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EBF KEY POINTS on selected aspects of the EBA Pillar 3 questionnaire

As the questionnaire of the EBA is mainly addressed to banks to map and understand the current disclosure and classification practices, the EBF encouraged its member banks to provide directly response to the questionnaire. We therefore provide views only on some aspects that are being addressed in the questionnaire in relation to future disclosure obligations under Article 8 and Pillar 3.

We will be continuing discussions on key aspects such as classification of exposures, KPIs, tracking of financed emissions etc in the coming months. We will be also releasing a joint report with the UNEP FI resulting from case studies testing the application of the EU Taxonomy on banks' products which will provide further recommendations on operationalizing of the taxonomy in the banking sector. We would be keen to continue the dialogue with the EBA on disclosures, to ensure disclosures devised both under Article 8 and Pillar 3 provide the most relevant, reliable and user-friendly information to the market, reflecting their purpose.

1) Interaction of Pillar 3 disclosures with other ESG disclosures of institutions and with other policy initiatives in the EU

Ensuring harmonized and consistent requirements across EU legislation and regulation is key. Increased complexity will negatively impact effectivity as well as usability of the tools developed by the EU. While reporting requirements under Pillar 3, Article 6, SFDR and NFRD) should be complementary and as consistent as possible, it has to be kept in mind that they have a different objectives and different users of information (investors and depositors, stakeholders, shareholders, supervisors... The EBA in cooperation with the ESAs is best placed to ensure alignment between the different pieces of regulation, and that the core transparency data to be collected can be aligned with the other reporting requirements, as well as ensuring that information is useful from risk perspective.

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Banks' own reporting will be substantially dependant on the availability of data and willingness of the companies outside of the NFRD scope to deliver data. Financial institutions should not be required to report sustainability-related information on their portfolios/activities, if sufficient and reliable information is not available.

Ideally, companies should be required to report only once to a central data register, material information based on common standards. These data should be structured in such a way that will allow multiple usage (SFDR, Pillar 3, Article 8, supervisory requirements). It is therefore advisable that all reporting requirements are based on double materiality, common definitions and metrics.

Given the current lack of data, lack of methodologies and to avoid subjectivity and comparability, a simple set of metrics and mandatory disclosures that all industries have to use and report on would help achieve a better outcome in the short term and could be built on over time as understanding improves—with the caveat that financial and non-financial undertakings will have a different set of metrics to disclose. **The starting point for disclosures should be simple common metrics and KPIs related to:**

- (i) GHG emissions (for banks estimated financed emissions)
- (ii) disclosure of material information enabling the assessment of physical risk, transition risk or other specific categories of ESG risk,
- (iii) the management of environmental and social related risks and opportunities.

2) Pillar 3, implementation of disclosure requirements included in Article 449a CRR, green and brown ratio

We do agree that more exposure of counterparties to transition risk means also more transition risk for the bank - implying that a bank that assist its customers in the transition is also lowering its own transition risk. However, the same logic cannot be applied for improving a green asset ratio. It could simply mean that bank is financing more activities that are taxonomy compliant.

It is crucial that markets understand the different ratios, their objectives, scope and limitations.

A green ratio provides a snapshot of the volume of taxonomy compliant activities at a given time and could show progress over time as ratios in different periods are being compared. It does however not help to fully understand the extent the institution contributes to the transition or to the achieving of climate neutrality objectives (for the time being focusing only on climate).

It is also not seen as risk indicator. While green activities as such may have a low transition risk, physical risk will depend on the geographical location. It also does

not capture proactive risk management efforts or transitioning strategies at entity level. It will also fall short of capturing exposures with undefined use of proceeds. Increase in green ratio could mean that banks are financing more taxonomy compliant activities or more data become available enabling the assessment but overall risk may remain the same.

Finally, as climate factors are considered as a driver of other risk, green activities may or may not have overall reduced financial risk which will have to be assessed per asset class.

The Brown ratio could be a potential indicator of increased financial risk but again will not provide the whole picture if not capturing how risk is being mitigated at entity level. Any brown classification should not hinder the transition of entire sectors and their access to finance. Finance is essential for those sectors to be able to undertake the necessary transition and any brown classification should not result in establishing penalizing factors relating to the financing of such transitioning activities. Information including transitioning would provide better picture both for risk management as well on bank's contribution to climate objectives. The definition of transition (beyond what is captured in the taxonomy at activity level) should however be clarified as currently the understanding may differ. A common set of KPIs would have to be developed to avoid potential greenwashing.

We would propose differentiating between Taxonomy compliant asset ratio and another ratio that will have to be defined and capture efforts of banks and companies in the overall transitions.

The taxonomy compliant ratio can however be only applied to limited part of balance sheet so the limited information value needs to be well understood by the market. The EU Taxonomy is not well suited for general purpose loans that represent a substantial part of banks' balance sheet (see the forthcoming EBF – UNEP FI project). In addition, corporate data availability is an issue in particular when applied to SMEs and non-EU based assets and unless assumptions can be used, evaluation of the do no significant harm at activity level is also challenging and at times impossible to assess for non-EU activities.

To increase the availability of the data, we are proposing corporates self-assessment of compliance with thresholds and metrics of the EU Taxonomy and development of a simplified reporting for SMEs as well as use of assumptions for DNSH evaluation for EU based activities.

In addition, the use of NACE classification for economic sectors brings an additional complexity and challenge in particular for banks that use International Standard Industrial Classification for their internal classification of activities at entity level rather than NACE at activity level and will require mapping between NACE and ISIC¹ and national classification systems. Some codes in NACE will still also have to be developed.

A solution to capture general lending should be discussed, in particular whether part of the exposure equivalent to the percentage of the activities of the entity that are considered taxonomy compliant could be recorded as taxonomy compliant and reflected in the ratio.

The 'green asset ratio' proposed by Article 8 should in our view be a proportion of the volume of Eligible Financial Assets (EFA) that are EU taxonomy-aligned /on Total Eligible Financial Assets, with EFA defined as all asset classes for which the EU taxonomy is **relevant and can be applied**. This would result in the following banking products included in the scope of the EFA, taking further into account the data availability (**initial focus on EU counterparties within the scope of the NFRD) and distinguishing between existing and new exposures:**

- Corporate loans and/or project finance facilities with specified use of proceeds aligned with EU taxonomy
- General purpose loans to companies undertaking taxonomy compliant activities
- Performance bonds to support a taxonomy aligned activities
- Financial guarantees to support the payment obligations arising from financing a taxonomy-aligned activity

Assets with limited relevance for the purposes of Article 8 such as reserves in central banks, trading books, hedging derivatives, sovereigns, general purpose lending (loans without use of proceeds) unless for companies with taxonomy compliant activities, etc. should not be included in the ratio.

For further details, please see our position on Article 8

https://www.ebf.eu/wp-content/uploads/2020/09/EBF_042309-EBF-Feedback-on-Art-8-IIA-.pdf

A positive contribution to other environmental objectives and social impact or governance related information should also be captured at least at qualitative level pending the developments of the taxonomy and methodologies.

Pillar 3 reporting should focus on information that is useful to understand where potential financial losses could materialize, either within the bank or for the financial system as well as information on how this risk is being mitigated. The information should remain understandable, material and comparable. Inclusion of forward looking information in terms of targets and level of progress is key.

3) Availability of relevant and meaningful information

The EU Commission should build or support, based on existing solutions and infrastructures already in place, an EU infrastructure that could collect periodically, with the help of new reading technologies, existing climate change mitigation and

adaptation data of companies that published non-financial statements under the NFRD and other available relevant information, ESG metrics and relevant data points.

Ensuring availability of high quality and comparable ESG data should be regarded as an EU strategic infrastructure project to meet the EU sustainability objectives both under the Action Plan on Sustainable Finance and the EU Green Deal". We are convinced that centralized data register would substantially improve the data availability and thus fasten the achievement of the objectives.

With regards to the database, we would like to call for a dialogue to start as soon as possible on key elements of the database, the data collection process, KPIs and templates with participation of financial industry from both investment and lending side, corporates, ESAs and the Commission. While we welcome the recognition of the need for ESG database, we are concerned that the several initiatives may lead to some fragmentation or multiple reporting obligations for corporates. The ESAP (Action 1 CMU Action Plan), by which the EC will adopt a legislative proposal in Q3 2021 plans to set up a European single access point. This platform shall provide seamless, EU-wide access to all relevant information (including financial and sustainability-related information) disclosed to the public by companies, including financial companies. The platform should contribute to meeting the objectives of the European Green Deal. The platform will build on the EFTG pilot project and be complementary to the business registers interconnection system (BRIS) – key to avoid reporting burden for companies. The common European Green Deal dataspace is envisage to support the Green Deal priorities is being envisaged in the [EU data strategy & EU Green Deal](#) - The "GreenData4All" initiative, which (following an evaluation/impact assessment) will aim to review and possibly revise two pieces of existing legislation: Access to Environmental Information Directive (2003/4/EC) & INSPIRE Directive (2007/2/EC).

These projects cannot be separate, and cannot be only investor-focused, as all relevant data reported by corporates needs to be useful and usable for other purposes, including lending and risk management.

Data relevant for Pillar 3 disclosure should be part of the centralized and harmonized data collection and that the data reported to or collected by the central ESG data register are fit for multi-purpose use, complemented by the data from existing public databases that should be connected to the central ESG data register.