PRI Principles for Responsible Investment

SUSTAINABLE FINANCE IN EMERGING MARKETS AND THE ROLE OF SECURITIES REGULATORS

PRI RESPONSE TO THE GROWTH AND EMERGING MARKETS COMMITTEE (GEMC) OF THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS (IOSCO)

INTRODUCTION

The United Nations-backed Principles for Responsible Investment (PRI) is the world's leading initiative on responsible investment. The PRI works to understand the investment implications of environmental, social and governance (ESG) factors and to support its international network of investor signatories in incorporating these factors into their investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

Launched in 2006, today the PRI has over 2200 signatories (pension funds, insurers, investment managers and service providers) globally with approximately US $82 trillion in assets under management. The PRI has two official UN partners – UN Environment Programme Finance Initiative and UN Global Compact.

The PRI has experience of public policy on ESG integration and responsible investment across multiple markets and are available to further support the work of IOSCO on promoting sustainable finance.

Any questions or comments can be sent to policy@unpri.org .

ABOUT THE CONSULTATION

The Growth and Emerging Markets Committee (GEMC) of the International Organization of Securities Commissions (IOSCO) has published this Consultation Report with the aim of proposing a set of recommendations to assist growth and emerging markets (GEM) regulators in their efforts with regard to sustainable finance. The GEMC welcomes stakeholder views on its findings and recommendations. A final report, including recommendations to securities regulators, will be prepared after consideration of comments received in response to this Consultation Report.

PRI'S RESPONSE TO THE CONSULTATION REPORT

The PRI welcomes the GEMC consultation report: Sustainable finance in emerging markets and the role of securities regulators. The recommendations in the report will support securities regulators in emerging markets in promoting the development of responsible investment practices. In particular, we welcome:

- The consideration of a wider regulatory framework to promote sustainable finance and ESG integration, including market infrastructure, reporting and disclosure requirements, governance, strategy, risk management and role of institutional investors.
- The alignment of the consultation report's recommendations with IOSCO's Principles and Methodology.
- The statement that incorporating ESG factors into the business is becoming integral to a company's long-term viability (recommendation 1).
- The disclosure requirement on ESG risks and opportunities by issuers and CIS in alignment with traditional financial disclosures (recommendation 2).
- The inclusion of a recommendation that institutional investors should incorporate ESG-specific issues into their investment decision-making as part of their fiduciary duties (recommendation 10).

The PRI's priority recommendations are:

- To clarify that material ESG factors are a core component of long-term corporate value creation.
- To recommend that issuers and CIS are required to disclose all material factors that impact corporate performance, including ESG factors, in their traditional mandatory disclosure documents, including how they are integrated in their strategy, risk management and operations, and how they are likely to impact future performance.
- To recommend that securities regulators introduce mandatory ESG disclosures, aligned with international standards and existing best practice, including explicit reference to TCFD implementation and reporting.
- To support existing efforts to standardise ESG disclosure at an international level and align such disclosure with Sustainable Development Goals (SDG) reporting.

RESPONSE TO QUESTIONS OUTLINED IN THE CONSULTATION REPORT

Questions relating to Recommendation 1

Do you agree that it is important to include a general recommendation regarding the need for issuers and other regulated entities to integrate ESG-specific issues in the overall risk appetite and governance?

The PRI agrees with this statement. Recent PRI research on corporate ESG reporting[1] pointed to the consensus that boards must understand a company's enterprise-wide risks, which include ESG factors. By embedding knowledge and responsibility of sustainability factors into their core duties, directors can effectively manage the mainstreaming of ESG factors into business strategy, organisation culture and operational practices in a way that supports the long-term profitability and viability of the company.

Do you have specific comments on the proposed Recommendation 1?

We recommend rewording recommendation 1 as follows: "Issuers and other regulated entities should systematically integrate ESG factors, along with all long-term value drivers, in the overall risk management and governance of these entities, and disclose how they do so."

We recommend adding the following at the beginning of the supporting text, to ensure ESG issues are not regarded as a separate category but are clearly understood as related to corporate performance: "ESG factors impact corporate performance and should therefore be integrated in corporate strategy, risk management, operations and performance assessment."

We also recommend adding the following: "The Board should issue a public statement on how it is considering ESG factors. Board commitment to reporting provides credibility for corporate sustainability commitments and performance. It indicates that ESG risks and opportunities that may impact corporate performance are considered alongside all value drivers in corporate strategy and management."

We also recommend changing the wording of the third paragraph of the supporting text to reflect the fact that ESG factors should be integrated in traditional governance and risk management processes.

Questions relating to ESG-specific disclosures and reporting, and data quality (Recommendations 2 and 3)

Do you have specific comments on the proposed recommendation for ESG-specific disclosures and reporting?

[1] See https://d8g8t13e9vf2o.cloudfront.net/Uploads/h/u/x/esgreportingdiscussionpaper_996785.pdf

We recommend that mandatory disclosure is required in recommendation 2. Evidence demonstrates that mandatory disclosure regulations are more impactful than voluntary guidelines.

We also recommend adding the following text to recommendation 2 to ensure that issuers disclose how they identified the material ESG information they are reporting: "Issuers should clearly articulate their materiality analysis and the choice of ESG factors as part of corporate disclosure requirements."

In the related supporting text, we recommend adding the following text: "Disclosure should include information on the issuer's analysis of ESG factors, the stakeholders involved in the process, and the link between ESG factors, corporate performance and the overall corporate strategy."

The PRI also recommends explicit reference to TCFD implementation and reporting:

- Clarifying that climate change is a material risk factor and integrating the TCFD recommendations through IOSCO corporate governance and reporting guidance and standards.
- Join the Central Banks and Supervisors Network for Greening the Financial System (NGFS) for peer-to-peer learning and to support the global coordination of approaches by financial market regulators towards climate change.

Do you agree that a separate recommendation on data quality is needed? Do you have specific comments on the proposed recommendation?

We believe this separate recommendations is essential.

We recommend adding in the supporting text: "Evidence demonstrates that mandatory reporting requirements are associated with improved corporate ESG scores. ESG disclosure requirements, for example, should be strengthened by systematically integrating them into listing rules."

We also recommend adding: "Regulators should support and contribute to efforts in creating standardised and comparable ESG disclosure framework and indicators, such as those led through the Corporate Reporting Dialogue."

Questions relating to sustainable instruments (Recommendations 4 to 9)

Do you agree that this set of recommendations should be applicable to all sustainable instruments, and not only debt instruments?

Our overall recommendation regarding recommendations 4 to 9 is that regulators need to cooperate on the establishment of comparable and standardized sustainability taxonomies to qualify sustainable instruments, project eligibility, offering documents and disclosure requirements, funding and external reviews.

On recommendation 4, we believe all instruments should be included.

Do you have specific comments on the proposed recommendation relating to the definition and taxonomy of sustainable instruments?

We recommend further referencing the EU Technical Expert Group and its work to create a unified classification system (or taxonomy) on environmentally sustainable economic activities. We see this as a first and essential enabling step in the overall effort to channel investments into sustainable activities.

Do you agree with how eligible projects have been framed in recommendation 5?

We welcome the inclusion of the 'do no harm' principle in this recommendation. We recommend emphasising the importance of aligning projects and activities with the goals of the Paris agreement and the Sustainable Development Goals.

Do you agree that it is useful to have separate recommendations for offering document requirements and for ongoing disclosure requirements, respectively? Do you have specific comments with regard to these recommendations?

Do you agree that regulators should provide for measures to prevent, detect and sanction misuse of funds raised through the issuance of sustainable instruments?

Do you agree with the recommendation relating to external reviews? Do you think that such external reviews should be mandatory or voluntary?

We agree with these recommendations (the above three questions). We recommend that any such specific requirements are integrated as much as possible in existing securities regulations, to avoid creating a dichotomy between traditional and sustainable projects and investments. Ad-hoc requirements should be introduced when the specificity of the disclosure or fund use regarding for example a green or social bond clearly requires doing so.

Questions relating to institutional investors (Recommendation 10)

Do you agree that it is important to have a specific recommendation with regard to institutional investors?

The PRI welcomes this recommendation. PRI research shows that pension fund regulation on ESG integration and stewardship codes are correlated to better corporate ESG risk management. This clearly supports the necessary alignment of ESG regulations on issuers and investors.

This recommendation is also aligned with ongoing work on ESG guidelines at IOPS, confirming that the explicit integration of ESG factors in investment and risk management processes is in line with fiduciary duties.

Do you agree that regulators should consider asking institutional investors to incorporate ESG-specific issues into their investment analysis, strategies and overall governance?

Yes. In addition to the points raised above, the PRI's international experience shows that investment guidelines and codes that are embedded in the legal framework are more impactful than those that are voluntary.[2]

Do you agree that regulators should ask the institutional investors to take into account ESG disclosures of the entities in which they invest?

Yes. To promote an effective use of material ESG data and disclosures provided by companies, regulators should require that investors systematically and explicitly integrate such data and disclosures in investment analysis and decision making. We recommend adding the words 'systematically and explicitly' in the text of recommendation 10.

As noted in the country analysis preceding the recommendations in the consultation report, many emerging markets have taken steps to clarify investor duties on ESG integration and provided guidance on how investors should integrate ESG factors. We therefore suggest deleting the second sentence from the supporting text following recommendation 10.

Questions relating to capacity building (Recommendation 11)

Do you agree that it is important to have a specific recommendation relating to capacity building?

Yes. Increasing the understanding and awareness of sustainable finance issues among regulators and market participants is a key step in developing sustainable finance markets, as is monitoring the implementation of the report recommendations.

We recommend replacing in the supporting text following recommendation 11 the phrase 'ESG investment' with 'ESG integration'.

Do you also agree that this recommendation should apply both to regulators and market participants?

Yes. Ensuring uptake from both groups is essential to the broader success of implementing the recommendations above.

[2] See https://www.unpri.org/policy-and-regulation/global-guide-to-responsible-investment-regulation/207.article