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**NOTE**

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| From: | General Secretariat of the Council |
| To: | Permanent Representatives Committee (Part 2) |
| No. Cion doc.: | COM (2018) 355 final |
| Subject: | Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2016/1011 on low carbon benchmarks and positive carbon impact benchmarks<br>- Presidency compromise text |

Delegations will find attached the Presidency compromise text on the above proposal.

Changes in red correspond to modifications made to the text in light of the Working Party of 12 December.

2018/0180 (COD)

Proposal for a

**REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**

**amending Regulation (EU) 2016/1011 on low carbon benchmarks and positive carbon impact benchmarks**

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Central Bank[1],

Having regard to the opinion of the European Economic and Social Committee[2],

Acting in accordance with the ordinary legislative procedure,

Whereas:

(1) On 25 September 2015, the UN General Assembly adopted a new global sustainable development framework: the 2030 Agenda for Sustainable Development[3], having at its core the Sustainable Development Goals (SDGs). The Commission's Communication of 2016 on the next steps for a sustainable European future[4] links the SDGs to the Union policy framework to ensure that all Union actions and policy initiatives, within the Union and globally, take the SDGs on board at the outset. The European Council conclusions of 20 June 2017[5] confirmed the commitment of the Union and the Member States to the implementation of the 2030 Agenda in a full, coherent, comprehensive, integrated and effective manner and in close cooperation with partners and other stakeholders.

(2) In 2015, the Union concluded the Paris Climate Agreement[6]. Article 2(c) of that Agreement sets the objective to strengthen the response to climate change, among other means by making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.

1 OJ C […], […], p. […].

2 OJ C , , p. .

3 Transforming our World: The 2030 Agenda for Sustainable Development (UN 2015).

4 COM(2016) 739 final.

5 CO EUR 17, CONCL. 5.

6 OJ L 282, 19.10.2016, p. 4.

(3) Sustainability and the transition to a low carbon and climate resilient, more resource- efficient and circular economy are key in ensuring long-term competitiveness of the Union economy. Sustainability has long been at the heart of the Union project and the Union Treaties give recognition to its social and environmental dimensions.

(4) In March 2018, the Commission published its Action Plan 'Financing Sustainable Growth'[7], setting up an ambitious and comprehensive strategy on sustainable finance. One of the objectives of that Action Plan is to reorient capital flows towards sustainable investment to achieve sustainable and inclusive growth.

(5) Decision No. 1386/2013/EU of the European Parliament and of the Council[8] called for an increase in private sector funding for environmental and climate-related expenditure, notably through putting in place incentives and methodologies that stimulate companies to measure the environmental costs of their business and profits derived from using environmental service.

(6) Achieving SDG objectives in the Union requires the channelling of capital flows towards sustainable investments. It is important to exploit fully the potential of the internal market for the achievement of those goals. In that context, it is crucial to remove obstacles to the efficient movement of capital into sustainable investments in the internal market and to prevent such expected obstacles from emerging.

(7) Regulation (EU) 2016/1011 of the European Parliament and of the Council[9] establishes uniform rules for benchmarks in the Union and caters for different types of benchmark. An increasing number of investors pursue low carbon investment strategies and take recourse to low carbon benchmarks to reference or measure the performance of investment portfolios.

(8) A wide variety of indices is currently grouped together as low carbon indices. Those low carbon indices are used as benchmarks for investment portfolios and products that are sold across borders. The quality and integrity of low carbon benchmarks affect the effective functioning of the internal market in a wide variety of individual and collective investment portfolios. Many low carbon indices used as performance measures for investment portfolios, in particular for segregated investment accounts and collective investment schemes, are provided in one Member State but used by portfolio and asset managers in other Member States. In addition, portfolio and asset managers often hedge their carbon exposure risks by using benchmarks produced in other Member States.

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7 COM(2018) 97 final.

8 Decision No. 1386/2013/EU of the European Parliament and of the Council of 20 November 2013 on a General Union Environment Action Programme to 2020 ‘Living well, within the limits of our planet’ (OJ L 354, 28.12.2013, p. 171).

9 Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014 (OJ L 171, 29.6.2016, p. 1).

(9) Different categories of low carbon indices with various degrees of ambition have emerged in the marketplace. While some benchmarks aim to lower the carbon footprint of a standard investment portfolio, others aim to select only components that contribute to attaining the 2°C degree objective set out in the Paris Climate Agreement. Despite differences in objectives and strategies, all of these benchmarks are commonly promoted as low carbon benchmarks.

(10) Divergent approaches to benchmark methodologies result in fragmentation of the internal market because users of benchmarks do not have clarity on whether a particular low carbon index is a benchmark aligned to the 2C° objective or merely a benchmark that aims to lower the carbon footprint of a standard investment portfolio. To address potentially illegitimate claims by administrators about the low carbon nature of their benchmarks, Member States are likely to adopt different rules to avoid the ensuing investors' confusion and ambiguity about the aims and level of ambition underpinning different categories of so called low carbon indices used as benchmarks for a low carbon investment portfolio.

(11) In the absence of a harmonised framework to ensure the accuracy and integrity of the main categories of low carbon benchmarks used in individual or collective investment portfolios, it is likely that differences in Member States' approaches will create obstacles to the smooth functioning of the internal market.

(12) Therefore, to maintain the proper functioning of the internal market, to further improve the conditions of its functioning, and to ensure a high level of consumer and investor protection, it is appropriate to adapt Regulation (EU) 2016/1011 to ~~lay~~ introduce ~~down~~ a regulatory framework ~~for harmonised~~ laying down minimum requirements for low carbon benchmarks at Union level.

(13) It is furthermore necessary to introduce a clear distinction between low carbon and positive carbon impact benchmarks. While the underlying assets in a low carbon benchmark should be selected with the aim of reducing carbon emissions of the index portfolio when compared to the parent index, a positive carbon impact ~~index~~ benchmark should only comprise components whose emissions savings exceed their carbon emissions.

(14) In order to ensure that the denominations 'low carbon benchmark' and 'positive carbon impact benchmark' are reliable and easily recognisable for investors across the Union, only administrators that comply with the requirements laid down in this Regulation should be eligible to use the denominations when marketing these benchmarks in the Union.

(15) Where administrators of benchmarks do not wish to use the denomination 'low carbon benchmark' or 'positive carbon impact benchmark' then this Regulation does not apply. The regulation should only apply to benchmarks using the denomination 'low carbon benchmark' or 'positive carbon impact benchmark'.

(14~~6~~) Each company whose assets are selected as underlying in a positive impact benchmark should save more carbon emissions than it produces, hence have a positive impact on the environment. The asset and portfolio managers who claim to pursue an investment strategy compatible with the Paris Climate Agreement should therefore use positive carbon impact benchmarks.

(1~~5~~7) A variety of benchmark administrators claim that their benchmarks pursue environmental, social and governance ('ESG') objectives. The users of those benchmarks do however not always have the necessary information on the extent to which the methodology of those benchmark administrators takes into account those ESG objectives. The existing information is also often scattered and does not allow for effective comparison for investment purposes across borders. To enable market players to make well-informed choices, benchmark administrators should be required to disclose how their methodology takes into account the ESG factors for each benchmark or family of benchmarks that is promoted as pursuing ESG objectives. That information should also be disclosed in the benchmark statement. The administrators of benchmarks that do not promote or take into account the ESG objectives, should not be subject to this disclosure obligation. The Commission may review the scope of this requirement and whether it should be extended to cover all benchmarks in the light of future market, technological and regulatory developments. Within that review it should also be assessed whether an introduction of longer-term solutions into the BMR is needed, to help deal with future situations where the orderly wind down of a critical benchmark may be required.

(1~~6~~8) For the same reasons, administrators of low carbon and of positive carbon impact benchmarks should equally publish their methodology used for their calculation. That information should describe how the underlying assets were selected and weighted and which assets were excluded and for what reason. The benchmark administrators should also specify how the low carbon benchmarks differ from the underlying parent index, notably in terms of the applicable weights, market capitalisation and financial performance of the underlying assets. To assess how the benchmark contributes to the environmental objectives, the benchmark administrator should disclose how the carbon footprint and carbon savings of the underlying assets were measured, their respective values, including the total carbon footprint of the benchmark, and the type and source of the data used. To enable asset managers to choose the most appropriate benchmark for their investment strategy, benchmark administrators should explain the rationale behind the parameters of their methodology and explain how the benchmark contributes to the environmental objectives, including its impact on climate-change mitigation. The published information should also include details on the frequency of reviews and the procedure followed.

(17) In addition, administrators of positive carbon impact benchmarks should disclose the positive carbon impact of each underlying asset included in those benchmarks, specifying the method used to determine whether the emission savings exceed the investment asset's carbon footprint.

(18) To ensure continued adherence to the selected climate-change mitigation objective, administrators of low carbon and positive carbon impact benchmarks should regularly review their methodologies and inform users of the applicable procedures for any material change. When introducing a material change, benchmark administrators should disclose the reasons for that change and explain how the change is consistent with the benchmarks' initial objectives.

(19) In order to enhance transparency and ensure an adequate level of harmonization, the power to adopt acts in accordance with Article 290 of the Treaty on the Functioning of the European Union should be delegated to the Commission to specify further the minimum content of the disclosure obligations that benchmark administrators that take into account the ESG objectives should be subject to, and to specify the minimum standards for harmonization of the methodology of low carbon and positive carbon impact benchmarks, including the method for the calculation of carbon emissions and carbon savings associated with the underlying assets, taking into account the Product and Organisation Environmental Footprint methods as defined in points (a) and (b) of point 2 of Commission Recommendation 2013/179/EU[10]. It is of particular importance that the Commission carr~~y~~ies out appropriate consultations during its preparatory work, including at expert level, and that those consultations be conducted in accordance with the principles laid down in the Interinstitutional Agreement on Better Law-Making of 13 April 2016. In particular, to ensure equal participation in the preparation of delegated acts, the European Parliament and the Council receive all documents at the same time as Member States' experts, and their experts systematically have access to meetings of Commission expert groups dealing with the preparation of delegated acts, and be transmitted with the minutes of all meetings of the Commission technical expert group on sustainable finance.

(20) Article 51(1) of Regulation (EU) 2016/1011 introduced a transitional period whereby an index provider providing a benchmark on 30 June 2016 shall apply for authorisation by 1 January 2020. The discontinuation of a critical benchmark can impact market integrity, financial stability, consumers, the real economy or the financing of households and businesses in Member States. The discontinuation of a critical benchmark by an administrator could affect the validity of financial contracts or financial instruments. The discontinuation of such a critical benchmark could cause disruption to both investors and consumers, with potentially severe repercussions on financial stability. In addition, should input data to critical benchmarks cease, this could undermine the representative nature of such benchmarks and negatively impact the benchmarks' ability to reflect its underlying market or economic reality. The possibility to mandate the administration of critical benchmarks, as well as the possibility to mandate contributions to such benchmarks, should therefore be ensured for an overall period of 5 years in total. Critical benchmarks are in a process of reform. Switching from an existing critical benchmark to an appropriate successor rate requires a period of transition so that all legal and technical arrangements necessary for such a switch can be completed without disruption. During this transitional period the existing critical benchmark will need to be published alongside its ultimate successor rate. It is therefore necessary to extend the period during which an existing critical benchmark can be published and used without their administrator having **applied for authorisation.** ~~**obtained the necessary regulatory authorisations**~~.

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10 Commission Recommendation 2013/179/EU of 9 April 2013 on the use of common methods to measure and communicate the life cycle environmental performance of products and organisations (OJ L 124, 4.5.2013, p. 1).

(2~~0~~1) Regulation (EU) 2016/1011 should therefore be amended accordingly.

HAVE ADOPTED THIS REGULATION:

*Article 1*

**Amendments to Regulation (EU) 2016/1011**

Regulation (EU) 2016/1011 is amended as follows:

1. in Article 3(1), the following paragraphs 23(a) and 23(b) are inserted:

“(23a) ‘low carbon benchmark’ means a benchmark that is marketed as a low carbon impact benchmark where the underlying assets, for the purposes of point 1(b)(ii) of this paragraph, are selected so that the resulting benchmark portfolio has less carbon emissions when compared to the assets that comprise a standard capital-weighted benchmark and which is constructed in accordance with the standards laid down in the delegated acts referred to in Article 19a(2);

(23b) ‘positive carbon impact benchmark’ means a benchmark that is marketed as a positive carbon impact benchmark where the underlying assets, for the purposes of point 1(b)(ii) of this paragraph, are selected on the basis that their carbon emissions savings exceed the asset's carbon footprint and which is constructed in accordance with the standards laid down in the delegated acts referred to in Article 19a(2).”;

2. Article 13 is amended as follows:

(a) in paragraph 1, the following points (d) and (e) ~~is~~are added:

“(d) an explanation of how the key elements of the methodology laid down in point (a) reflect environmental, social or governance (‘ESG’) factors for each benchmark or family of benchmarks which pursue or take into account ESG objectives

(e) by 31 December 2021, the Commission shall review whether the requirement laid down in point (d) could be extended to all benchmarks, in the light of future market, technological and regulatory developments;”

(b) the following paragraph 2a is inserted:

“2a. The Commission shall be empowered to adopt delegated acts in accordance with Article 49 to specify further the minimum content of the explanation referred to in point (d) of paragraph 1.”;

3. in Title III, the following Chapter 3a is inserted:

"Chapter 3a

**Low carbon benchmarks and positive carbon impact benchmarks**

Article 19a

**Low carbon benchmarks and positive carbon impact benchmarks**

(1) The requirements laid down in Annex III shall apply to ~~the provision of, and contribution to,~~benchmarks marketed as low carbon benchmarks or positive carbon impact benchmarks in addition to, ~~or as a substitute for,~~ the requirements of Title II, III and IV.

(2) The Commission shall be empowered to adopt delegated acts in accordance with Article 49 to specify further the minimum standards ~~for~~ applicable to benchmarks marketed as low carbon benchmarks and positive carbon impact benchmarks, including:

(a) the criteria for the choice of the underlying assets, including, where applicable, any exclusion criteria for assets;

(b) the criteria and method for the weighting of the underlying assets in the benchmark;

(c) the method for the calculation of carbon emissions and carbon savings associated with the underlying assets.";

(d) By 31 December 202~~3~~1, the Commission shall review the methodology of the low carbon benchmarks and positive carbon impact benchmarks in order to reflect how the selection of the underlying assets may take into account the environmentally sustainable investments as defined in Article 2 of [Please insert reference to Regulation on the establishment of a framework to facilitate sustainable investment].

4. in Article 27, the following paragraphs 2a, ~~and~~2b and 2c are inserted:

"2a. For each requirement in paragraph 2, a benchmark statement shall contain an explanation of how environmental, social and governance factors are reflected for each benchmark or family of benchmarks provided and published which pursue or take into account ESG objectives.

2b. By 31 December 2021, the Commission shall review whether the requirement laid down under paragraph 2a could be extended to all benchmarks in the light of future market, technological and regulatory developments.

2~~b~~c.The Commission shall be empowered to adopt delegated acts in accordance with Article 49 to specify further the information referred to in in paragraph 2a".

5. ~~the text of the annex to this Regulation is added~~ Article 49 is amended as follows:

(a) in paragraph (2), the term "19a" is inserted after "in Articles (2)".

(b) in paragraph (6), the term "19a" is inserted after "to Articles 3(2)"

6. Article 51 (4a) is inserted: An existing benchmark designated as critical by an implementing act adopted by the Commission in accordance with Article 20 may be used in existing and new financial instruments, financial contracts, or measurement of the performance of an investment fund until 31 December 2021."

7. Article 21, last subparagraph of paragraph (3) is amended as follows: By the end of that period, the competent authority shall review its decision to compel the administrator to continue to publish the benchmark and may, where necessary, extend the time period by an appropriate period not exceeding a further 12 months. The maximum period of mandatory administration shall not exceed 5 years in total.

8. Article 23, last subparagraph of paragraph 6 is amended as follows: The maximum period of mandatory contribution under points (a) and (b) of the first subparagraph shall not exceed 5 years in total.

9. the text of the ~~a~~Annex to this Regulation is added.

*Article 2*

This Regulation shall enter into force on the day following that of its publication in the *Official Journal of the European Union*. A benchmark administrator providing a low carbon benchmark and a positive carbon impact benchmark in accordance with Article 19a shall be required to comply with the requirements by 30 April 2020.

It shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

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| *For the European Parliament* | *For the Council* |
| *The President* | *The President* |

**<u>ANNEX III</u>**

# Low-carbon <u>benchmarks</u> and positive carbon impact benchmarks

***Methodology for low carbon benchmarks***

1. The administrator of a low-carbon benchmark shall formalise, document and make public any methodology used for the calculation of low carbon benchmarks, describing the following:

   (a) the list of the underlying assets that are used for calculating the low carbon benchmark;

   (b) all criteria and methods, including selection and weighting factors, metrics, proxies used in the benchmark calculation;

   (c) the criteria applied to exclude assets or companies that are associated with a level of carbon footprint or a level of fossil reserves that are incompatible with inclusion in the low carbon benchmark;

   (d) the criteria for and the methods of how the low carbon benchmark measures the carbon footprint and carbon savings associated with the underlying assets in the index portfolio;

   (e) the tracking error between the low carbon benchmark and the parent index;

   (f) the positive reweighting of low-carbon assets in the low carbon benchmark versus the parent index and the explanation of why this reweighting is necessary to reflect the chosen objectives of the low carbon benchmark;

   (g) the ratio between the market value of the securities that are in the low carbon benchmark and the market value of the securities in the parent index;

   (h) the type and source of ~~**input**~~ data used for the selection of assets or companies eligible for the low carbon benchmark, including:

      (i) emissions from sources that are controlled by the company;

      (ii) emissions from the consumption of purchased electricity, steam, or other sources of energy generated upstream from the company;

      (ii) emissions that are a consequence of the operations of a company but that are not directly controlled by the company;

      (iv) emissions which would continue to exist if the company's products or services would be replaced by more carbon emitting substitutes ('emission savings');

      (v) whether the ~~**input**~~ data uses the Product and Organisation Environmental Footprint methods as defined in points (a) and (b) of point 2 of Commission Recommendation 2013/179/EU;

(i) the total carbon-footprint exposure of the index portfolio and the estimated impacts on climate-change mitigation of the low carbon strategy pursued by the benchmark;

(j) the rationale for adopting a particular low-carbon methodology strategy or objective and an explanation of why the methodology is appropriate for the calculation of the low-carbon objectives of the benchmark;

(k) the procedure for internal review and approval of a given methodology, as well as the frequency of such internal review.

***Methodology for positive carbon impact benchmarks***

2. The administrator of a positive carbon impact benchmark, in addition to the obligations applicable to the administrator of a low carbon benchmark, shall disclose the positive carbon impact of each underlying asset included in the benchmark and shall specify the formula or calculation that is used to determine whether the emission savings exceed the investment asset's or company's carbon footprint ('positive carbon impact ratio').

***Changes to the methodology***

3. Administrators of low-carbon **benchmarks** and positive carbon impact benchmarks shall adopt and make public to users procedures for and the rationale of any proposed material change in their methodology. Those procedures shall be consistent with the overriding objective that benchmark calculations adhere continuously to the low-carbon or positive carbon impact objectives. Those procedures shall provide:

(a) advance notice in a clear time frame that gives users sufficient opportunity to analyse and comment on the impact of such proposed changes, having regard to the administrators' calculation of the overall circumstances;

(b) for the possibility for users to comment on those changes and for the administrators to respond to those comments, where those comments shall be accessible for all market users after any given consultation period, except where the commenter has requested confidentiality.

4. Administrators of low-carbon **benchmarks** and positive carbon impact benchmarks shall regularly examine their methodologies to ensure that they reliably reflect the relevant low-carbon or positive carbon objectives and shall have a process in place for taking the views of relevant users into account.".