

1 November 2019

Bundesanstalt für Finanzdienstleistungsaufsicht
Marie-Curie-Str. 24-28
60439 Frankfurt am Main

Submitted via email to: Konsultation-16-19@bafin.de

RE: Konsultation 16/2019 – Merkblatt der BaFin zum Umgang mit Nachhaltigkeitsrisiken

Dear Sirs,

BlackRock¹ is pleased to have the opportunity to respond to Bundesanstalt für Finanzdienstleistungsaufsicht's (BaFin's) call for feedback on the guidelines on sustainability risks.

As an important part of our fiduciary duty to our clients, BlackRock advocates for public policies that we believe are in the long-term best interests of investors. We support the creation of regulatory regimes that increase financial market transparency, protect investors, and facilitate responsible growth of capital markets, while preserving consumer choice and properly balancing benefits versus implementation costs.

BlackRock firmly believes that sustainability-related risks can be material drivers of investment value. Integration of sustainability-related data points and risk considerations in investment and risk management processes, as relevant to a particular investment management mandate, is therefore consistent with asset managers' responsibilities to exercise due care and skill when acting as a fiduciary for asset owners.

We welcome BaFin's efforts to provide the companies it supervises an orientation in managing sustainability risks, understood as a sub-category of existing risk types. We believe that as expertise, information and the regulatory framework around sustainability and sustainable investment evolves, both market participants and regulators will need to work closely together to ensure that market and supervisory practices evolves along with it.

Due to the range of market participants with differing business models covered by this guidance, and the huge variety of different sustainability-related investment approaches that exist today, supervisory guidance must be adaptable enough to meet a wide range of circumstances. We therefore support the principles-based approach that BaFin has taken, leaving sufficient flexibility for implementation, market developments and alignment with forthcoming EU policy initiatives.

We provide further commentary below, and welcome further discussion on any of the issues raised.

Yours faithfully,

Dirk Schmitz
CEO, BlackRock Asset
Management Deutschland AG

Joanna Cound
Head of Public Policy, EMEA

¹ BlackRock is a leading provider of investment, advisory and risk management solutions. Our clients include pension plans, insurers, banks, foundations, official institutions, and other financial institutions, as well as individuals – both in Germany and globally. Two thirds of the assets we manage are in long-term retirement solutions. Our clients can access our investment solutions through a variety of product structures, including institutional separate accounts, mutual funds and other pooled investment vehicles, and the industry-leading iShares ETFs. We have been present in Germany since 1994. The investment activities of BlackRock in Germany are regulated by the KAGB (German Investment Code), as well as EU law, including MiFID II (covering investment services and transaction reporting); the AIFM Directive (ruling alternative investment managers and funds); the UCITS Directive. BlackRock in Germany is supervised by BaFin and Bundesbank.

Ensure the guidelines are grounded in a shared definition of sustainability risks

Sustainability-related factors can be material drivers of the value of a particular investment, and they therefore can be important considerations, alongside other factors, in assessing investment risks and opportunities. The ability of supervised firms to follow the best practice guidance set out by BaFin is contingent on agreement around a shared definition of sustainability risks. BaFin's definition of ESG risks, rooted in the United Nations Sustainable Development Goals, reflects the impact of companies or investments on these sustainability goals. Conversely, the concept of sustainability risks, per most rating systems and existing investment approaches, focuses on the material risks, related to sustainability factors, to a particular portfolio company or investment.

In the context of asset management, we would recommend aligning the definition of sustainability risk with the more materiality-focused definition in the EU Disclosure Regulation: A sustainability risk means an environmental, social or governance event or condition that, if it occurs, could cause a negative material impact on the value of the investment.

Generally speaking, the concept of sustainability risk is best understood as the impact of idiosyncratic sustainability factors or broader sustainability-related macro themes on *specific investments* – not as an aggregated risk at the portfolio-level for a fund or other portfolio.

We welcome BaFin's explicit reference to the materiality of sustainability risks, since the same piece of sustainability-related data regarding a particular company may be material to some portfolios and not to others, depending on the investment strategy, time horizon, end-investor preferences and risk profile.

We welcome best practice guidance that is additive to the current European proposals from the Sustainable Finance Action Plan, as alignment will be key to ensuring shared objectives are achieved without increasing complexity unnecessarily.

Clarifying application of the guidelines to asset managers

While we note that BaFin's guidance leaflet is intended to be high-level enough to cover all supervised firms, we believe we can add most value by commenting on their possible application to an asset manager. Asset managers manage investments on behalf of their clients, the asset owners, and differ from most financial institutions, in that they do not use their balance sheet in the ordinary course of business.

While noting BaFin's objective to create a cross-sectoral guidance note, it is unlikely that a one-size-fits-all approach to the integration and management of sustainability risks in risk management and investment processes will be appropriate to the huge variety of different investment approaches and institutions that exist today. For example, we note that some of the references in the draft guidance to investment due diligence processes are most similar to the corporate lending or underwriting process that a bank might undertake: this process will look very dissimilar to (for example) the process that a portfolio manager for a fund focused on listed equities might undertake as part of their investment process. We are therefore pleased to see that BaFin recognises the need for requirements to be principles-based and proportional, to allow for the adaptability of the rules to meet the wide variety of circumstances and applications in which they will be expected to apply.

That said, we recommend that BaFin distinguishes more clearly between guidelines relevant for different financial services institutions, for example, some guidelines pertain to credit institutions and others to asset managers, as this would support broad take up of the guidelines.

Even within sectors of market participants, the potential for wide variation of relevance of some parts of the guidance exist. For example, we also suggest making clear that the guidelines cater for differences at the product level, such as for index-based investment strategies compared to active investment strategies, where managers have significantly different levels of legal ability to control investment decisions.

Business organization and proportionality

To support practical uptake of the guidelines, BaFin should make clear that guidance for sustainability risk management relates to the most appropriate level of the organization: for example, risk

management of funds, rather than the business operations of the supervised asset management entity itself.

At the entity level, we support BaFin's view that responsibility for developing and communicating a strategy with regard to managing sustainability risk at the supervised entity level lies with the management, however we note that this can and should mean different levels within wider group structures. Supervised entities that are part of a larger group structure should have the flexibility to fulfil the spirit of the guidelines in a way that is most appropriate to their business structure and client needs, in order to best meet the intended objectives. For example, clear tone from the top on sustainability risk may be fulfilled primarily at a group level, where Board level leadership or centralized sustainability functions exist, and reiterated at the supervised entity level.

At the product or investment level, we support the concept of sustainability risks as being a complimentary facet of existing risk management approaches, such as operational and market risk, and not a separate risk category in itself. BaFin should ensure this is clearly and consistently expressed throughout the guidelines. However, we note that this means something different for an active investment strategy, which has the option to sell a holding impacted by material sustainability risks, that for an index investment strategy, which holds an investment for as long as it is included in the index tracked.

Risk management across different types of products

As part of its investment process on behalf of its clients, BlackRock assesses a range of factors that might affect the long-term financial sustainability of the companies in which we invest.

BlackRock offers investors a wide range of environmentally sustainable investment options, with the largest range of Sustainable ETFs in the world, and as a leading investor in renewable power generation globally. Sustainability risk management methods should be consistent with the investment approach and risk strategy of a given investment product, as described in its offering documents, enabling companies to appropriately manage sustainability risks.

Role of investment stewardship activities in addressing sustainability risks

We welcome the recognition of the role of investment stewardship engagement with investee companies, and of voting in shareholder meetings, in order to address sustainability risks. BlackRock's investment stewardship team – the largest in the asset management industry – engages directly with companies held globally in index and active portfolios alike to encourage them to adopt the robust business practices consistent with sustainable long-term performance. This year we participated in over 2,000 engagements with nearly 1,500 companies.

At BlackRock we frame our investment stewardship work, including the treatment of environmental, social and corporate governance (ESG) factors, within an investment context. We have long believed that a sound corporate governance framework promotes strong leadership by boards of directors, as well as good management practices, and contributes to the long-term financial success of companies. We are seeking to evaluate how companies manage the material sustainability-related risks and opportunities within their businesses, and engagement helps build mutual understanding on these topics. For example, BlackRock believes that climate change presents significant investment risks that have the potential to impact the long-term value of many companies. We therefore prioritise climate risk in our evaluation of and engagement with companies – over the past two years, we engaged over 370 companies globally on this topic. Further information on BlackRock's approach to investment stewardship engagement on climate risk is available at <https://www.blackrock.com/corporate/literature/publication/blk-commentary-engaging-on-climate-risk.pdf>.

Finally, we understand the guidance to be a non-binding recommendation of good practice. This should be reflected consistently throughout the language of the guidance, so that it is clear that, for example, choosing to follow external sustainability standards and implement relevant recommendations is entirely voluntary. As such, monitoring does not necessarily fall within the purview of a supervised entity's regulatory compliance function.

We hope these comments are helpful to your deliberations, and welcome further discussion on any specific issues that may assist BaFin. We look forward to continued engagement with you as the new regulatory framework around sustainability, and the growth of sustainable investment products and practices will inevitably raise a range of new questions that it will be incumbent on supervisors and market participants to collectively answer.