Background Note to the Public Consultation on the Legislative Proposals by the European Commission on the Financing of Sustainable Growth

Introduction

In 2015, Malta committed to the Sustainable Development Goals (SDGs) and the Paris Agreement – promising to end extreme poverty, address corrosive inequality, boost peace and prosperity, and stop climate change. In this regard, the SDGs provide a framing to the action needed in developing and scaling investments, technology, and the policy needed to achieve major transitions in energy, water, agriculture, and consumption; and in supporting the actions needed to adapt to higher temperatures, higher sea levels, disrupted weather patterns and extreme weather events. In this context, Government is consulting with the general public with regards to a set of legislative proposals focused on sustainable finance launched by the European Commission.

Background

On 7 March 2018, the European Commission released an Action Plan for Financing Sustainable Growth. The plan is a response to recommendations from the High-Level Expert Group (HLEG) on Sustainable Finance, which were submitted to the Commission on 31 January 2018. The legislative proposals emanating from the Action Plan were adopted by the Commission and published on 24 May 2018. The Commission also issued a number of information documents on the package which can be accessed online.

The Action Plan for Financing Sustainable Growth outlines ten reforms in three areas:

A. Reorient capital flows towards sustainable investment, in order to achieve sustainable and inclusive growth
   1. Establishing an EU classification system for sustainability activities
   2. Creating standards and labels for green financial products
   3. Fostering investment in sustainable projects
   4. Incorporating sustainability when providing investment advice
   5. Developing sustainability benchmarks

B. Manage financial risks stemming from climate change, resource depletion, environmental degradation and social issues
   6. Better integrating sustainability in ratings and research
   7. Clarifying institutional investors and asset managers' duties
   8. Incorporating sustainability in prudential requirements

C. Foster transparency and long-termism in financial and economic activity
    9. Strengthening sustainability disclosure and accounting rule-making
    10. Fostering sustainable corporate governance and attenuating short-termism in capital markets

At publication date of the Action Plan (8 March), the Commission legislative proposals were still to be impact assessed. Therefore it is worth highlighting that since the legislative proposals of 24 May have then been assessed, the actual proposal might be different than the idea put forward in the Action Plan. The Annex to this Background Note refers to the key points as presented in the Commission Action Plan.

Measures emanating from the Action Plan took form of a legislative proposal, a level 2 measure, or a non-legislative measures. This Public Consultations seeks your feedback on the legislative proposals as adopted by the Commission on 24 May. The actual package consists of three proposed regulations and two delegated acts amending directives.

European Commission's Legislative Proposals on Sustainable Finance

More specifically;

1. **Proposal for a Regulation on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016/2341**

The Commission proposal on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016/2341 aims to increase transparency on the integration of sustainability risks and on the pursuance of sustainable investments. This regulation will introduce disclosure obligations on how institutional investors and asset managers integrate environmental, social and governance (ESG) factors in their risk processes. Requirements to integrate ESG factors in investment decision-making processes, as part of their duties towards investors and beneficiaries, will be further specified through delegated acts.

2. **Proposal for a Regulation amending Regulation (EU) 2016/1011 on low carbon benchmarks and positive carbon impact benchmarks**

The Commission proposal for amending Regulation (EU) 2016/1011 on low carbon benchmarks and positive carbon impact benchmarks aims to address the risk of 'greenwashing', whereby all low carbon indices are being equally promoted as environmentally relevant, by putting forward an amendment to the already in place Benchmark Regulation. The proposed amendment will create a new category of benchmarks comprising low-carbon and positive carbon impact benchmarks, which will provide investors with better information on the carbon footprint of their investments.

3. **Proposal for a Regulation on the establishment of a framework to facilitate sustainable investment**

The Commission proposal for a regulation on the establishment of a framework to facilitate sustainable investment launches a gradual process for the establishing of the conditions and the framework to gradually create a unified EU classification system (taxonomy) which will be the basis for establishing a definition of sustainable investment and criteria for an environmentally sustainable economic activity. According to the proposed legislation, the uniform criteria for determining environmentally sustainable economic activities will be developed and operationalised through subsequent delegated acts, which will define the technical screening criteria. Those delegated acts will be duly impact assessed.

4. **Commission Delegated Regulation amending Regulation (EU) 2017/565 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive**

The Commission Delegated Regulation amending Regulation (EU) 2017/565 supplementing Directive 2014/65/EU, the MiFID II Directive, aims to include ESG considerations into the advice that investment firms offer to individual clients. Through the delegated act it is being proposed that investment firms consider environmentally sustainable investments, social investments or good governance investments when offering advice to their clients. The delegated regulation provides for a definition for these three different investment terms.

5. **Commission Delegated Regulation amending Delegated Regulation (EU) 2017/2359 with regard to environmental, social and governance preferences in the distribution of insurance-based investment products**

A Commission Delegated Regulation amending Delegated Regulation (EU) 2017/2359, the Insurance Distribution Directive (IDD), with regards to ensuring that sustainability preferences related to ESG factors are taken into account in the suitability assessments undertaken in the distribution of insurance-based investment products. The delegated regulation seeks to clarify that insurance intermediaries and insurance undertakings are obliged to conduct, as part of the suitability assessment, an assessment of sustainable preferences of their customers both in the selection process and the questionnaire to collect customers' information. In addition, insurance intermediaries and insurance undertakings have to include information on the ESG preferences in the sustainability statement explaining how the recommendation meets the customer's objectives, risk profile, capacity for loss and ESG preferences (ex-post information).

Consultation Questions

Q1. What impact would you expect to see in Malta's financial sector when implementing the proposed Commission regulations?

Q2. What changes would you expect to see in your day to day business when implementing the proposed Commission regulations?

Q3. From a consumer perspective, are clients interested in ESG factors in their investment decisions? If yes, what specific factors are usually particulalry interested in? If on the contrary, what are the main bottlenecks hindering investors from opting for investments which factor in ESG principles?

Q4. Can you outline opportunities/threats associated with the legislative proposals? Specific drafting suggestions are appreciated.

Maria Mifsud
Economics Analyst
Economic Policy Department

t +356 25998610 **e** maria.j.mifsud@gov.mt | www.finance.gov.mt
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