectives. The financial sector is responding to the challenges in sustainable finance with a diverse range of product structures and transaction types in the derivatives market. While conventional derivatives can certainly be used to hedge non-ESG related risks associated with green instruments, including credit, FX and interest rate risks, a new wave of sustainability-linked derivatives and exchange-traded ESG derivatives has also developed in recent years, alongside existing derivatives such as emissions trading derivatives, renewable energy and renewable fuels derivatives, and catastrophe and weather derivatives. The exponential grown of ESG markets inevitably implies a need for forward prices of these assets and their related indices. Hence, derivatives markets are a key component of mature secondary markets and it will therefore be increasingly necessary over time that ESG and ESG-linked derivatives are accounted for in the relevant sustainability KPIs.
- In line with previous industry response to the ESA's Joint Consultation Paper concerning Taxonomy-related sustainability disclosures[4] and in view of the Securities and Markets Stakeholder Group (SMSG) advice[5] to the same Consultation Paper, we strongly believe that derivatives can serve many purposes, including ESG purposes and in such contexts, the relevant KPIs measuring alignment with sustainability purposes should gradually be extended to include such derivatives, provided that it is adequately disclosed how they serve ESG purposes.
- However, given the low volume of derivative transactions that currently attain ESG characteristics or objectives and the absence of clear methodologies to assess their sustainability alignment, we recommend that such derivatives be included in the calculation of the GAR's numerator at a later stage following a more in-depth assessment of their current uses by EU policymakers and regulators.
- With regard to the Trading Book KPI proposed, we seek clarity with regard to the materiality of the value added by the proposed KPI at this stage and would recommend that its usefulness be assessed in the future once further work by the regulators has been achieved (please refer to **AFME/ISDA comments of the European Commission's proposal for a delegated act specifying disclosure requirements under the EU Taxonomy for entities in the scope of EU NFRD** for our full position. Furthermore, if the trading book were to be required as part of the GAR then to ensure the consistency between all credit institutions' GAR calculation, we consider that the trading portfolio of all

[2] https://www.eba.europa.eu/sites/default/documents/files/document_library/About%20Us/Missions%20and%20tasks/Call%20for%20Advice/2021/CfA%20on%20KPIs%20and%20methodology%20for%20disclosures%20under%20Article%208%20of%20the%20Taxonomy%20Regulation/963616/Report%20-%20Advice%20to%20COM_Disclosure%20Article%208%20Taxonomy.pdf

[3] https://ec.europa.eu/info/law/better-regulation/

[4] https://www.isda.org/a/XYzTE/ISDA-Responds-to-ESAs-on-Taxonomy-related-Sustainability-Disclosures.pdf

[5] https://www.esma.europa.eu/sites/default/files/library/esma22-106-3375_smsg_advice_on_taxonomy_related_sustainability_disclosures.pdf

institutions, irrespective the size of their trading book, should be taken into consideration for the computation of the GAR. Otherwise, GAR would not be comparable among entities (with a trading book above and under a certain threshold) and may lead to incorrect interpretations and conclusions by stakeholders and market participants (this principle also applies to the trading book more generally as is referred to above under Template 6).

- Additionally, we believe that the inconsistent treatment of including derivatives in the denominator while they are excluded in whole or in part from the numerator for credit institutions is not optimal from a methodological consistency standpoint and could potentially prove problematic for banks who provide liquidity in derivatives having structurally poor GARs. This inconsistent treatment also applies to the trading book in the denominator while being excluded from the numerator in the EC's draft delegated Regulation for NFRD-entity reporting under Art. 8 of the Taxonomy-Regulation. This in turn would make EU GSIBs less attractive issuers and counterparties for GAR-sensitive investors, and accordingly undermine their capital and funding costs at the very same time as the EU is relying on those same banks to build its CMU and to provide financing for the transition to a sustainable economy. We would thus like to call on the European Commission to reassess its approach for derivatives holistically in the GAR until this matter has been appropriately examined in more detail as indicators should not be constructed in an inconsistent way that structurally dis-favour banks. Finally, we suggest this approach, as highlighted above, to be applied consistently across all relevant calculation KPIs in respect of NFRD entity reporting under Article 8 of the Taxonomy Regulation as differing interpretations could create investor confusion, result in fragmented outcomes and minimise the potential for evolution of risk management practices in the ESG space going forward.

Qualitative disclosures

Tables 1,2 and 3

- The extent to which disclosures will align with the new Corporate Sustainability Reporting Directive ('CSRD') is not clear, which raises potential risks around the consistency of information provided and its interpretation.
- It would be useful to have more detailed and therefore standardised instructions in relation to the sections on social and governance aspects.
- Definitions of 'short-term', 'medium-term', and 'long-term' would be useful as an additional item to paragraph 68 of the text set out in the consultation paper.
- Clarification would be welcome also on disclosure requirements in relation to transmission channels, for example are banks expected to provide information concerning service providers or similar operational relationships.
- In terms of Table 1, Qualitative environmental risk- *row 3 Current investment activities and (future) investment targets in sustainable economy and EU Taxonomy-aligned activities:* We believe that the definition/interpretation of "sustainable economy" is the same as "EU Taxonomy-aligned activities". If they are different, how is "sustainable economy" defined, or is this something which would be defined by the disclosing entities.
- Row 16 of Table 1 requests a: *Description of limits to environmental risks (as drivers of prudential risks) that are set, and triggering escalation and exclusion in the case of breaching these limits:* We would note that short of hard exclusions set by environmental/ sensitive sector policies, risk limits are not commonly codified in terms of specific risk limits. Environmental and social risks are frequently assessed on a client and a transaction level and must be considered on a case by case basis. As such

the current requirement is unlikely to produce clear, understandable and comparable disclosures between financial institutions.

- We would note the same issue in relation to risk limits for Row 12 of Table 2, Qualitative social risk: *Description of setting limits to social risk and cases to trigger escalation and exclusion in the case of breaching these limits.*
- More widely in relation to Table 2, it is not clear how the requirement for engagement with customers on their strategy to mitigate/reduce socially harmful activities might work in practice. For instance, challenges are likely to arise in seeking to ensure that customers are representative of the social risks which firms are seeking to manage – e.g. an EU27 customer might not be representative of particular social risks such as unemployment, that is prevalent from transactions in different countries.
- Other consideration for Table 2 relate to the lack of clarity as to where and by whom labour standards and human rights are defined and set and there is likely to be further work needed on the alignment of social risk with remuneration policy.
- In terms of Table 3, Qualitative governance risk: Some of the main issues that we would like to raise concern (a) fragmentation risks given the granular nature of these disclosures in the absence of internationally agreed standards approved by NGFS (ii) the potential for the duplication and fragmentation with existing and prospective corporate reporting requirements under the ECB Guide to Climate and Environmental related risks, the proposals for amendments to the EU Non-Financial Reporting Directive and TCFD/national corporate reporting obligations (iii) the complication of bank group governance structures by requiring different governance models for EU subsidiaries for banks incorporated outside of the EU (iv) poor and/or absent definitions of environmental and social risks will make implementation of the requirements problematic and (v) the lack of ESG data in certain fields, including concerns with the verification/completeness of such data and legal/regulatory liability this may give rise to.
- We would recommend that the Qualitative information templates **be replaced by the TCFD report**. As TCFD standards are recognized at international level, they ensure comparability and level playing field among banks.

We would welcome the opportunity to discuss the points made in our response with the EBA further, if this would be helpful.

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