BETTER FINANCE
The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

Ref: Consultation on the renewed sustainable finance strategy

Link to consultation: https://ec.europa.eu/info/consultations/finance-2020-sustainable-finance-strategy_en

BETTER FINANCE Reply

Executive Summary

Opportunities and challenges	BETTER FINANCE believes that the main challenges and opportunities for next coming 10 years will be: • Reorienting the equity and bond funding towards sustainable investments. • The identification of sustainable investments must be based on facts and science, not on emotions and ideologies, and on the probability to have a positive impact on the environment, society and corporate governance. • Addressing short-termism and barriers to shareholder engagement in corporate and investor governance: - professional equity investment intermediaries (asset managers, pension funds, life insurers) must engage with investee companies for long term sustainability, - and barriers to the engagement of individual equity investors (who are mostly long term oriented) must be lifted. • Addressing the issues related to investment advice, in particular regarding ESG matters: it should be unbiased, competent and intelligible.
Company reporting, transparency and comparability	Currently, there is little harmonised, standardized and comparable ESG data published by issuers. Moreover, the parallel but separate build-up of an EU taxonomy, of EU ESG disclosures and of the review of the EU non-financial reporting directive does not ensure consistency of the future harmonisation and standardization frameworks. BETTER FINANCE believes that the creation of a common, publicly accessible, free-of-cost data portal for ESG would be beneficial for investors, in particular for individual investors, that are in need of comparable and meaningful ESG information regarding companies and sustainable investment funds. One of the main issues at the moment is the diversity of approaches and methodologies to assess the sustainability of companies and sustainable investment products by assets managers and ESG rating providers. Therefore, it is essential that ESG analysis/assessment uses the same "language" adopting criteria and standardised ESG information disclosure in order to guarantee the comparability of sustainable investment products.

Sustainability research and ratings	BETTER FINANCE's *Sustainable Investment Funds Research*[1]reveals a high degree of heterogeneity on how the ESG rating providers assess the sustainability of companies. Each company individually could receive different ratings from different ESG rating providers, thus increasing the complexity for the investor to understand the real degree of sustainability of the company. Considering the high degree of misalignment of ESG ratings, we advise the EU Commission to develop a regulatory framework for ESG rating providers. Also, for nonprofessional individual investors, it is essential to keep the comparison of the long term performance of ESG investment products with simple, objective mainstream capital market indices chosen by the asset managers, as warranted by the current UCITS funds rules.
EU green bonds standards	The highest risk threatening the future of green bods is the one of greenwashing. It is necessary to guarantee harmonization and coordination among regulations. Third-party service providers of sustainability data, rating and research requires reform that would guarantee a high degree of correlation among providers reducing the existing gaps and divergences of practices. This need to be done in harmonization with the other initiatives and regulations such taxonomy, non-financial reporting directive, green bonds standards etc.
Reorientation of the capital market into real economy investments and activities	The main objective of the renewed sustainable finance strategy needs to reflect a reorientation of capital flows into greener real economy investments and activities. This will not be possible if the new framework targets an already existing number of financial products with misleading environmental, social and governance claims. Sustainable investing should not become a marketing gimmick. It would be possible to reorient capital flows towards sustainable investment in order to achieve sustainable and inclusive growth only if new sustainable products with high environmental social and governance standards are issued. The EU Commission has the opportunity to set high level standards for impactful products that will allow to measure the real effects of sustainable products in our economy. The identification of sustainable investments must be based on facts and science, not on emotions and ideologies, and on the probability to have a positive impact on the environment, society and governance of companies.
Corporate governance, long-termism and investor engagement	BETTER FINANCE believes Employee Share Ownership (ESO) to be crucial in addressing the impending Covid19 financial crisis, but also key for the success of the Capital Markets Union (CMU) and of any sustainable finance strategy by reacquainting EU Citizens with equities as the financial instrument most likely to protect the real value of their lifetime financial savings over the long-term. Indeed, ESO has a proven and direct link to increased financial literacy and knowledge about equities and capital markets, since the workplace is the only independent way for adults to get educated on equity investment, equity ownership and related engagement responsibilities, and capital markets. Studies also show that companies with a significant ESO are more focused on sustainability issues and are more resilient in terms of employment and salary levels during crisis. Biased investment "advice" at the retail points of sale must be eliminated to enable actual access of EU savers to equity investments. Also , EU Authorities must

[1] BETTER FINANCE Sustainable Investment Funds Research not yet published

	at last eliminate the barriers to the engagement of EU citizens as shareholders towards more sustainability of investee companies. This implies to have an EU-wide definition of "shareholder" to ensure that the actual shareholders can exercise their voting rights , instead of financial intermediaries ("other people's money") as it is very often the case for cross-border voting within the EU. And - in the XXIst century – it is about time the EU develops a plan to enable EU citizens to exercise their voting rights on their smart phones. The transparency requirements of the SRD II on both asset managers and proxy advisers could be improved or expanded to more granular duties under the Sustainable Finance Agenda.
A complete taxonomy framework	The review clause should further expand the taxonomy to include also the social and governance aspects. Taxonomy as currently drafted remains incomplete as provides a framework only for the environmental dimension but leaves out the social and governance one. Social and governance considerations are integrated aspects of the overall sustainability assessment performed by asset managers and ESG rating providers. The missed opportunity to establish a complete taxonomy would jeopardize the efforts aiming at addressing the divergent market practices. In addition, its non-mandatory nature would have only small impact on the entire sustainable investments landscape.
Asset managers fiduciary duties	The EU Commission should consider developing **a stewardship code** – a framework of duties that asset managers must observe with regards to the issuer – should be instituted, enforcing a comply or explain principle. In addition, institutional investors should be obliged to produce reports justifying why their actions in corporate governance of companies best serve the company and their clients (beneficial owners).

Contents

About BETTER FINANCE

BETTER FINANCE, the European Federation of Investors and Financial Services Users, is the European public interest non-governmental organization solely dedicated to the interests of European citizens as savers, individual investors and financial services users at the European level to lawmakers and the public in order to promote research, information and training on investments, savings and personal finances.

BETTER FINANCE acts as an independent financial expertise and advocacy center to the direct benefit of European financial services users. Since the BETTER FINANCE constituency includes individual and small shareholders, fund and retail investors, savers, pension fund participants, life insurance policy holders, borrowers, and other stakeholders who are independent from the financial industry, it has the best interests of all European citizens at heart. As such its activities are supported by the European Union since 2012.

Instructions on how to read this paper: this document contains the response of BETTER FINANCE to the European Commission's online survey (public consultation) concerning the consultation on the renewed sustainable finance strategy but it is not the actual response form submitted.[2] Each section contains a ***short summary*** of the corresponding section in the consultation and of the questions analysed so the reader can understand the context.[3]

Introduction

This consultation is part of the EU Commission' objective to increase the EU climate action and environmental policy ambitions set in the European Green Deal.

As expressed in the Consultation document: ***The ongoing COVID-19 outbreak in particular shows the critical need to strengthen the sustainability and resilience of our societies and the ways in which our economies function.*** *This is necessary to, above all, minimise the risk of similar health emergencies in the future, which are more likely to occur as climate and environmental impacts escalate. In parallel, it will be paramount to ensure the resilience and capacity of our societies and economies to resist and recover from such emergencies. The COVID-19 outbreak underscores some of the subtle links and risks associated with human activity and biodiversity loss. Many of the recent outbreaks (e.g. SARs, MERS, and avian flu) can be linked to the illegal trade in, and consumption of, often endangered wild animal species. Furthermore, experts suggest that degraded habitats coupled with a warming climate may encourage higher risks of disease transmission, as pathogens spread more easily to livestock and humans. Therefore, it is important – now more than ever - to address the multiple and often interacting threats to ecosystems and wildlife to buffer against the risk of future pandemics, as well as preserve and enhance their role as carbon sinks and in climate adaptation.*[4]

The intent of the Renewed Sustainable Finance Strategy is focus predominately on three aspects:

- To reinforce the foundations for sustainable investing by creating a framework that addresses short-termism.
- To maximise the impact of the sustainable finance framework
- To integrate and manage climate and environmental risks into financial institutions and the financial system.

This consultation builds on a number of previous initiatives and reports, as well as complementing other consultation activities of the Commission, in particular[5]:

- The final report of the High-Level Expert Group on Sustainable Finance (2018);
- The EU Action Plan on Financing Sustainable Growth (2018);
- The communication of the Commission on 'The European Green Deal' (2019);
- The communication of the Commission on 'The European Green Deal Investment Plan'(2020);
- The reports published by the Technical Expert Group on sustainable finance (TEG) with regard to an EU taxonomy of sustainable activities, an EU Green Bond Standard,

[3] https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/2020-sustainable-finance-strategy-consultation-document_en.pdf
[4] https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/2020-sustainable-finance-strategy-consultation-document_en.pdf
[5] Ibid.

methodologies for EU climate benchmarks and disclosures for benchmarks and guidance to improve corporate disclosure of climate-related information.

This consultation also makes references to past, ongoing and future consultations, such as the public consultation and inception impact assessment on the possible revision of the Non-Financial Reporting Directive (NFRD), the inception impact assessment on the review of the Solvency II Directive or the future consultation on investment protection.

Consultation questions

Section I: questions addressed to all stakeholders on how the financial sector and the economy can become more sustainable

Question 1: With the increased ambition of the European Green Deal and the urgency with which we need to act to tackle the climate and environmental-related challenges, do you think that (please select one of the following):

- ✓ **Major additional policy actions are needed to accelerate the systematic sustainability transition of the EU financial sector.**
- Incremental additional actions may be needed in targeted areas, but existing actions implemented under the Action Plan on Financing Sustainable Growth are largely sufficient.
- No further policy action is needed for the time being.

Question 2: Do you know with sufficient confidence if some of your pension, life insurance premium or any other personal savings are invested in sustainable financial assets?

- Yes
- ✓ **No**
- Do not know

If yes, do you consider that you have had sufficient access to information with regard to the integration of sustainability criteria and options to invest in sustainable financial assets? Please explain and specify whether you searched for the information yourself or whether the information was made available to you [BOX 2000 characters].

If no, would you like to be offered more information with regard to the integration of sustainability criteria and options to invest in sustainable financial assets and divest from non-sustainable assets?

- ✓ **Yes**
- No
- Do not know

If necessary, please explain your answer [BOX 2000 characters].

It is less a question of more information but rather of better and reliable information to enable investors making informed investment decisions.

Question 3: When looking for investment opportunities, would you like to be systematically offered sustainable investment products as a default option by your financial adviser, provided the product suits your other needs?

- ✓ **Yes**
- No
- do not know

Question 4: Would you consider it useful if corporates and financial institutions were required to communicate if and explain how their business strategies and targets contribute to reaching the goals of the Paris Agreement?

- Yes, corporates.
- Yes, financial institutions.
- **Yes, both**
- No

If no, what other steps should be taken instead to accelerate the adoption by corporates and financial sector firms of business targets, strategies and practices that aim to align their emissions and activities with the goals of the Paris Agreement? [BOX, 2000 characters]

N/A

Question 5: One of the objectives of the European Commission's 2018 Action Plan on Financing Sustainable Growth is to encourage investors to finance sustainable activities and projects. Do you believe the EU should also take further action to:

- Encourage investors to engage, including making use of their voting rights, with companies conducting environmentally harmful activities that are not in line with environmental objectives and the EU-wide trajectory for greenhouse gas emission reductions, as part of the European Climate Law, with a view to encouraging these companies to adopt more sustainable business models: scale from 1 (strongly disagree) to 5 (strongly agree).

1	2	3	4	~~5~~

- Discourage investors from financing environmentally harmful activities that are not in line with environmental objectives and the EU-wide trajectory for greenhouse gas emission reductions, as part of the European Climate Law: scale from 1 (strongly disagree) to 5 (strongly agree).

1	2	3	~~4~~	5

- In case you agree or strongly agree with one or both options [4-5]: what should the EU do to reach this objective? [BOX, 2000 characters]

Small shareholders face many difficulties in exercising their rights in the corporate governance of companies. The EU framework for the Shareholder Rights Directive should go much further in clarifying the rights and obligations of issuers and improving the conditions for individual shareowners to actively participate in the decision-making process. Moreover, institutional shareholders have the largest impact on corporate governance as the former manage billions of euros of capital on behalf of EU citizens. **However, asset managers have little incentive – and put little effort – to actively engage with investee companies and far too often change ownership (buy and sell) in companies**. **Long-termism in equity markets must be fostered through regulation**. The EU Commission should consider developing **a stewardship code** – a framework of duties that asset managers must observe with regards to the issuer – should be instituted, enforcing a comply or explain principle. In addition, institutional investors should be obliged to produce reports justifying why their actions in corporate governance of companies best serve the company and their clients (beneficial owners).

In addition, the issuer and the shareholder are currently disconnected as a result of the intermediaries' chain in between, the constant breach of (local company) law of by certain intermediaries, and because a common definition of "shareholder" is lacking. A common definition of shareholders is necessary:
The absence of an EU definition of "shareholder" in EU rules is extremely damaging to long term shareholder engagement. SRD II failed again to adopt an EU definition of "shareholder", allowing still a lot of "agency owners" (nominee accounts in the UK in particular, global custodians for equity held outside of the investee companies' domiciles)

to hold and exercise the voting rights instead of the real shareholders. For example, in France, most foreign held shares in the French blue-chip companies are voted at AGMs by global custodians who never disclose who are the shareholders they are voting for, and claiming they have a general proxy agreement from those. We requested to see these agreements and could never see any. These agency owners have totally misaligned interests from the shareholders and are often those who are most active in the securities lending markets.[6] In Spain, we experienced at several AGMS, that intermediaries as nominee shareholders did not accept vote instructions from the real shareholders, i.e. those who have invested money, but brought forward their own vote instructions which in all cases were in favour of the Board of Director's proposals. Such a behaviour is detrimental for the exercise of real shareholders' rights in the corporate governance of issuers.

Section II: Questions targeted at experts

The following section asks further technical and strategic questions on the future of sustainable finance, for which a certain degree of financial or sustainability-related expertise may be useful. This section is therefore primarily addressed at experts.

Question 6: What do you see as the three main challenges and three main opportunities for mainstreaming sustainability in the financial sector over the coming 10 years? *[BOX, 2000 characters].*

We believe that the main challenges and opportunities for next coming 10 years will be:

1- **Reorienting equity and bond funding towards sustainable investments**: It is clear that disclosure requirements for financial advisers, taxonomy and rules on non-financial reporting are not sufficient to reorient the capital market towards sustainable investments. Also market practices need to change, allowing product manufactures to issue a new generation of sustainable financial products that have high standards and that have a concrete impact in the real economy. The EU Commission has the opportunity to create impact investing label that set high level standards for impactful products that will allow to measure the real effects of sustainable products on our economy. The identification of sustainable investments must be based on facts and science, not on emotions and ideologies, and on the probability to have a positive impact on the environment, society and governance of companies.

2- **Addressing short-termism and barriers to shareholder engagement in corporate and investor governance:**

[6] From short-termism paper we have prepared for Jella

- professional equity investment intermediaries (asset managers, pension funds, life insurers) must engage with investee companies for long term sustainability,
- and barriers to the engagement of individual equity investors (who are mostly long term oriented) must be lifted.

Small shareholders face many difficulties in exercising their rights in the corporate governance of companies. The EU framework for the Shareholder Rights Directive should go much further in clarifying the rights and obligations of investors and improving the conditions for individual shareowners to actively participate in the decision-making process. Moreover, institutional shareholders have the largest impact on corporate governance as the former manage billions of euros of capital on behalf of EU citizens. However, asset managers have little incentive – and put little effort – to actively engage with investee companies and far too often change ownership (buy and sell) in companies. Long-termism in equity markets must be fostered through regulation. A stewardship code – a framework of duties that asset managers must observe with regards to the issuer – should be instituted, enforcing a comply or explain principle. In addition, institutional investors should be obliged to produce reports justifying why their actions in corporate governance of companies best serve the company and their clients (beneficial owners).

3- **Addressing the issues related to investment advice, in particular regarding ESG matters: it should be unbiased, competent and intelligible.** Investment advisors should be concerned only with the best interest of the investor and should be objective and independent of any selling incentive. The new rules of MiFID II partially addressed the issue of biased advice. However, these rules should be mirrored for the insurance and banking sector as well and should be found in an equivalent regime for closed architecture distribution systems. A duty of care, in the shape of a code of conduct or "**Hippocratic oath**" for investment services providers, must be put in place to ensure that the best interests of investors are taken into account at all stages of the investment process: advice, distribution, and execution. Lastly, EU and national supervisory authorities should pay particular attention to the risks stemming from new FinTech business models that could result in breaches of investor protection and ethical rules. The attitude of public authorities should be proactive in creating tools – such as regulatory sandboxes – to test and identify potential inefficiencies of these innovations and take solution-oriented steps in order to prevent larger negative effects on the financial system.

Question 7: Overall, can you identify specific obstacles in current EU policies and regulations that hinder the development of sustainable finance and the integration and management of climate, environmental and social risks into financial decision-making?

- *Please provide a maximum of three examples [BOX max. 2000 characters].*

Lack of common definitions in sustainable finance is one of the main obstacles that hinder the development and the integration of environmental, social and governance risks into financial decision-making. Individual investors are confronted with a multitude of labels, definitions and practices that increase the complexity of sustainable investment products. The lack of a standardised framework has led market participants to develop different approaches on how to assess the sustainability of issuers and funds thus making almost impossible the possibility to compare the sustainable performance of these products.

Prioritising E over S and G in the taxonomy as well as in the Ecolabel project is counterproductive and may have discouraging effect on consumer/investors interested in fully sustainable financial products. In BETTER FINANCE opinion, environmentally-friendly products should not come with concessions on social and governance aspects (Criterion 3); there should be no trade-off between ecological (E) and other (SG) standards.

Question 8: The transition towards a climate neutral economy might have socio-economic impacts, arising either from economic restructuring related to industrial decarbonisation, because of increased climate change-related effects, or a combination thereof. For instance, persons in vulnerable situations or at risk of social exclusion and in need of access to essential services including water, sanitation, energy or transport, may be particularly affected, as well as workers in sectors that are particularly affected by the decarbonisation agenda. How could the EU ensure that the financial tools developed to increase sustainable investment flows and manage climate and environmental risks have, to the extent possible, no or limited negative socio-economic impacts? *[BOX, 2000 characters]*

The negative impact of decarbonisation and climate change policies on the society and local communities can be prevented if well-planned and carefully addressed with multi-stakeholder engagement. Climate change mitigation policies need to be based on a pro-poor[7] approach. The aim is not only to prevent the negative impact of climate change policies but also to reduce the existing inequalities.[8] Policy making in this context needs to assess the indirect effects of climate change mitigation policies by integrating an ex-ante approach that evaluates the impact of these reforms on society (risk of social exclusion, aggravation of inequalities, access to essential services, jobs etc). In case of possible risk, additional measures should be implemented (at EU and national level) in order to counteract on negative socio-economic implications by providing specific targeted measures for disadvantaged people or communities affected by these reforms. However, it is widely accepted that climate change will exacerbate inequalities in the long-term. Therefore, negative effects associated to climate change policies should not be taken as an excuse to avoid the implementation of such policies but it should be an opportunity to address also social and economic inequalities that guarantee a just transition phase.

[7] Social impacts of climate change mitigation policies and their implications for inequalities https://www.tandfonline.com/doi/full/10.1080/14693062.2019.1596873

[8] *Ibid.*

Question 9: As a corporate or a financial institution, how important is it for you that policy-makers create a predictable and well-communicated policy framework that provides a clear EU-wide trajectory on greenhouse gas emission reductions, based on the climate objectives set out in the European Green Deal, including policy signals on the appropriate pace of phasing out certain assets that are likely to be stranded in the future?

Please express your view by using a scale from 1 (not important at all) to 5 (very important).

1	*2*	*3*	*4*	*5*

For scores of 4 to 5, what are, in your view, the mechanisms necessary to be put in place by policy-makers to best give the right signals to you as a corporate or a financial institution? [BOX, 2000 characters].

Question 10: Should institutional investors and credit institutions be required to estimate and disclose which temperature scenario their portfolios are financing (e.g. 2°C, 3°C, 4°C), in comparison with the goals of the Paris Agreement, and on the basis of a common EU-wide methodology?

- *Yes, institutional investors*
- *Yes, credit institutions*
- ✓ ***Yes, both***
- *No*
- *Do not know*

Question 11: Corporates, investors, and financial institutions are becoming increasingly aware of the correlation between biodiversity loss and climate change and the negative impacts of biodiversity loss in particular on corporates who are dependent on ecosystem services, such as in sectors like agriculture, extractives, fisheries, forestry and construction. The importance of biodiversity and ecosystem services is already acknowledged in the EU Taxonomy. However, in light of the growing negative impact of biodiversity loss on companies' profitability and long-term prospects, as well as its strong connection with climate change, do you think the EU's sustainable finance agenda should better reflect growing importance of biodiversity loss?

- ✓ ***Yes***
- *No*
- *Do not know*

If yes, please specify potential actions the EU could take. [BOX max. 2000 characters]

According to the OECD study on Comprehensive Overview of Global Biodiversity Finance, [9] governments expenditure that is harmful to biodiversity is six time bigger than the total spending for biodiversity.[10] Therefore, it is crucial to provide a standardised, integrated and consistent framework for corporate sustainability reporting in the sustainable finance strategy to address biodiversity loss that includes a better tracking of harmful private and public expenditure that harm biodiversity, further granularity on biodiversity related information disclosure and additional initiative that addresses biodiversity loss. Such a framework needs to include mandatory KPIs on material ESG issues including biodiversity.

Question 12: In your opinion, how can the Commission best ensure that the sustainable finance agenda is appropriately governed over the long term at the EU level in order to cover the private and public funding side, measure financial flows towards sustainable investments and gauge the EU's progress towards its commitments under the European Green Deal and Green Deal Investment Plan? *[BOX, 2000 characters]*

On the one hand, the objectives proposed by the European Green Deal represent steps in the right direction, putting the continent on a more sustainable path. On the other hand, the project might lack the necessary potential to "land on the moon". For instance, the Commission aims to reduce carbon emissions by 50-55% by 2030 and to reach carbon neutrality by 2050. However, in order to fulfil this goal and limit global warming, carbon emissions need to be reduced by at least 60-65% by 2030[11]. Therefore, the actual plan might be insufficient to meet the 1.5° C target. From a financial perspective, the Commission intends to mobilize 3 trillion euros over 10 years via public funds and private funds. Even if this figure seems impressive at first, it might not be enough to reach the estimated targets. Therefore, it is crucial to mobilize further actions from Members States and national investments through a reform of the EU fiscal framework, i.e. authorising a long-term deviation or exemption from EU fiscal rules for green public expenditures.

It is crucial for the EU Commission to walk the talk and truly reorient capital flows towards investments that really impact the environment and global warming in particular. Indeed, in our view, merely screening investment portfolios will not generate any positive impact. For example, asset managers as shareholders should get much more involved in greening the massive investment market embodied by oil companies, including specific measures to assess the environmental impact of the investments. For example, an impact investing can be an investment fund that aim to preserve and sustain the full ecological value of a forest ecosystem by improving the conservation, replanting and providing job to the local community. The final objective is to finance a project for sustain forest management, thus achieving impact generating alongside financial return.[12] The added value of impact investing is the possibility to measure the impact of the financial products in relation to KPIs and specific targets.

[9] OECD, Comprehensive Overview of Global Biodiversity Finance: https://www.oecd.org/environment/resources/biodiversity/report-a-comprehensive-overview-of-global-biodiversity-finance.pdf
[10] *Ibid.*
[11] https://www.ipcc.ch/site/assets/uploads/sites/2/2019/02/SR15_Chapter2_Low_Res.pdf
[12] https://thegiin.org/research/profile/ecotrust-forests-i-llc-ef-i

Therefore, the we believe that the Commission should consider developing an impact label that set criteria, KPIs to measure the impact of a sustainable financial product.

For additional information see Better Finance Press Release on the Green Deal.

Question 13: In your opinion, which, if any, further actions would you like to see at international, EU, or Member State level to enable the financing of the sustainability transition? Please identify actions aside from the areas for future work identified in the targeted questions below (remainder of Section II), as well as the existing actions implemented as part of the European Commission's 2018 Action Plan on Financing Sustainable Growth. *[BOX, 2000 characters]*

Strengthening the foundations for sustainable finance

In order to enable the scale-up of sustainable investments, it is crucial to have sufficient and reliable information from financial and non-financial companies on their climate, environmental and social risks and impacts. To this end, companies also need to consider long-term horizons. Similarly, investors and companies need access to reliable climate- related and environmental data and information on social risks, in order to make sound business and investment decisions. Labelling tools, among other measures, can provide clarity and confidence to investors and issuers, which contributes to increasing sustainable investments. In this context, the full deployment of innovative digital solutions requires data to be available in open access and in standardised formats.

1.1 Company reporting and transparency

In its Communication on the European Green Deal, the Commission recognised the need to improve the disclosure of non-financial information by corporates and financial institutions. To that end, the Commission committed to reviewing the Non-Financial Reporting Directive (NFRD) in 2020, as part of its strategy to strengthen the foundations for sustainable investment. A public consultation is ongoing for that purpose.

The political agreement on the Regulation on establishing a framework to facilitate sustainable investment ('Taxonomy Regulation') places ***complementary reporting requirements on the companies that fall under the scope of the NFRD****.*

In addition to the production of relevant and comparable data, it may be useful to ensure open and centralised access not only to company reporting under the NFRD, but also to relevant company information on other available ESG metrics and data points (please also see the dedicated section on sustainability research and ratings 1.3). To this end, a ***common database*** *would ease transparency and comparability, while avoiding duplication of data collection efforts. The Commission is developing a common European data space in order to create a single market for data by connecting existing databases through digital means. Since 2017, DG FISMA has been assessing the prospects of using Distributed Ledger Technologies (including blockchain) to* *federate and provide a single point of access to information relevant to investors in European listed companies (European Financial Transparency Gateway - EFTG).*

Question 14: In your opinion, should the EU take action to support the development of a common, publicly accessible, free-of-cost environmental data space for companies' ESG information, including data reported under the NFRD and other relevant ESG data?

- ✓ **Yes**
- No
- Do not know

If yes, please explain how it should be structured and what type of ESG information should feature therein. [BOX, 2000 characters]

Currently, there is little harmonised, standardized and comparable ESG data published by issuers. Moreover, the parallel but separate build-up of an EU taxonomy, of EU ESG disclosures and of the review of the EU non-financial reporting directive does not ensure consistency of the future harmonisation and standardization frameworks.

BETTER FINANCE believes that the creation of a common, publicly accessible, free-of-cost data portal for ESG data would be beneficial for investors, in particular for individual investors, that are in need of comparable and meaningful ESG information regarding companies and sustainable investment funds. Therefore, it is essential that the non-financial reporting directive will provide high degree of harmonisation on ESG information disclosure for companies. In addition, the free-of-cost data space should provide also ESG information on sustainable investments (sustainable investments funds, green bonds, etc)

One of the main issues at the moment is the diversification of approaches and methodologies to assess the sustainability of companies and sustainable investment products by assets managers and ESG rating providers. Therefore, it is essential that ESG analysis/assessment uses the same "language" adopting criteria and standardised ESG information disclosure in order to guarantee the comparability Sustainable investment products.

Digitisation could also generate benefits, such as comparability and accessibility. However, it is crucial to ensure that the digital tagging process does not undermine the whole process and will facilitate the analysis of sustainability risks of the companies. The tagging of non-financial information would only be possible if reporting is compliant with standards. Therefore, coordination and harmonization with the taxonomy is crucial on this aspect.

Question 15: According to your own understanding and assessment, does your company currently carry out economic activities that could substantially contribute to the environmental objectives defined in the Taxonomy Regulation?[13]

- Yes

[13] The six environmental objectives are climate change mitigation and adaptation, sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control, protection and restoration of biodiversity and ecosystems.

- No
- Do not know.

If yes, once the EU Taxonomy is established (end-2020 for climate change mitigation and adaptation),[14] how likely is it that you would use the taxonomy for your business decisions (such as adapting the scope and focus of your activities in order to be aligned with the EU Taxonomy)? Please use a scale of 1 (not likely at all) to 5 (very likely). If necessary, please specify [BOX, 2000 characters].

1.2 Accounting standards and rules

Financial accounting standards and rules can have a direct impact on the way in which investment decisions are made *since they form the basis of assessments that are carried out to evaluate the financial position and performance of real economy and financial sector companies.* ***In this context, there is an ongoing debate around whether existing financial accounting standards might prove challenging for sustainable and long-term investments****. In particular, some experts question whether existing impairment and depreciation rules fully price in the potential future loss in value of companies that today extract, distribute, or rely heavily on fossil fuels, due to a potential future stranding of their assets.*
Recognising the importance of ensuring that accounting standards do not discourage sustainable and long-term investments, as part of the 2018 Action Plan on Financing Sustainable Growth, the Commission already requested the European Financial Reporting Advisory Group (EFRAG) to explore potential alternative accounting treatments to fair value measurement for long-term investment portfolios of equity and equity-type instruments. EFRAG issued its advice to the Commission on 30 January 2020. Following this advice, the Commission has requested the IASB to consider the re-introduction of re-cycling through the profit or loss statement of profits or losses realised upon the disposal of equity instruments measured at fair value through other comprehensive income (FVOCI).

Question 16: Do you see any further areas in existing financial accounting rules (based on the IFRS framework) which may hamper the adequate and timely recognition and consistent measurement of climate and environmental risks?

- Yes
- No
- Do not know.

[14] Assuming that for climate change mitigation and adaptation, it would be based on the recommendations of the TEG for the EU Taxonomy.

If yes, what is in your view the most important area (please provide details, if necessary): o Impairment and depreciation rules. [BOX, 2000 characters]

- Provision rules. [BOX, 2000 characters]

- Contingent liabilities. [BOX, 2000 characters]

- Other, please specify. [BOX, 2000 characters]

1.3 Sustainability research and ratings

A variety of sustainability-related assessment tools (ratings, research, scenario analysis, screening lists, carbon data, ESG benchmarks, etc.) are offered by specialised agencies that analyse individual risks and by traditional providers, such as rating agencies and data providers. In the autumn of 2019, the Commission launched a study on the market structure, providers and their role as intermediaries between companies and investors. The study will also explore possible measures to manage conflicts of interest and enhance transparency in the market for sustainability assessment tools. The results are due in the autumn of 2020. To complement this work, the Commission would like to gather further evidence through this consultation.

Question 17: Do you have concerns on the level of concentration in the market for ESG ratings and data?

Please express your view by using a scale of 1 (not concerned at all) to 5 (very concerned).

1	2	3	4	5

If necessary, please explain the reasons for your answer. [BOX, 2000 characters]

Currently, the market has experienced a consolidation of ESG data providers, with several mergers and acquisition by big players. If on the one hand higher concentration of ESG data providers could reduce the proliferation of different and divergent methodologies of ESG analysis and assessments on the other hands this could potentially decrease the transparency and independence of ESG data. Contrary to Credit ratings that are regulated and have a correlation factor almost perfect, ESG ratings are highly misaligned, as observed in our research *BETTER FINANCE Sustainable Investment Funds Research*.[15] ESG data providers use different methodologies on how to assess sustainability and different scales such as ratings,

[15] BETTER FINANCE Sustainable Investment Funds Research is being finalised at the moment of submission of our response to the consultation and is not yet published

scores, symbols etc. In our research, we have also investigated the methodologies applied by some ESG data providers but lack of clear and detail information, and sometimes complete omission of the relevant information prevents from assessing the reliability of ESG ratings. Therefore, the main issue is not the consolidation per se, but the independence and the quality of the data provide by ESG rating agencies.

ESG rating agencies need to be truly independent providing qualitative and non-misaligned ratings.

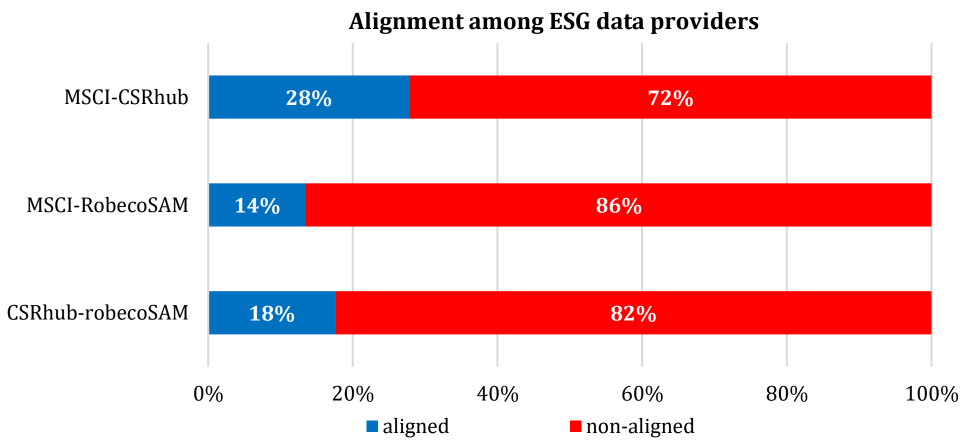
Question 18: How would you rate the comparability, quality and reliability of ESG data from sustainability providers currently available in the market?

Please express your view by using a scale of 1 (very poor) to 5 (very good).

1	2	3	4	5

If necessary, please explain the reasons for your answer. [BOX, 2000 characters]

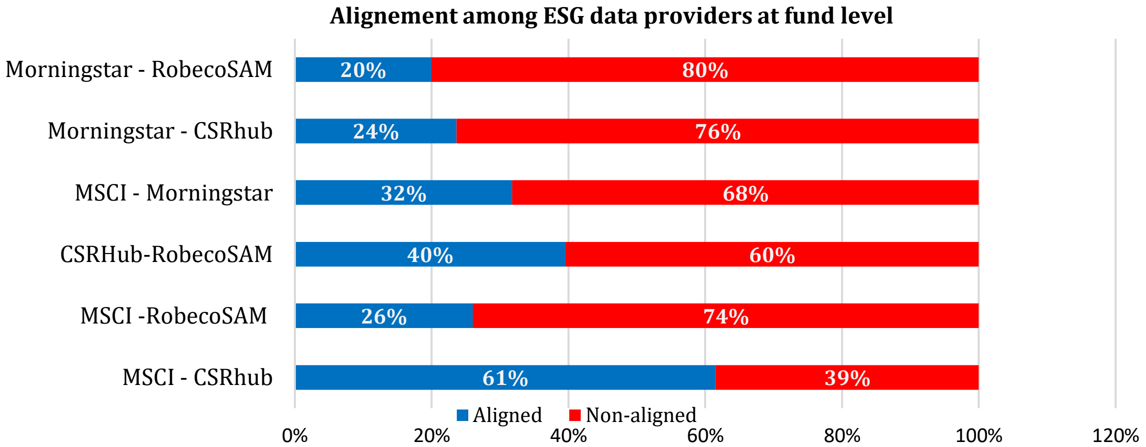
In the *BETTER FINANCE Sustainable Investment Funds Research*[16], the ESG s ratings of issuers reveals a high degree of heterogeneity on how the ESG rating providers assess the sustainability of companies. Each company individually could receive different ratings from different ESG rating



providers, thus increasing the complexity for the investor to understand the real degree of sustainability of the company (table below). The analysis considers 792 total companies.

[16] BETTER FINANCE Sustainable Investment Funds Research is being finalised at the moment of submission of our response to the consultation and is not yet published

Also looking at the alignment among ESG rating at fund level, it is possible to observe a **high degree of divergences among platforms** (table below). The analysis is based on the screening of the top 10 holdings of 321 UCITS funds domiciliated in Luxembourg.



This report's first finding is the divergence of ESG rating methodologies, at least from a "label" or "category" point of view. Based on our desk research, we found as many as 9 different ESG rating systems, which do not allow for any comparability. Furthermore, research shows that most platforms perform a *peer group analysis*, which can return misleading results in terms of ESG factoring. *Peer group analysis* would allow to score the company against a small group of companies in the same sector/economic activity contrary to a global analysis that identify a much larger number of companies thus a larger number of sustainability risks affecting the companies.

Question 19: How would you rate the quality and relevance of ESG research material currently available in the market?

Please express your view by using a scale of 1 (very poor) to 5 (very good).

1	~~2~~	3	4	5

If necessary, please explain the reasons for your answer. [BOX, 2000 characters]

As previously explained the main issues are the different practices adopted by ESG ratings. The providers have different and divergent views on how to assess the sustainability of the same company. To cite an article from the Financial Times questioning the integrity of the scoring system of these providers: *Facebook for example, was docked to a rating of 21 out of 100 last year by S&P Global, which worried about its privacy and transparency standards. Yet MSCI's rating for the social platform has hovered in the "average" range fluctuation between double B and triple-B.* [17]

ESG ratings have been under the magnifying glass of several research showing discrepancies and different perception of credibility.[18] ESG rating providers may adopt different models to assess the

[17] Heavy flows into ESG Funds raise questions over ratings, Financial Times March, 2, 2020 https://www.ft.com/content/0bd9d2ea-5c15-11ea-8033-fa40a0d65a98

[18] See Rate the Raters 2019, SustainAbility Research, https://sustainability.com/our-work/reports/rate-raters-2019/, see also Responsible Investing Guide to ESG Data Providers and Relevant Trends, Elyse Douglas, Tracy Van Holt, Tensie Whelan, Journal of Environmental investing

sustainability of the company as computer driven models, algorithms, analyst-based evaluation or a mix of the previous.[19] In addition, the disclosure of information regarding the methodology of the providers results extremely important in order to verify the complete assessment, but since providers want to protect their competitive advantage the methodologies are generally opaque or incomplete when publicly disclosed.

Question 20: How would you assess the quality and relevance of ESG ratings for your investment decisions, both ratings of individual Environmental, Social or Governance factors and aggregated ones?

Individual: Please express your view by using a scale of 1 (very poor quality and relevance) to 5 (very good).

1	~~2~~	3	4	5

Aggregated: Please express your view by using a scale of 1 (very poor quality and relevance) to 5 (very good).

1	~~2~~	3	4	5

If necessary, please explain the reasons for your answer. [BOX, 2000 characters]

Question 21: In your opinion, should the EU take action in this area?

- ✓ **<u>Yes</u>**
- No
- Do not know

If yes, please explain why and what kind of action you consider would address the identified problems. In particular, do you think the EU should consider regulatory intervention? [BOX, 2000 characters]

8,No1(2017)https://cbey.yale.edu/sites/default/files/Responsible%20Investing%20%20Guide%20to%20ESG%20Data%20Providers%20and%20Relevant%20Trends.pdf, see also Aggregate Confusion: the divergence of ESG rating, Florian Berg, Julian F Kolbel, Roberto Rigobon May 17, 2020. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3438533, see also Measuring the level and risk of corporate responsibility- an empirical comparison of different ESG rating approaches, Gregor Dorfleinter, Gerhard Halbritter & Mai Nguyen, Journal of asset management (2015) : https://link.springer.com/article/10.1057/jam.2015.31, See also What a difference an ESG rating Provider Makes!, FeiFei Li, Ari Polychronopoulos, Research Affiliates, January 2020: https://www.researchaffiliates.com/en_us/publications/articles/what-a-difference-an-esg-ratingsprovidermakes.html#:~:text=ESG%20portfolios%20constructed%20using%20the,and%20low%20correlation%20of%20returns.&text=The%20differences%20in%20how%20ratings,and%20quite%20poorly%20by%20another.

[19] Responsible Investing: Guide to ESG Data Providers and Relevant Trends, Elyse Douglas, Tracy Van Holt, Tensie Whelan, Journal of environmental Investing 8, No 1 (2017): https://cbey.yale.edu/sites/default/files/Responsible%20Investing%20%20Guide%20to%20ESG%20Data%20Providers%20and%20Relevant%20Trends.pdf

<u>*Creation of a Regulatory framework for ESG rating providers:*</u> if the ongoing legislative initiatives could help foster the standardisation and the transparency of sustainable-related information, additional requirements and standards should be considered for ESG rating agencies. Contrary to Credit ratings that are regulated and have a correlation factor almost perfect, ESG ratings are highly misaligned. The need for such regulation is essential to reduce the discrepancies among ratings and fight greenwashing. Also, for nonprofessional individual investors, it is essential to keep the comparison of the long term performance of ESG investment products with simple, objective mainstream capital market indices chosen by the asset managers, as warranted by the current UCITS funds rules.

The Commission action plan on sustainable finance specifically set as objective: "*to reorient capital flows towards sustainable investment in order to achieve sustainable and inclusive growth*."[20] This can be <u>only possible by issuing new products with clear and effective impact in the real economy.</u>

The already existing products on the market are just an attempt to optimize sustainability within the current regime only scratching the surface to reorient the capital flows towards sustainable investments.

1.4 Definitions, standards and labels for sustainable financial assets and financial products

The market for sustainable financial assets (loans, bonds, funds, etc.) is composed of a wide variety of products, offered under various denominations like 'green', 'SDG', 'transition', 'ESG', 'ethical', 'impact', 'sustainability-linked', etc. While a variety of products allows for different approaches that can meet the specific needs and wishes of those investing or lending, it can be difficult for clients, in particular retail investors, to understand the different degrees of climate, environmental and social ambition and compare the specificities of each product. ***Clarity on these definitions through standards and labels can help to protect the integrity of and trust in the market for sustainable financial products, enabling easier access for investors, companies, and savers.***

As set out in the 2018 Action Plan on Financing Sustainable Growth, the Commission services started working on: (i) developing possible technical criteria for the <u>EU Ecolabel scheme for retail funds, savings and deposits</u>, and (ii) establishing an EU Green Bond Standard (EU GBS). The Commission also committed to specifying the content of the prospectus for green bond issuances to provide potential investors with additional information, within the framework of the Prospectus Regulation.

EU Green Bond Standard

[20] Sustainable Finance Action Plan https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0097&from=EN

The Technical Expert Group on Sustainable Finance (TEG) put forward a report in June 2019 with 10 recommendations for how to create an EU Green Bond Standard (EU GBS). This was completed with a usability guide in March 2020, as well as with an updated proposal for the standard (see Annex 1).

The TEG recommends the creation of an official voluntary EU GBS building on the EU Taxonomy. Such an EU Green Bond Standard could finance both physical assets and financial assets (including through covered bonds and asset-backed securities), capital expenditure and selected operating expenditure, as well as specific expenditure for sovereigns and sub-sovereigns. The standard should in the TEG's view exist alongside existing market standards.

The overall aim of the EU GBS is to address several barriers in the current market, including reducing uncertainty on what is green by linking it with the EU Taxonomy, standardising costly and complex verification and reporting processes, and having an official standard to which certain (financial) incentives may be attached. The TEG has recommended that oversight and regulatory supervision of external review providers eventually be conducted via a centralised system organised by ESMA. However, as such a potential ESMA-led supervision would require legislation and therefore take time, the TEG suggests the set-up of a market-based, voluntary interim registration process for verifiers (the Scheme) of EU Green Bonds for a transition period of up to three years.

*Below you will find four questions in relation to the EU GBS. **A separate dedicated consultation with regards to a Commission initiative for an EU Green Bond Standard will be carried out in the future**. Please note that questions relating to green bond issuances by public authorities are covered in section 2.7 and questions on additional incentives can be found in section 2.6.*

Question 22: The TEG has recommended that verifiers of EU Green Bonds (green bonds using the EU GBS) should be subject to an accreditation or authorisation and supervision regime. Do you agree that verifiers of EU Green Bonds should be subject to some form of accreditation or authorisation and supervision?

- ✓ **Yes, at European level**
- Yes, at a national level
- No
- Do not know
- If necessary, please explain the reasons for your answer [BOX 2000 characters]

BETTER FINANCE agrees with the TEG recommendations regarding a centralised system of oversight and regulatory supervision conducted by ESMA. However, as the implementation of this regime would require time and a new legislation, we agree for a transitional and standardised external verification of issues, but we encourage to set a form of accreditation or authorisation for verifiers of EU Green bonds. Verifiers should go through a screening process that allows the operator to act as external verifier of EU green bonds against EU GBS. This transitional system should be in place only for the limited time of period before the verification is fully operational at EU level.

Question 23: Should any action the Commission takes on verifiers of EU Green Bonds be linked to any potential future action to regulate the market for third-party service providers on sustainability data, ratings and research?

- ✓ **Yes**
- No
- Do not know
- If necessary, please specify the reasons for your answer [BOX 2000 characters]

It is necessary to guarantee harmonization and coordination among regulations. Third-party service providers on sustainability data, rating and research are in dire need of a reform that would guarantee a high degree of correlation among providers reducing the existing gaps and divergent practices. This need to be harmonised with the other initiatives and regulations such taxonomy, non-financial reporting directive, green bonds standards etc.

Question 24: The EU GBS as recommended by the TEG is intended for any type of issuer: listed or non-listed, public or private, European or international. Do you envisage any issues for non-European issuers to follow the proposed standard by the TEG?

- ✓ **Yes**
- No
- Do not know
- If necessary, please specify the reasons for your answer [BOX 2000 characters

Prospectus and green bonds

Question 25: In those cases where a prospectus has to be published, do you believe that requiring the disclosure of specific information on green bonds in the prospectus, which is a single binding document, would improve the consistency and comparability of information for such instruments and help fight greenwashing?

Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree)

1	2	3	4	5

If necessary, please specify the reasons for your answer [BOX, 2000 characters]

Disclosure of standardized and intelligible information is essential to guarantee comparability among sustainable products in general. In case of products targeted at individual investors, the prospectus needs to disclose essential information that allows to understand the main sustainability features of the product.

Question 26: In those cases where a prospectus has to be published, to what extent do you agree with the following statement:

"Issuers that adopt the EU GBS should include a link to that standard in the prospectus instead of being subject to specific disclosure requirements on green bonds in the prospectus"

Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree)

~~1~~	2	3	4	5

If necessary, please specify the reasons for your answer [BOX]

Disclosure for individual investors must be at all times **simple, short, clear, avoiding jargon, not misleading and comparable.** To be simple, short and concise, it must focus only on key elements that can and should guide the financial decision making of an average investor. To be comparable, it must reach the highest degree of standardisation at a cross-sectoral levels and standardisation concerns not only the type of information to be included, but also the order flow and format; in other words, it must exhibit the same structure. Therefore, standardised information should be provided in the prospectus and not via a link in the prospectus as information included in marketing communication material as brochure, factsheet etc is not regulated and does not provide comparability.

Other standards and labels

Already now, the Disclosure Regulation defines two categories of sustainable investment products: those promoting environmental or social characteristics and those with environmental or social objectives, the latter being defined as 'sustainable investments'. Both types of products have to disclose their use of the EU Taxonomy, for the environmental portion of the product.

Question 27: Do you currently market financial products that promote environmental characteristics or have environmental objectives?

- Yes
- No
- Do not know

If yes, once the EU Taxonomy is established,[21] how likely is it that you would use the EU Taxonomy in your investment decisions (i.e. invest more in underlying assets that are partially

[21] Assuming that for climate change mitigation and adaptation, it would be based on the recommendations of the TEG for the EU taxonomy.

or fully aligned with the EU Taxonomy)? Please use a scale of 1 (not likely atall) to 5 (very likely).

1	2	3	4	5

Please specify if necessary [box, 2000 characters]

Question 28: In its final report, the High-Level Expert Group on Sustainable Finance recommended to establish a minimum standard for sustainably denominated investment funds (commonly referred to as ESG or SRI funds, despite having diverse methodologies), aimed at retail investors. What actions would you consider necessary to standardise investment funds that have broader sustainability denominations?

- No regulatory intervention is needed.
- The Commission or the ESAs should issue guidance on minimum standards.
- ✓ ***Regulatory intervention is needed to enshrine minimum standards in law.***
- Regulatory intervention is needed to create a label.

Question 29: Should the EU establish a label for investment funds (e.g. ESG funds or green funds aimed at professional investors)?

- **Yes**
- No
- Do not know.

If necessary, please explain your answer [BOX, 2000 characters]

If yes, regarding green funds aimed at professional investors, should this be in the context of the EU Ecolabel?

- ✓ **Yes**
- No
- Do not know

If necessary, please explain your answer [BOX, 2000 characters]

We believe that the Ecolabel should be open also for professional AIFs (like in the case of Austrian ecolabel). This would facilitate to increase the scope and the target market of the ecolabel. However, for these specific products a prominent warning for individual investors esp. regarding costs must be included: If an Ecolabel retail fund invests in an Ecolabel professional AIF, it will generate two layers of fees for the EU saver: the retail fund ones plus the AIF's ones. The total costs have to be clearly disclosed to the saver, which is the case currently for UCITs funds, but not the case when the PRIIPS KID will replace the UCITS KIID in 2021. [22]

Question 30: The market has recently seen the development of sustainability-linked bonds and loans, whose interest rates or returns are dependent on the company meeting pre-determined sustainability targets. This approach is different from regular green bonds, which have a green use-of-proceeds approach. Should the EU develop standards for these types of sustainability-linked bonds or loans?

Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree).

1	2	3	4	~~**5**~~

If necessary, please explain. [BOX, 2000 characters]

These sustainability bonds and loans would be encouraged as they have a much higher potential to have a real impact on ESG factors than the "use-of-proceeds approach".

Question 31: Should such a potential standard for target-setting sustainability-linked bonds or loans make use of the EU Taxonomy as one of the key performance indicators?

Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree).

1	2	3	4	5

If necessary, please explain. [BOX, 2000 characters]

Question 32: Several initiatives are currently ongoing in relation to energy-efficient mortgages[23] and green loans more broadly. Should the EU develop standards or labels for these types of products?

✓ **Yes**

[22] BETTER FINANCE's feedback to the EC Consultation on the Development of EU Ecolabel criteria for Retail Financial Products : https://betterfinance.eu/publication/better-finances-feedback-to-the-ec-consultation-on-the-development-of-eu-ecolabel-criteria-for-retail-financial-products/

[23] See for instance the work of the EEFIG (Energy Efficiency Financial Institutions Group set by the EC and the United Nations Environment Program Finance Initiative or UNEP FI) on the financial performance of energy efficiency loans or the energy efficient mortgages initiatives.

- No
- Do not know.

If yes, please select all that apply:

- ✓ **a broad standard or label for sustainable mortgages and loans (including social and environmental considerations);**

- a standard or label for green (environmental and climate) mortgages and loans;

- a narrow standard or label only for energy-efficient mortgages and loans for the renovation of a residential immovable property;

- other: please specify what type of standard or label on sustainability in the loan market you would like to see [BOX, 2000 characters]

Question 33: The Climate Benchmarks Regulation creates two types of EU climate benchmarks - 'EU Climate Transition' and 'EU Paris-aligned' - aimed at investors with climate-conscious investment strategies. The regulation also requires the Commission to assess the feasibility of a broader 'ESG benchmark'. Should the EU take action to create an ESG benchmark?

- Yes
- ✓ **No**
- Do not know

If no, please explain the reasons for your answer, if necessary. [BOX, 2000 characters]

BETTER FINANCE believes that competent authorities should have explicit and defined powers to verify that an investment firm, UCITS management company or alternative fund manager complies with the requirements of the Regulation. In addition, competent authorities must have the power (and use it) to verify that the investment strategy is in line with the minimum standards of the climate related benchmarks.

If on the one hand climate related benchmarks can be useful for retail investors to observe the alignment of the investment strategy to climate related indictors on the other hand BETTER FINANCE, once again warns against the use of these Benchmarks with regard to individual nonprofessional investors. We believe that what individual investors need are clear, fair and not misleading (in the sense of Mifid II) mainstream capital markets' benchmarks ("standard indices" as the EC calls them) allowing them to easily assess the performance of different funds against the same benchmark. We already pointed out the need to measure and clearly inform EU savers about the impact of applying ESG criteria on the actual long-term real performance by allowing for the comparison between the actual performance and the corresponding mainstream capital markets' benchmarks.

ESG products must benchmark themselves against objective mainstream benchmarks to allow to check if their ESG approach made any difference over the long term (it would be impossible if the funds are using only climate related benchmarks instead and if they created any long-term value for EU savers. The Key Information Document must refer to - and disclose a mainstream benchmark in order to be intelligible, which is a legal requirement from the MiFID Directive: information must be intelligible to the majority of people to whom it is targeted. Mainstream benchmarks are already poorly explained to end investors and not easily understood by them, thus violating MiFID II rules on "clear" and "not misleading" information. It will be worse with even more complex, numerous and diverse benchmarks that include specific and technical climate/environmental standards.

See also BETTER FINANCE response to the EC Public consultation on the "Review of the EU benchmark regulation

If yes, please explain what the key elements of such a benchmark should be. [BOX max. 2000 characters]

Question 34: Beyond the possible standards and labels mentioned above (for bonds, retail investment products, investment funds for professional investors, loans and mortgages, benchmarks), do you see the need for any other kinds of standards or labels for sustainable finance?

- ✓ **Yes**
- No
- Do not know

If yes, what should they cover thematically and for what types of financial products? [box max. 2000 characters]

BETTER FINANCE regrets that the Commission did not consider creating an Ecolabel based on impact investing, i.e. a specific investment strategy that uses indicators to measure and assess the environmental /social impact of the investment.

Even if several sustainable products have misleading impact claims, we see that there can be a big potential of this type of sustainable strategy. Therefore, the setting of criteria for impact investing can be extremely important to create a common definition of a sustainable product that effectively delivers an environmental impact.

The Ecolabel captures the investments funds that use traditional positive and negative screening in their investment policies which are far from providing any concrete environmental or social impact.

This is the reason why we call for a review of the Ecolabel in 2023 allowing to design a new type of Ecolabel that would set new market practice on impact investing.

In addition, BETTER FINANCE would like to warn against the use of some definitions and claims. The technical report continues using the exposure to green activities as a proxy for the environmental impact of the asset management service. This claim could be extremely misleading as there is no evidence that exposure to green activities would generate any significant impact.

As these products are exchanged in the secondary market, they have very little impact (or none) on the companies in which they invest. The only instrument that could be used (in theory) to generate and assess the impact of the Ecolabel is engagement. But the EU Ecolabel, as designed at the moment, lacks specific targets and monitoring. [24]

1.5 Capital markets infrastructure

The recent growth in the market for sustainable financial instruments has raised questions as to whether the current capital markets infrastructure is fit for purpose. Having an infrastructure in place that caters to those types of financial instruments could support and further enhance sustainable finance in Europe.

Question 35: Do you think the existing capital market infrastructure sufficiently supports the issuance and liquidity of sustainable securities?

Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree).

1	~~2~~	3	4	5

For scores of 1 and 2, please list the main problems you see (maximum three). [BOX, 2000 characters].

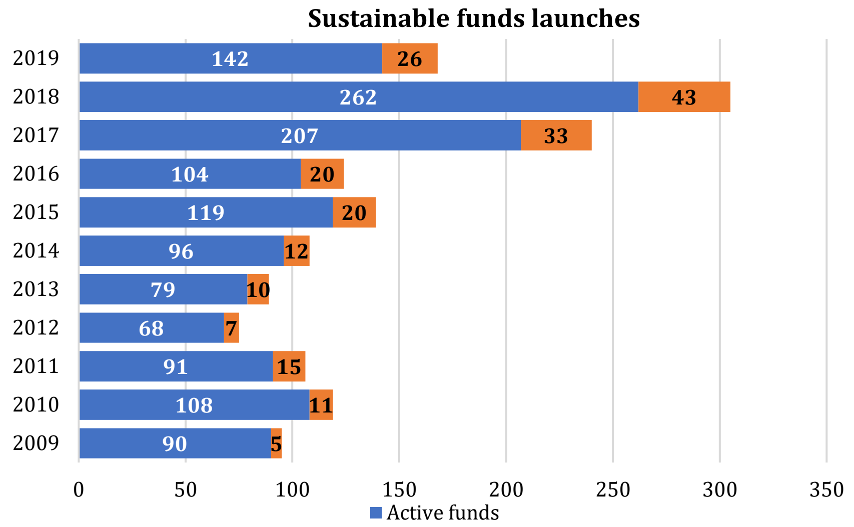
European landscape: The increasing demand of these type of investments has led asset managers to take advantage of this by integrating ESG considerations into their investment process.[25] Converting conventional funds into sustainable would require implementing specific changes on the investment policy and portfolio composition of the fund.[26] According to Morningstar, the biggest increase in number of converting conventional funds into sustainable took place in the period 2017-2018. [27] **On the other hand already existing mainstream funds have been turned or renamed into "sustainable" funds without making relevant changes in the**

[24] BETTER FINANCE's feedback to the EC Consultation on the Development of EU Ecolabel criteria for Retail Financial Products : https://betterfinance.eu/publication/better-finances-feedback-to-the-ec-consultation-on-the-development-of-eu-ecolabel-criteria-for-retail-financial-products/

[25] https://www.morningstar.com/en-uk/lp/sustainable-funds-landscape
[26] *Ibid.*
[27] *Ibid.*

portfolio holdings and the investment policy. [28] In order to avoid these practices specific regulatory standards on sustainable financial products such as a complete taxonomy, that includes not only the environmental dimension but also social and governance, and regulatory standards would streamline the market practices providing a common definition of sustainable investments.

According to Morningstar, in the first half of 2019 the launch of new sustainable funds accounted to 168 out of which 26 are passive funds and 142 active funds (table below).[29]



Source: *Morningstar European Sustainable fund landscape. *2019: period from 01/01/2019 to 30/06/2019*

Despite their rapid growth, ESG funds represent **less than 2% of the overall European retail funds market.[30] Yet very few retail investors currently have the opportunity to invest according to their ESG preferences.** For this market the offer doesn't match the increasing demand of retail investors that want to invest in more green and sustainable financial products.

The main objective of the renewed sustainable finance strategy needs to reflect a reorientation of capital flow into real economy investments and activities. This would not be possible if the new framework allows to target an already existing number of financial products with misleading environmental, social and governance claims. Sustainable investing should not become a marketing gimmick. It would be possible to reorient capital flows towards sustainable investment in order to achieve sustainable and inclusive growth only if new products with high standards are created.

Question 36: In your opinion, should the EU foster the development of a sustainable finance-oriented exchange or trading segments that caters specifically to trading in sustainable finance securities and is better aligned with the needs of issuers?

- **Yes**
- No

[28] *Ibid.*
[29] *Ibid.*
[30] https://ec.europa.eu/info/sites/info/files/180131-sustainable-finance-final-report_en.pdf

- Do not know.

If necessary, please explain the reasons for your answer. [BOX max. 2000 characters]

The creation of exchange or trading segments for sustainable finance securities could facilitate to identify and exchange sustainable investments as long as a common definition of sustainable investments and ESG factoring is adopted.

Question 37: In your opinion, what core features should a sustainable finance–oriented exchange have in order to encourage capital flows to ESG projects and listing of companies with strong ESG characteristics, in particular SMEs?

[BOX max. 2000 characters]

As first it is necessary to increase SMEs participation in Capital Market. Even though the availability of funding through banks and equity issuance has significantly increased significantly increased over the period 2014-2018 (from 4 to 14%), it is still at a very low level.

Facing difficulties to obtain finance and high compliance costs, coupled with a drop in risk equity research,[31] caused the number of publicly listed SMEs companies to fluctuate and, overall, decrease from 2014 (1180) to 2018 (1137), with the market capitalization of their shares dropping dramatically from €122.1 billion to €53.45 billion in 2018 (-56%).

In the EU, IPOs have been "*moderate and rather volatile over time and barely exist for SMEs*".[32] Public listing, for the purpose of raising capital through equity or corporate bond issuance, may prove very costly and not profitable for SMEs, considering their income volatility[33] and the fact that a high number of SMEs (cca. 200,000) go bankrupt annually.[34]

Chart 15. Number of IPOs per year

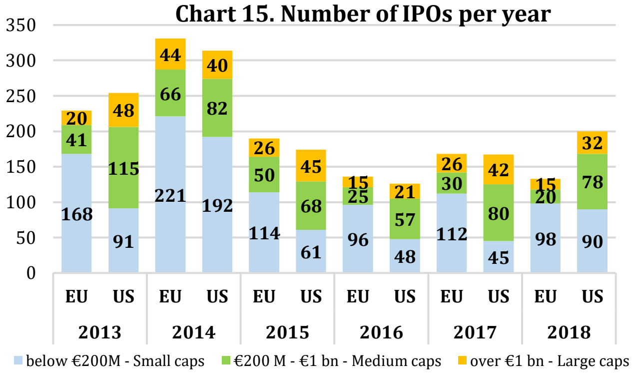
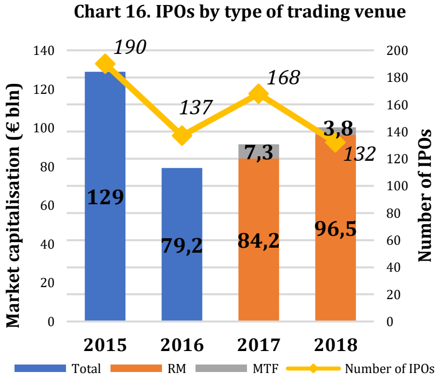


Chart 16. IPOs by type of trading venue



[31] See CFA Institute, *MiFID II – A New Paradigm for Investment Research: Investor Perspectives on Research Costs and Procurement* (2017) https://www.cfainstitute.org/-/media/documents/support/advocacy/mifid_ii_new-paradigm-for-research-report.ashx; see also Elizabeth Pfeuti, 'MiFID II Research Rules "Hitting Sector Coverage and Quality"' (18 February 2019, IPE.com), last accessed 3 November 2019, available at https://www.cfainstitute.org/-/media/documents/support/advocacy/mifid_ii_new-paradigm-for-research-report.ashx.

[32] Apostolos Thomadakis, 'Developing EU Capital Markets for SMEs: Mission Impossible?' 46 (4 September 2017) European Capital Markets Institute Commentary, p. 2.

[33] Ibid.

[34] EESC Opinion (n 43), p. 5.

The IPOs taking place on RMs totalled €96.5 billion (1st trading day) in 2018. The size of the EU public equity market has grown over the past 9 years but in favour of institutional financial and corporate investors (domestic and foreign). The smaller EU businesses have not profited from the pooling of capital into the EU economy.

Therefore, the number of SMEs and start-ups going public has decreased in the EU. The SME and IPO markets are still underdeveloped compared to those in the US and Asia. In addition, with many Eastern European markets lagging behind, equity trading in the EU is concentrated in a handful of trading venues in Western Europe.

For additional information see BETTER FINANCE CMU Assessment report 2015-2019.

Small and medium-sized enterprises are essential to Europe's competitiveness and prosperity. Despite the benefits of public listings, EU markets struggle to attract new issuers. Therefore, in order to encourage capital flows to ESG projects and listing of SMEs, it is necessary as first:

- **To increase the attractiveness of EU stock exchanges** for EU SMEs in general, e.g. through tax incentives. EU stock markets are still struggling to attract IPOs and London is still the most important market for IPOs in the EU. The Commission should build on the experience and expertise built up in well-established capital markets to find out how to make EU stock exchanges more attractive.
- **To strengthen the IPO market in Continental Europe**. The Commission should review the regulatory barriers to small firms for their admission to trading on public markets to ensure that the regulatory environment for the SME Growth Markets is fit for purpose.

1.6 Corporate governance, long-termism and investor engagement

To reflect long-term opportunities and risks, such as those connected to climate change and environmental degradation, ***companies and investors need to integrate long-term horizons and sustainability in their decision-making processes****. However, this is often difficult in a context where market pressure and prevailing corporate culture prompt corporate managers and financial market participants to focus on near-term financial performance at the expense of mid- to long-term objectives. Focusing on short-term returns without accounting for long-term implications may lead to underperformance of the corporation and investors in the long-term, and, by extension, of the economy as a whole. In this context, investors should be driving long-termism, where this is relevant, and not pressure companies to deliver short-term returns by default.*

The ongoing COVID-19 outbreak in particular underscores that companies should prioritise the long term interests of their stakeholders*. Many companies in the EU have decided to prioritise the interests of key stakeholders, in particular employees, customers and* *suppliers, over short-term shareholder interest.*[35] *These factors contribute to driving long-term returns as they are crucial in order to maintain companies' ability to operate. Therefore, institutional investors have an important role to play in this context. As part of action 10 of the Action Plan on Financing Sustainable Growth, in December 2019 the* ***European Supervisory Authorities delivered reports (ESMA report, EBA report, EIOPA report) that had the objective of assessing evidence of undue short-term pressure from the financial sector on corporations****. They identified areas within their remit where they found some degree of short-termism and issued policy recommendations accordingly. For instance, they advise the adoption of longer-term perspectives among financial institutions through more explicit legal provisions on sustainability.*

Question 38: In your view, which recommendation(s) made in the ESAs' reports have the highest potential to effectively tackle short-termism? Please select among the following options.

- ✓ **Adopt more explicit legal provisions on sustainability for credit institutions, in particular related to governance and risk management;**

- ✓ **Define clear objectives on portfolio turn-over ratios and holdings periods for institutional investors;**

- Require Member States to have an independent monitoring framework to ensure the quality of information disclosed in remuneration reports published by listed companies and funds (UCITS management companies and AIFMs);

- Other, please specify. [box max. 2000 characters]

Question 39: Beyond the recommendations issued by the ESAs, do you see any barriers in the EU regulatory framework that prevent long-termism and/or do you see scope for further actions that could foster long-termism in financial markets and the way corporates operate?

- ✓ **Yes**
- No
- Do not know

If yes, please explain what action(s). [BOX max. 2000 characters]

[35] The European Central Bank also recommended on 27 March 2020 that significant credit institution refrain from distributing dividend so that "they can continue to fulfil their role to fund households, small and medium businesses and corporations" during the COVID-19 economic shock.

Further actions: With the current crisis calling for a tightening of the link between employees and their companies, especially in the case of SMEs, BETTER FINANCE's member organisation EFES, the European Federation of Employee Share Ownership, launched a concrete proposal[36]on how to co-opt **Employee Share Ownership (ESO)** to help fund companies under threat of bankruptcy from the pandemic and complement governments in their struggle against the fallout from the crisis.

The proposal is aimed at developing a generic European ESOP model as a Pension Plan, to be adapted to the specific legal and tax specificities of each EU Member State upon rolling out. Such a long-term employee shareholding plan would benefit from a clever financing model, based on an original tax system, thereby allowing the ESOP model to supersede all other existing employee shareholding formulas used by SMEs. ESO can play a crucial role in increasing the resilience of businesses and reduce employment-fluctuation in times of economic crisis.[37]

BETTER FINANCE believes Employee Share Ownership (ESO) to be crucial in addressing the impending Covid19 financial crisis, but also key for the success of the Capital Markets Union (CMU) and of any sustainable finance strategy by reacquainting EU Citizens with equities as the financial instrument most likely to protect the real value of their lifetime financial savings over the long-term. Indeed, ESO has a proven and direct link to increased financial literacy and knowledge about equities and capital markets, since the workplace is the only independent way for adults to get educated on equity investment, equity ownership and related engagement responsibilities, and capital markets. Studies also show that companies with a significant ESO are more focused on sustainability issues and are more resilient in terms of employment and salary levels during crisis.

Crucially, ESO leads to **an increased long-term engagement of employee shareholders with a stronger focus on sustainability and improving the corporate governance of the companies they are invested in**, since employee-owned companies tend towards increased responsibility and hold their immediate environment in higher regard, because they internalise the externalities.[38] This however only if employees can vote their shares individually and those shares are not voted (like very often in France) through bodies in which the company management is involved and can exercise influence on the voting decision.

For additional information see our press release: [BETTER FINANCE urges to put Employee Share Ownership at the core of efforts to tackle the Corona-induced financial crisis]

Biased investment "advice" at the retail points of sale must be eliminated to enable actual access of EU savers to equity investments. Also, EU Authorities must at last eliminate the barriers to the engagement of EU citizens as shareholders towards more sustainability of investee companies. This implies to have an EU-wide definition of "shareholder" to ensure

[36] Proposal Employee share ownership against the crisis http://www.efesonline.org/corona/EN.htm
[37] David P. Ellerman & Tej Gonza, "COVID-19: Government Aid that also promotes Employee Ownership"
[38] Ibid.

that the actual shareholders can exercise their voting rights , instead of financial intermediaries ("other people's money") as it is very often the case for cross-border voting within the EU. And - in the XXIst century – it is about time the EU develops a plan to enable EU citizens to exercise their voting rights on their smart phones.

*The Shareholder Rights Directive II states that **directors' variable remuneration** should be based on both financial and non-financial performance, where applicable. However, there is currently no requirement regarding what the fraction of variable remuneration should be linked to, when it comes to non-financial performance.*

Question 40: In your view, should there be a mandatory share of variable remuneration linked to non-financial performance for corporates and financial institutions?

- ✓ **Yes**
- No
- Do not know

If yes, please indicate what share. [box 2000 characters]

BETTER FINANCE acknowledges the existence of disproportionate remuneration of some directors in some of the big listed EU companies. For this reason, we consider that the establishment of renumeration caps for directors is necessary. The maximum remuneration should be adopted for base salaries and as well for variable remunerations. Therefore, the same considerations should apply with mandatory share of variable remuneration linked to non-financial performance.

KPIs

We would support incorporating robust governance, social and relevant climate risk metrics in the Key Performance Indicators used to calculate long term remuneration for senior executives. We believe that being aware that remuneration can be affected can help effectively change the optics and behaviour of executives.

Question 41: Do you think that a defined set of EU companies should be required to include carbon emission reductions, where applicable, in their lists of ESG factors affecting directors' variable remuneration?

- ✓ **Yes**
- No
- Do not know

*The Shareholder Rights Directive II introduces **transparency requirements** to better align long-term interests between institutional investors and their asset managers.*

Question 42: Beyond the Shareholder Rights Directive II, do you think that EU action would be necessary to further enhance long-term engagement between investors and their investee companies?

- ✓ **Yes**
- No
- Do not know

If yes, what action should be taken? Please explain or provide appropriate examples. [BOX max. 2000 characters]

Oversight of boards: Supervisory boards/(non-executives on the) boards of directors oversee the performance/strategy of management. It is crucial and considered as good governance that members of the boards are knowledgeable, diverse, independent (sufficient number of independent members) and not overly burdened with other mandates (so called overboarding). The supervisory board members/non executive BoD members representing shareholders are appointed by the general meeting, therefore the nomination process should be transparent for shareholders in advance of the vote to be held on the election of a board member.

The auditor of a company should likewise be independent. A regular audit rotation and transparency of the audit tender process is part of good governance. In addition, there should be a separation of non-audit and audit services. Also, given the Wirecard case, there is the need for a greater emphasis on forensic accounting (in order to detect fraud). Also, the liability cap at auditors, for example in Germany, is currently restricted to 4 million EUR and only in case of deliberate intention. This cap needs to be lifted and extended to gross negligence.

Increased dialogue between investors and issuers is necessary to hold the boards' to account. They have to explain their actions and may reconsider if they find out that the majority of their owners is not in favour of a certain measures. The problem is that direct ownership is more and more decreasing while indirect ownership via funds or ETFs is increasing. This intermediated ownership has led to a lack of oversight as many institutional investors (asset managers) do not (fully) exercise the voting rights of the shares they hold in their portfolios. SRD II only requires transparency on how institutional investors engage. They should be required to engage and to exercise of voting rights.

Question 43: Do you think voting frameworks across the EU should be further harmonised at EU level to facilitate shareholder engagement and votes on ESG issues?

- ✓ **Yes**
- No
- Do not know

Question 44: Do you think that EU action is necessary to allow investors to vote on a company's environmental and social strategies or performance?

- ✓ **<u>Yes</u>**
- No
- Do not know

If yes, please explain. [BOX max. 2000 characters]

The transparency requirements of the SRD II on both asset managers and proxy advisers could be improved or expanded to more granular duties under the Sustainable Finance Agenda. It is important to guarantee the rights of investors to exercise their rights in the lead-up to further revisions. The exercise of these rights is a key prerequisite for the allocation of capital towards sustainable companies.

This should be also an obligation for institutional investors to exercise their voting rights. "The EU Shareholder Rights Directive should clarify rights and intensify obligations of institutional investors to actively engage in the decision-making process of investee companies.

Also, the common shareholder definition would be helpful here or at least the abolition of nominee accounts.

Questions have been raised about whether passive index investing could lower the incentives to participate in corporate governance matters or engage with companies regarding their long term strategies.

Question 45: Do you think that passive index investing, if it does not take into account ESG factors, could have an impact on the interests of long-term shareholders?

- Yes
- ✓ **<u>No</u>**
- Do not know

If no, please explain the reasons for your answer if necessary. [BOX max. 2000 characters]

BETTER FINANCE believes that indexed asset management that does not take into account ESG factors does not have a negative impact per se. Index asset managers hold the shares for a much longer time than "active" ones (average turnover for those is less than one year, making it in reality impossible to seriously and effectively engage with the investee companies). So index managers are in a much better position to engage with investee companies to reach long term sustainable goals. Nonetheless, it is important to disclose relevant information to individual investors regarding the risk associated to index products that incorporate/or not ESG factors, and to the engagement policy and results of the index manager, in particular with regard to ESG factors.

Having said that, we believe there are meaningful ways in which passive investors can carry out effective stewardship.[39]

If yes, in your view, what do you think this impact is, do you think that the EU should address it and how? [box max. 2000 characters]

See above

To foster more sustainable corporate governance, as part of action 10 of the 2018 Action Plan on Financing Sustainable Growth, ***the Commission launched a [study on due diligence](#)*** *(i.e. identification and mitigation of adverse social and environmental impact in a company's own operations and supply chain), which was published in February 2020. This study indicated the need for policy intervention, a conclusion which was supported by both multinational companies and NGOs. Another study on directors' duties and possible sustainability targets will be finalised in Q2 2020.*

Question 46: Due regard for a range of 'stakeholder interests', such as the interests of employees, customers, etc., has long been a social expectation vis-a-vis companies. In recent years, the number of such interests have expanded to include issues such as human rights violations, environmental pollution and climate change. Do you think companies and their directors should take account of these interests in corporate decisions alongside financial interests of shareholders, beyond what is currently required by EU law?

- Yes, a more holistic approach should favour the maximisation of social, environmental, as well as economic/financial performance.
- ✓ **Yes, as these issues are relevant to the financial performance of the company in the long term.**
- No, companies and their directors should not take account of these sorts of interests.
- I do not know.

Question 47: Do you think that an EU framework for supply chain due diligence related to human rights and environmental issues should be developed to ensure a harmonised level-playing field, given the uneven development of national due diligence initiatives?

- ✓ **Yes**
- No
- Do not know

[39] https://shareaction.org/wp-content/uploads/2020/03/Point-of-no-Returns.pdf

Question 48: Do you think that such a supply chain due diligence requirement should apply to all companies, including small and medium sized companies?

- ✓ **Yes**
- No
- Do not know

If yes, please select your preferred option:

- All companies, including SMEs.
- ✓ **All companies, but with lighter minimum requirements for SMEs.**
- Only large companies in general, and SMEs in the most risky economic sectors sustainability-wise.
- Only large companies.

If necessary, please explain the reasons for your answer. [box max. 2000 characters]

2. Increasing opportunities for citizens, financial institutions and corporates to enhance sustainability

Increased opportunities need to be provided to citizens, financial institutions and corporates in order to enable them to have a positive impact on sustainability. *Citizens can be mobilised by providing them with opportunities to invest their pensions and savings sustainably or by using digital tools to empower them to make their communities, their homes and their businesses more resilient. Financial institutions and corporates can increase their contribution to sustainability if the right policy signals and incentives are in place. Furthermore, international cooperation and the use of sustainable finance tools and frameworks in developing countries can help build a truly global response to the climate and environmental crisis.*

As part of the European Green Deal, the Commission has launched a European Climate Pact *to bring together regions, local communities, civil society, businesses and schools in the fight against climate change, incentivising behavioural change from the level of the individual to the largest multinational, and to launch a new wave of actions. A consultation on the European Climate Pact is open until 27 May 2020 in order to better identify the areas where the Commission could support and highlight pledges as well as set up fora to work together on climate action (including possibly on sustainable finance).*

2.1 Mobilising retail investors and citizens

Although retail investors today are increasingly aware that their own investments and deposits can play a role in achieving Europe's climate and environmental targets, they are not always offered sustainable financial products that match their expectations. In order to ensure that the *sustainability preferences of retail investors are truly integrated in the financial system, it is crucial to help them to better identify which financial products best correspond to these preferences, providing them with user-friendly information and metrics they can easily understand. To that end, the European Commission will soon publish the amended delegated acts of MIFID II and IDD, which will require investment advisors to ask retail investors about their sustainability preferences.*

Question 49: In order to ensure that retail investors are asked about their sustainability preferences in a simple, adequate and sufficiently granular way, would detailed guidance for financial advisers be useful when they ask questions to retail investors seeking financial advice?

- ✓ **Yes**
- No
- Do not know

If necessary, please provide an explanation of your answer. [box max. 2000 characters]

Questions regarding sustainability preferences should not be a "tick the box" job for financial adviser. Guidelines on simple, adequate and sufficient granular question should be asked to retail investors.

Question 50: Do you think that retail investors should be systematically offered sustainable investment products as one of the default options, when the provider has them available, at a comparable cost and if those products meet the suitability test?

- ✓ **Yes**
- No
- Do not know

Question 51: Should the EU support the development of more structured actions in the area of financial literacy and sustainability, in order to raise awareness and knowledge of sustainable finance among citizens and finance professionals? Please reply using a scale of 1 (completely disagree) to 5 (fully agree)

If you agree (for scores of 4 to 5), please choose what particular action should be prioritised:

Integrate sustainable finance literacy in the training requirements of finance professionals. [1-5]

1	2	3	4	~~5~~

Stimulate cooperation between Member States to integrate sustainable finance as part of existing subjects in citizens' education at school, possibly in the context of a wider effort to raise awareness about climate action and sustainability. [1-5]

1	2	3	4	5

Beyond school education, stimulate cooperation between Member States to ensure that there are sufficient initiatives to educate citizens to reduce their environmental footprint also through their investment decisions. [1-5]

1	2	3	4	5

Directly, through targeted campaigns. [1-5]

1	2	3	4	5

As part of a wider effort to raise the financial literacy of EU citizens. [1-5]

1	2	3	4	5

As part of a wider effort to raise the knowledge citizens have of their rights as consumers, investors, and active members of their communities. [1-5]

1	2	3	4	5

Promote the inclusion of sustainability and sustainable finance in the curricula of students, in particular future finance professionals. [1-5]

1	2	3	4	5

Other, please explain.[box max. 2000 characters]

Especially financial advisers need to be trained on ESG issues and this should also be mandatorily included in the qualification requirements and continuing education for financial advisers.

2.2 Better understanding the impact of sustainable finance on sustainability factors

While sustainable finance is growing, there are questions on how to measure and assess the positive impact of sustainable finance on the real economy*. Recently, tools have been developed that can be used to approximate an understanding of the climate and environmental impact of economic activities that are being financed. Examples of such tools include the EU Taxonomy, which identifies under which conditions economic activities can be considered environmentally sustainable, use-of-proceeds reporting as part of green bond issuances, or the Disclosure Regulation, which requires the reporting of specific adverse impact indicators.*

Yet, an improved understanding of how different sustainable financial products impact the economy may further increase their positive impact on sustainability factors and accelerate the transition.

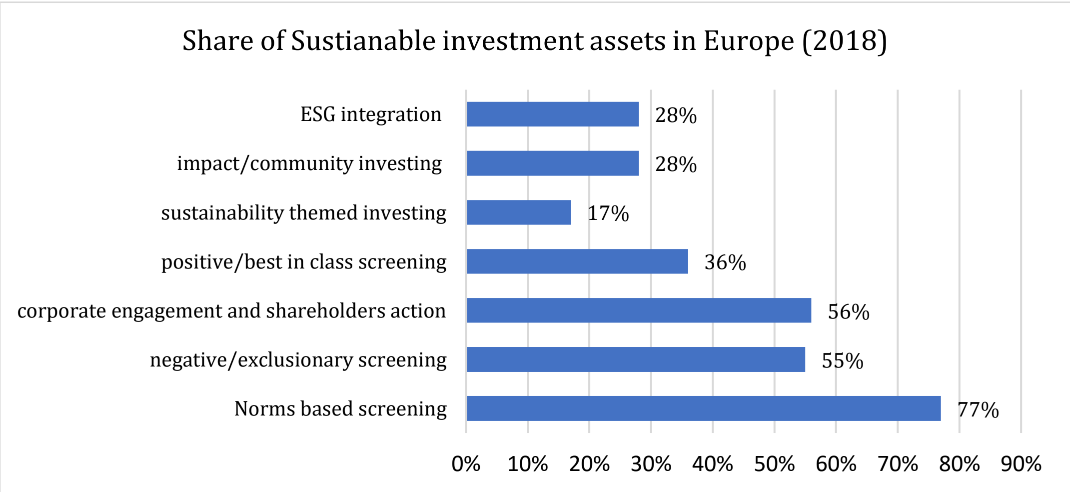
Question 52: In your view, is it important to better measure the impact of financial products on sustainability factors?

Please express your view by using a scale of 1 (not important at all) to 5 (very important).

1	2	3	4	5

For scores of 4 to 5, what actions should the EU take in your view? [BOX max. 2000 characters]

The Renewed Sustainable Finance Strategy should develop a scheme that allow to measure the impact of sustainable investments as the EU Eco-management and audit scheme (EMAS)[40] for companies. The scheme should develop indicators and techniques that allow to evaluate and report the environmental, social performance of sustainable investments.



Source: Statista (publicly available data)

As represented, in the table above, impact investing accounts only for a small share (28%)[41] of the European market compared to the other investment strategies. Although, at the moment several market practices use impact claims as a marketing gimmick for retail investment products, impact investing has the potential to allocate capital to sustainable projects that have impact in the real economy. Effective and reliable impact investments can measure the non-financial impact of the investment.

In addition, the Commission should consider developing an EU Ecolabel that is designed for impact investing. This would provide a strong incentive to push impact investments in the market that deliver reliable and measurable impact in the real economy.

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[40] https://ec.europa.eu/environment/emas/index_en.htm

[41] https://www.statista.com/statistics/718164/european-share-of-global-socially-responsible-investment-assets-strategy/

Question 53: Do you think that all financial products / instruments (e.g. shares, bonds, ETFs, money market funds) have the same ability to allocate capital to sustainable projects and activities?

- Yes
- ✓ **No**
- Do not know

If no, please explain what you would consider to be the most impactful products/instruments to reallocate capital in this way.[box max. 2000 characters]

Different types of investment products combined with different sustainable investment strategies provide very different results in allocating capital to sustainable projects. For example, green bonds have higher ability to finance specific green projects compared to equities. In addition, there are no evidence that sustainable investment funds that uses negative screening techniques will produce an environmental impact. Therefore, the setting of criteria for impact investing can be extremely important to create a common definition of sustainable products that effectively deliver an environmental impact.

2.3 Green securitisation

Securitisation is a technique that converts illiquid assets, such as bank loans or trade receivables, into tradeable securities. As a result, banks can raise fresh money as well as move credit risk out of their balance sheets, thereby freeing up capital for new lending. Securitisation also facilitates access to a greater range of investors, who can benefit from the banks' expertise in loan origination and servicing, thereby diversifying risk exposure. Green securitisations and collaboration between banks and investors could play an important role in financing the transition as banks' balance sheet space might be too limited to overcome the green finance gap. The EU's new securitisation framework creates a specific framework for high-quality Simple, Transparent and Standardised (STS) securitisations, together with a more risk-sensitive prudential treatment for banks and insurers.

Question 54: Do you think that green securitisation has a role to play to increase the capital allocated to sustainable projects and activities?

Please express your view by using a scale of 1 (not important at all) to 5 (very important).

1	2	**3**	4	5

If necessary, please explain your answer. [box, max. 2000 characters]

Green securitisation is the process of transforming illiquid assets (loans and leases on assets such as electric cars, solar panels certified buildings) into securities or tradable financial assets also called green asset-backed securities (ABS). These securities are then sold to investors which in turn can trade them on the secondary market. Consequently, freed up capital can be used to for additional green lending but also for non-green lending projects which in turn can be packaged into green ABS.

The main issues with green securitisation are the following:

1- There is not yet a clear definition of green projects. In the near future, only the taxonomy provides a classification of green activities, but its scientific justification (actual positive impact on the environment) is sometimes questionable, and its application is not binding.
2- Due to its complex nature, securitisation can involve multiple underlying assets for which is difficult to assess which one should be considered for the sustainability assessment.
3- Green assets can end up to finance non-green assets thus increasing the risk of green washing.
4- The general process of securitisation has had a central role in the 2008 financial crisis. The wide and uncontrolled use of securitisation to elude capital requirements could increase the systemic risk in the financial system.

However well-defined scopes of eligible "green" securitization should be further assessed for standardized asset categories (e.g. electric cars) provided they replace less environment friendly assets (e..g. fossil fueled cars).

Question 55: Do the existing EU securitisation market and regulatory frameworks, including prudential treatment, create any barriers for securitising 'green assets' and increasing growth in their secondary market?

- Yes
- No
- ✓ **Do not know**

If yes, please list the barriers you see (maximum three). [BOX max. 2000 characters]

Question 56: Do you see the need for a dedicated regulatory and prudential framework for 'green securitisation'?

- ✓ **Yes**
- No

- Do not know

If yes, what regulatory and/or prudential measures should the dedicated framework contain and how would they interact with the existing general rules for all securitisations and specific rule for STS securitisations? [box max. 2000 characters]

See previous reply above. Specific requirements should be applied in order to avoid that green assets are used to finance non-green assets thus preventing any risk of green washing.

2.4 Digital sustainable finance

The ongoing COVID-19 outbreak is highlighting the key role of digitalisation for the daily personal and professional lives of many Europeans. However, it has also revealed how digital exclusion can exacerbate financial exclusion – a risk that needs to be mitigated. Digitalisation is transforming the provision of financial services to Europe's businesses and citizens As shown in the Progress Report of the UN Secretary-General's Task Force on Digital Financing of the Sustainable Development Goals (SDGs), digital finance brings a wide array of opportunities for citizens worldwide by making it easier to make payments, save money, invest, or get insured. However, digital finance also brings new risks, such as deepening the digital divide. It is therefore paramount to ensure that the potential of digitalisation for sustainable finance is fully reaped, while mitigating associated challenges appropriately. In this context, the Commission has launched a consultation dedicated to digital finance.

In the area of sustainable finance, technological innovation such as Artificial intelligence (AI) and machine learning can help to better identify and assess to what extent a company's activities, a large equity portfolio, or a bank's assets are sustainable. The application of Blockchain and the Internet of Things (IoT) may allow for increased transparency and accountability in sustainable finance, for instance with automated reporting and traceability of use of proceeds for green bonds.

Question 57: Do you think EU policy action is needed to maximise the potential of digital tools for integrating sustainability into the financial sector?

- ✓ **Yes**
- No
- Do not know

If yes, what kind of action should the EU take and are there any existing initiatives that you would like the European Commission to consider? Please list a maximum of three actions and a maximum of three existing initiatives. [BOX max. 2000 characters]

In particular, digitalisation has the potential to empower citizens and retail investors to participate in local efforts to build climate resilience. For instance, M-Akiba is a Government of Kenya-issued retail bond that seeks to enhance financial inclusion for economic development. Money raised from issuance of M-Akiba is dedicated to infrastructural development projects, both new and ongoing.

Question 58: Do you consider that public authorities, including the EU and Member States should support the development of digital finance solutions that can help consumers and retail investors to better channel their money to finance the transition?

- Yes
- No
- Do not know

If yes, please explain what actions would be relevant from your perspective and which public authority would be best-positioned to deliver it. Please list a maximum of three actions [BOX max. 2000 characters]

Question 59: In your opinion, should the EU, Member States, or local authorities use digital tools to involve EU citizens in co-financing local sustainable projects?

- Yes
- No
- Do not know

If yes, please detail, in particular if you see a role for EU intervention, including financial support. [BOX max. 2000 characters]

2.5 Project Pipeline

The existing project pipeline (availability of bankable and investable sustainable projects) is generally considered to be insufficient to meet current investor demand for sustainable projects. Profitability of existing business models plays a role, with some projects (e.g. renewable energy), being more bankable than others (e.g. residential energy efficiency). Identifying the key regulatory and market obstacles that exist at European and national level will be key in order to fix the pipeline problem. Please note that questions relating to incentives are covered in section 2.6.

Question 60: What do you consider to be the key market and key regulatory obstacles that prevent an increase in the pipeline of sustainable projects? Please list a maximum three for each. BOX max. 2000 characters

Question 61: Do you see a role for Member States to address these obstacles through their NECPs (National Energy and Climate Plans)?

- Yes
- No
- Do not know

If necessary, please provide details. [box. Max. 2000 characters]

Question 62: In your view, how can the EU facilitate the uptake of sustainable finance tools and frameworks by SMEs and smaller professional investors? Please list a maximum of three actions you would like to see at EU-level

[BOX max. 2000 characters]

Question 63: The transition towards a sustainable economy will require significant investment in research and innovation (R&I) to enable rapid commercialisation of promising and transformational R&I solutions, including possible disruptive and breakthrough inventions or business models. How could the EU ensure that the financial tools developed to increase sustainable investment flows turn R&I into investable (bankable) opportunities?

[Box max. 2000 characters]

Question 64: In particular, would you consider it useful to have a category for R&I in the EU Taxonomy?

- Yes
- No
- Do not know

Question 65: In your view, do you consider that the EU should take further action in:

Bringing more financial engineering to sustainable R&I projects?
- Yes
- No

Assisting the development of R&I projects to reach investment-ready stages, with volumes, scales, and risk-return profiles that interest investors (i.e. ready and bankable projects that private investors can easily identify)?

- Yes
- No

Better identifying areas in R&I where public intervention is critical to crowd in private funding?

- Yes
- No

Ensuring alignment and synergies between Horizon Europe and other EU programmes/funds?

- Yes
- No

Conducting more research to address the high risks associated with sustainable R&I investment (e.g. policy frameworks and market conditions)?
- Yes
- No

Identifying and coordinating R&I efforts taking place at EU, national and international levels to maximise value and avoid duplication?

- Yes
- No

Facilitating sharing of information and experience regarding successful low-carbon business models, research gaps and innovative solutions?

- Yes
- No

Increasing the capacity of EU entrepreneurs and SMEs to innovate and take risks?

- Yes
- No

If necessary, please explain your answer. [Box max. 2000 characters]

2.6 Incentives to scale up sustainable investments

While markets for sustainable financial assets and green lending practices are growing steadily, they remain insufficient to finance the scale of additional investments needed to reach the EU's environmental and climate action objectives*, including climate-neutrality by 2050. For instance, companies' issuances of sustainable financial assets (bonds, equity) and sustainable loans currently do not meet investors' increasing interest. The objective of the European Green Deal Investment Plan, published on 14 January 2020, is to mobilise through the EU budget and the associated instruments at least EUR 1 trillion of private and public sustainable investments over the coming decade. The purpose of this section is to identify whether there are market failures or barriers that would prevent the scaling up of sustainable finance, and if yes what kinds of public financial incentives could help rectify this.*

Question 66: In your view, does the EU financial system face market barriers and inefficiencies that prevent the uptake of sustainable investments?

Please express your view on the current market functioning by using a scale of 1 (not well functioning at all) to 5 (functioning very well).

1	2	3	4	5

Please specify your answer. [BOX max. 2000 characters]

First of all, one of the main barriers to sustainable investing is the lack of long-term vision of the financial markets. Failure in adopting long-term drivers which include Environmental, social governance aspects, have an impact on the growth of sustainable investments.

Second of all, lack of standardised information, data and research on sustainability risks has increased complexity and a lack of common agreement on what is considered sustainable or not.

Question 67: In your view, to what extent would potential public incentives for issuers and lenders boost the market for sustainable investments?

Please express your view on the importance of financial incentives by using a scale of 1 (not effective at all) to 5 (very effective).

1	2	3	4	5

In case you see a strong need for public incentives (scores of 4 to 5), which specific incentive(s) would support the issuance of which sustainable financial assets, in your view? Please rank their effectiveness using a scale of 1 (not effective at all) to 5 (very effective).

Types of incentives	Bonds	Loans	Equity	Other
Revenue-neutral subsidies for issuers	3	3	3	
De-risking mechanisms such as guarantees and blended financing instruments at EU-level	2	2	2	
Technical Assistance	1	1	1	
Any other public sector incentives - Please specify in the box below.	5	5	5	

The environment is a public good (an economic externality as economists call it). This means that for sustainable finance to really work, Governments must take up their responsibilities and tax “negative externalities, in particular environmental). Part of these taxes (like a carbon tax) could be used to incentivize these instruments for “green” investing.

Question 68: In your view, to what extent would potential incentives for investors (including retail investors) help create an attractive market for sustainable investments?

Please express your view by using a scale of 1 (not effective at all) to 5 (very effective).
For scores of 4 to 5, in case you see a strong need for incentives for investors, which specific incentive(s) would best support an increase in sustainable investments? [drop down menu]

1	2	3	~~4~~	5

- Revenue-neutral public sector incentives
- Adjusted prudential treatment
  Public guarantee or co-financing
- ✓ **Other**

Please specify the reasons for your answer (provide if possible links to quantitative evidence) and the category of investor to whom it should be addressed (retail, professional, institutional, other). [BOX max. 2000 characters]

The biggest problem with EU public sector influence on investors is the over taxation of long-term investments versus short term ones. Investments for sustainability have an inherent long term nature (equity in particular): long term returns are too often taxed on their nominal amount instead of their real one, ignoring the highly negative impact of inflation over time on the real returns of long term investments, therefore de facto favouring strongly short term investment , with very limited or no impact on sustainability.

Question 69: In your view, should the EU consider putting in place specific incentives that are aimed at facilitating access to finance for SMEs carrying out sustainable activities or those SMEs that wish to transition?

- ✓ **Yes**
- No
- Do not know.

If yes, what would be your main three suggestions for actions the EU should prioritise to address this issue? [box max. 2000 characters]

2.7 The use of sustainable finance tools and frameworks by public authorities

Even though the potential scope of sustainable finance is broad, it is often viewed as being only confined to the ambit of private financial flows within capital markets. *Nevertheless,* *the boundary between public and private finance is not always strict and some concepts that are generally applied to private finance could also be considered for the public sector, such as the EU Taxonomy. This is recognised in the European Green Deal Investment Plan and the Climate Law, where the Commission committed to exploring how the EU Taxonomy can be used in the context of the European Green Deal by the public sector, beyond InvestEU. The InvestEU programme, proposed as part of the EU's Multiannual Financial Framework 2021 – 2027, combines public and private funding and once the taxonomy is in place (from end-2020 onwards) will serve as a test case for its application in public sector-related spending.*

Question 70: In your view, is the EU Taxonomy, as currently set out in the report of the Technical Expert Group on Sustainable Finance, suitable for use by the public sector, for example in order to classify and report on green expenditures?

- Yes please explain which public authority could use it, how and for what purposes. [Box max. 2000 characters]

- Yes, but only partially - please explain which public authority could use it, how and for what purposes, as well as the changes what would be required to make it fit for purpose. [Box max. 2000 characters]

- No - please explain why you consider that it is not suitable for use by public authorities, and how those reasons could be best addressed in your view. [Box max. 2000 characters]

- Do not know.

Question 71: In particular, is the EU Taxonomy, as currently set out in the report of the Technical Expert Group on Sustainable Finance, suitable for use by the public sector in the area of green public procurement?

- Yes
- Yes, but only partially
- No
- Do not know

If no or yes, but only partially, please explain why and how those reasons could be best addressed. [BOX max. 2000 characters]

Question 72: In particular, should the EU Taxonomy[42] play a role in the context of public spending frameworks at EU level, i.e. EU spending programmes such as EU funds, Structural and Cohesion Funds and EU state aid rules, where appropriate? Please select all that apply.

- Yes, the taxonomy with climate and environmental objectives set out in the Taxonomy Regulation;
- Yes, but only if social objectives are incorporated in the EU Taxonomy, as recommended by the TEG, and depending on the outcome of the report that the Commission must publish by 31 December 2021 in line with the review clause of the political agreement on the Taxonomy Regulation.
- No;
- Do not know

Follow-up questions:

If yes, what role should it play and is the taxonomy, as currently set out in the report of the Technical Expert Group on Sustainable Finance, suitable for the following purposes? Select all that apply:

- In the context of some EU spending programmes: BOX [max 2000 characters]
- In the context of EU state aid rules: BOX [max 2000 characters]
- Other, please specify. BOX [max. 2000 characters]

If yes, but only if social objectives are included; what role do you see for a social, climate and environmental taxonomy? Select all that apply.

- In the context of some EU spending programmes: BOX [max 2000 characters]
- In the context of EU state aid rules: BOX [max 2000 characters]
- Other, please specify. BOX [max. 2000 characters]

[42] The six environmental objectives set out in the Taxonomy Regulation are the following: (1) climate change mitigation, (2) climate change adaptation, (3) sustainable use and protection of water and marine resources, (4) transition to a circular economy, (5) pollution prevention and control, (6) protection and restoration of biodiversity and ecosystems.

Question 73: Should public issuers, including Member States, be expected to make use of a future EU Green Bond Standard for their green bond issuances, including the issuance of sovereign green bonds in case they decide to issue this kind of debt?

- Yes
- No
- Do not know.

If no, are there specificities of public issuers and funded projects or assets that the existing guidance on green bonds, developed by the TEG, does not account for?
[BOX max. 2000 characters]

2.8 Promoting intra-EU cross-border sustainable investments

In order to attract and encourage cross-border investments, a range of investment promotion services have been put in place by public authorities. Investment promotion services include for instance information on the legal framework, advice on the project, such as on financing, partner and location search, support in completing authorisations and problem-solving mechanisms relating to issues of individual or general relevance. In some cases specific support is provided for strategic projects or priority sectors.

Question 74: Do you consider that targeted investment promotion services could support the scaling up of cross-border sustainable investments?

- ✓ **Yes**
- No
- Do not know

If yes, please specify what type of services would be useful for this purpose:

- ✓ **Information on legal frameworks**
- Individualised advice (e.g. on financing)
- Partner and location search
- Support in completing authorisations

- Problem-solving mechanisms
- Other, please specify [box max. 2000 characters]

2.9 EU Investment Protection Framework

To encourage long-term sustainable investments in the EU, it is essential that investors are confident that their investments will be effectively protected throughout their life-cycle in relation to the state where they are located. The EU investment protection framework includes the single market fundamental freedoms, property protection from expropriation, the principles of legal certainty, legitimate expectations and good administration which ensure a stable and predictable environment, including remedies and enforcement in national courts. These elements can have an impact on cross-border investment decisions, especially for long-term investments. While a separate consultation on investment protection will take place soon, ***the purpose of this section is to investigate whether the above-mentioned factors have an impact on sustainable projects in particular****, such as for instance for long-term infrastructure and innovation projects necessary for the EU's industrial transition towards a sustainable economy.*

Question 75: Do you consider that the investment protection framework has an impact on decisions to engage in cross-border sustainable investment? Please choose one of the following:

- Investment protection has no impact.
- ✓ **Investment protection has a small impact (one of many factors to consider).**
- Investment protection has **medium impact** (e.g. it can lead to an increase in costs).
- Investment protection has a **significant impact** (e.g. influence on scale or type of investment).
- Investment protection is a factor that can have a **decisive impact** on cross-border investments decisions and can result in cancellation of planned or withdrawal of existing investments.
- Do not know.

2.10 Promoting sustainable finance globally

The global financial challenge posed by climate change and environmental degradation requires an ***internationally coordinated*** *response. To complement the work done by the Network of Central Banks and Supervisors for Greening the Financial system (NGFS) on climate-related risks and the Coalition of Finance Ministers for Climate Action mainly on public budgetary matters and fiscal policies,* ***the EU has launched together with the relevant public authorities from like-***

minded countries the International Platform on Sustainable Finance (IPSF)*. The purpose of the IPSF is to promote integrated markets for environmentally sustainable investment at a global level. It will deepen international coordination on approaches and initiatives that are fundamental for private investors to identify and seize environmentally sustainable investment opportunities globally, in particular in the areas of taxonomy, disclosures, standards and labels.*

Question 76: Do you think the current level of global coordination between public actors for sustainable finance is sufficient to promote sustainable finance globally as well as to ensure coherent frameworks and action to deliver on the Paris Agreement and/or the UN Sustainable Development Goals (SDGs)?

Please express your view by using a scale of 1 (highly insufficient) to 5 (fully sufficient).

1	~~2~~	3	4	5

For scores of 1-2, what are the main missing factors at international level to further promote sustainable finance globally and to ensure coherent frameworks and actions? [BOX max. 2000 characters]

International sustainable finance market is characterized by high fragmentation due to the different understanding of environmental social and governance risks and characteristics of sustainable investments. The international platform on sustainable finance could foster to use a common "language" (taxonomy, standards, labels) that will help to improve the integration of sustainable finance investments. Brexit and the risk of future potential regulatory arbitrage is a key upcoming risk.

Question 77: What can the Commission do to facilitate global coordination of the private sector (financial and non-financial) in order to deliver on the goals of the Paris Agreement and/or SDGs? Please list a maximum of three proposals. [BOX max. 2000 characters]

1- To catalyse the development of international non-financial reporting standards in order to foster consistency and comparability. This will help to reduce the fragmentation of the market bosting the development of the market for sustainable investments.
2- To align international policy and framework (such as with the EU taxonomy) that concern sustainable finance in order to guarantee a coordinated approach to allocate capital into sustainable projects in line with the Paris Agreement and/or Sustainable Development Goals. This would help to avoid complexity and to develop level playing field for market participants at international level.
3- To create international certifications or labels on sustainable investments that facilitate comparability and cross-border capital flow into sustainable projects.

Question 78: In your view, what are the main barriers private investors face when financing sustainable projects and activities in emerging markets and/or developing economies? Please select all that apply.

- **Lack of internationally comparable sustainable finance frameworks (standards, taxonomies, disclosure, etc.);**
- Lack of clearly identifiable sustainable projects on the ground;
- Excessive (perceived or real) investment risk;
- Difficulties to measure sustainable project achievements over time;
- Other, please specify [BOX max. 2000 characters].

Question 79: In your opinion, in the context of European international cooperation and development policy, how can the EU best support the mobilisation of international and domestic private investors to finance sustainable projects and activities in emerging markets and developing countries, whilst avoiding market distortions?

Please provide a maximum of three proposals. [BOX max. 2000 characters]

> The creation of an international sustainable investment plan for developing countries: by mobilising private and public financing together with other financial institutions. This initiative can provide a well-established framework for coordination of investments for green transformation in developing countries.

Question 80: How can EU sustainable finance tools (e.g. taxonomy, benchmarks, disclosure requirements) be used to help scale up the financing of sustainable projects and activities in emerging markets and/or developing economies? Which tools are best-suited to help increase financial flows towards and within these countries and what challenges can you identify when implementing them? Please select among the following options.

- All EU sustainable finance tools are already suitable and can be applied to emerging markets and/or developing economies without any change.

- Some tools can be applied, but not all of them. If necessary, please explain [box max. 2000 characters].

✓ **These tools need to be adapted to local specificities in emerging markets and/or developing economies. Please explain how you think they could be adapted [box max. 2000 characters].**

> These tools need to be adapted considering the regional characteristics of emerging markets. For example, an international taxonomy framework should consider sectors and activities differences guaranteeing the level of granularity and comparability.

- Do not know.

Question 81: In particular, do you think that the EU Taxonomy is suitable for use by development banks, when crowding in private finance, either through guarantees or blended finance for sustainable projects and activities in emerging markets and/or developing economies?

- **Yes**
- Yes, but only partially
- no
- do not know

If no or yes, but only partially, please explain why and how the obstacles you identify could be best addressed [box max. 2000 characters].

Reducing and managing climate and environmental risks

Climate and environmental risks, including relevant transition risks, and their possible negative social impacts, can have a disruptive impact on our economies and financial system, if not managed appropriately. Against this background, the three European supervisory authorities (ESAs) have each developed work plans on sustainable finance.[43] *Building, among others, on the ESAs' activities further actions are envisaged to improve the management of climate and environmental risks by all actors in the financial system. In particular, the political agreement on the Taxonomy Regulation tasks the Commission with publishing a report on the provisions required for extending its requirements to activities that do significantly harm environmental sustainability (the so-called "brown taxonomy").*

3.1 Identifying exposures to harmful activities and assets and disincentivising environmentally harmful investments

Question 82: In particular, do you think that existing actions need to be complemented by the development of a taxonomy for economic activities that are most exposed to the transition due

[43] More information on the ESAs' activities on sustainable finance is available on the authorities' websites. See in particular ESMA's strategy (https://www.esma.europa.eu/sites/default/files/library/esma22-105-1052_sustainable_finance_strategy.pdf), EBA Action Plan (, and EIOPA's dedicated webpage (https://www.eiopa.europa.eu/browse/sustainable-finance_en)

to their current negative environmental impacts (the so-called "brown taxonomy") at EU level, in line with the review clause of the political agreement on the Taxonomy Regulation?

- ✓ **Yes**
- No
- Do not know

- If no, please explain why you disagree [BOX max. 2000 characters]

If yes, what would be the purpose of such a brown taxonomy? (select all that apply) o

- ✓ **Help supervisors to identify and manage climate and environmental risks.**
- ✓ **Create new prudential tools, such as for exposures to carbon-intensive industries.**
- ✓ **Make it easier for investors and financial institutions to voluntarily lower their exposure to these activities.**
- ✓ **Identify and stop environmentally harmful subsidies.**
- Other, please specify. [box max. 2000 characters]

Question 83: Beyond a sustainable and a brown taxonomy, do you see the need for a taxonomy which would cover all other economic activities that lie in between the two ends of the spectrum, and which may have a more limited negative or positive impact, in line with the review clause of the political agreement on the Taxonomy Regulation?

- ✓ **Yes**
- No
- Do not know

If yes, what should be the purpose of such a taxonomy? Please specify. [BOX max. 2000 characters]

The review clause should further expand the taxonomy to include also the social and governance aspects. Taxonomy as currently drafted remains incomplete as it provides a framework only for the environmental dimension but leaves behind the social and governance dimension. Social and governance considerations are integrated aspects of the overall sustainability assessment performed by asset managers and ESG rating providers. The missed opportunity to establish a complete taxonomy jeopardizes the efforts to address the divergent practices described in our research on Sustainable Investment research (please see previous answers about evidence on divergent

practices)[44] . In addition, its non-mandatory nature may result only limited impact on the entire sustainable investments landscape.

3.2 Financial stability risk

The analysis and understanding of the impact of climate-related and environmental risks on financial stability is improving, thanks in particular to the work done by supervisors and central banks,[45] regulators and research centres. However, significant progress still needs to be made in order to properly understand and manage the impact of these risks.

Question 84: Climate change will impact financial stability through two main channels: physical risks, related to damages from climate-related events, and transition risks, related to the effect of mitigation strategies, especially if these are adopted late and abruptly. In addition, second-order effects (for instance the impact of climate change on real estate prices) can further weaken the whole financial system. What are in your view the most important channels through which climate change will affect your industry? Please provide links to quantitative analysis when available.

- Physical risks, please specify if necessary [BOX max. 2000 characters]
- Transition risks, please specify if necessary [BOX max. 2000 characters]
- Second-order effects, please specify if necessary [BOX max. 2000 characters]
- Other, please specify [BOX max. 2000 characters]

Question 85: What key actions taken in your industry do you consider to be relevant and impactful to enhance the management of climate and environment related risks? Please identify a maximum of three actions taken in your industry [BOX max. 2000 characters]

Question 86: Following the financial crisis, the EU has developed several macro-prudential instruments, in particular for the banking sector (CRR/CRDIV), which aim to address systemic risk in the financial system. Do you consider the current macro-prudential policy toolbox for the EU financial sector sufficient to identify and address potential systemic financial stability risks related to climate change?

[44] BETTER FINANCE research on Sustainable Investment Funds is not published yet
[45] See for instance the Network of Central Banks and Supervisors for Greening the Financial System (NGFS).

Please express your view by using a scale of 1 (highly inadequate) to 5 (fully sufficient).

1	2	3	4	5

For scores of 1-2, what solution would you propose? Please list a maximum of three. [BOX max 2000 characters]

Insurance prudential framework

Insurers manage large volumes of assets on behalf of policyholders and they can therefore play an important role in the transition to a sustainable economy. At the same time, insurance companies have underwriting liabilities exposed to sustainability risks. In addition, the (re)insurance sector plays a key role in managing risks arising from natural catastrophes though risk-pooling and influencing risk mitigating behaviour. The Solvency II Directive sets out the prudential framework for insurance companies. The Commission requested technical advice from the European Insurance and Occupation Pensions Authority (EIOPA) on the integration of sustainability risks and sustainability factors in Solvency II. The Commission also mandated EIOPA to investigate whether there is undue volatility of their solvency position that may impede long-term investments, as part of the 2020 Review of Solvency II. EIOPA is expected to submit its final advice in June 2020.

In September 2019, EIOPA already provided an opinion on sustainability within Solvency II. EIOPA identified additional practices that should be adopted by insurance companies to ensure that sustainability risks are duly taken into account in companies' risk management.

On that basis, the Commission could consider clarifications of insurers' obligations as part of the review of the Solvency II Directive. Stakeholders will soon be invited to comment on the Commission's inception impact assessment as regards the review. The Commission will also launch a public consultation as part of the review.

Question 87: Beyond prudential regulation, do you consider that the EU should take further action to mobilise insurance companies to finance the transition and manage climate and environmental risks?

- Yes
- No
- Do not know

If yes, please specify which actions would be relevant. [BOX max. 2000 characters]

Banking prudential framework

In the context of the last CRR/D review, co-legislators agreed on three actions aiming at integrating ESG considerations into EU banking regulation:

- *a mandate for the EBA to assess and possibly issue guidelines regarding the inclusion of ESG risks in the supervisory review and evaluation process (SREP) (Article 98(8) CRD);*
- *a requirement for large, listed institutions to disclose ESG risks (Article 449a CRR) (note that some banks are also in the scope of the NFRD);*
- *a mandate for the EBA to assess whether a dedicated prudential treatment of exposures related to assets or activities associated substantially with sustainability objectives would be justified (Article 501c CRR).*

Because the work on ESG risks was at its initial stages, co-legislators agreed on a gradual approach to tackling those risks. However, given the new objectives under the European Green Deal, it can be argued that the efforts in this area need to be scaled up in order to support a faster transition to a sustainable economy and increase the resilience of physical assets to climate and environmental risks. Integrating sustainability considerations in banks' business models requires a change in culture which their governance structure needs to effectively reflect and support.

Question 88: Do you consider that there is a need to incorporate ESG risks into prudential regulation in a more effective and faster manner, while ensuring a level-playing field?

- Yes
- No
- Do not know.

If yes, is there any category of assets that could warrant a more risk-sensitive treatment? Are there any other prudential measures that could help promoting in a prudentially sound way the role of the EU banking sector in funding the transition to a more sustainable economy? [box max. 2000 characters]

Question 89: Beyond prudential regulation, do you consider that the EU should take further action to mobilise banks to finance the transition and manage climate-related and environmental risks?

- Yes one or both, please specify which action would be relevant [BOX max. 2000 characters]
- No.
- Do not know.

Question 90: Beyond the possible general measures referred to in section 1.6, would more specific actions related to banks' governance foster the integration, the measurement and mitigation of sustainability risks and impacts into banks' activities?

- Yes
- No
- Do not know.

If yes, please specify which measures would be relevant. [BOX max. 2000 characters]

Asset managers

Traditionally, the integration of material sustainability factors in portfolios, with respect to both their selection and management, has considered only their impact on the financial position and future earning capacity of a portfolio's holdings (i.e., the 'outside-in' or 'financial materiality' perspective). However, asset managers should take into account also the impact of a portfolio on society and the environment (i.e., the 'inside-out' or 'environmental/social materiality' perspective). This so-called "double materiality" perspective lies at the heart of the Disclosure Regulation, which makes it clear that a significant part of the financial services market must consider also their adverse impacts on sustainability (i.e. negative externalities).

Question 91: Do you see merits in adapting rules on fiduciary duties, best interests of investors/the prudent person rule, risk management and internal structures and processes in sectorial rules to directly require them to consider and integrate adverse impacts of investment decisions on sustainability (negative externalities)?

- ✓ **Yes**
- No
- Do not know.

If yes, what solution would you propose? [BOX max. 2000 characters]

stewardship code – a framework of duties that asset managers must observe with regards to the issuer – should be instituted at EU level, enforcing a comply or explain principle. In addition, institutional investors should be obliged to produce reports justifying why their actions in corporate governance of companies best serve the company and their clients (beneficial owners).

According to our report on Sustainable Value for Money[46] prepared in collaboration with CFA Institute, it is clear that the introduction of clear rules on duty of care and stewardship are essential to regain the trust of individual investors in the capital market. Society at large would be reassured to see that the relation between financial advisers and clients is taken seriously, reason why a Hippocratic oath, like in the medical profession, might help restoring confidence in the financial system as a whole, fostering investment firms to behave responsibly and operate as good stewards. Stewardship requires the right framework in order to work correctly. Therefore, a series of policies and procedures needs to be put in place in order to ensure client assets are safeguarded.

Particular attention should be given to stewardship and fiduciary duties in order to make prudent decision with the best interest of the beneficiaries at heart: considering all long-term values and interests that include environmental risks, social risks and governance issues that can affect the company.

Pension providers

Pension providers' long-term liabilities make them an important source of sustainable finance. They have an inherently long-term approach, as the beneficiaries of retirement expect income streams over several decades. Compared with other institutions, pension providers' long-term investment policies also make their assets potentially more exposed to long-term risks. Thus far, the issues of sustainability reporting and ESG integration by EU pension providers have been taken up in the areas of institutions for occupational retirement provision (IORPs) ("Pillar II" - covered at EU level by the IORP Directive) and private voluntary plans for personal pensions ("Pillar III" – covered at EU level by the PEPP Regulation) already in 2016 and 2017, respectively. The Commission will review the IORP II Directive by January 2023 and report on its implementation and effectiveness.

However, according to a stress test on IORPs run by EIOPA in 2019 and assessing for the first time the integration of ESG factors in IORPs' risk management and investment allocation, only about 30% of IORPs in the EU have a strategy in place to manage ESG-related risks to their investments. Moreover, while most IORPs claimed to have taken appropriate steps to identify ESG risks to their investments, only 19% assess the impact of ESG factors on investments' risks and returns.[47] Lastly, the study provided a preliminary quantitative analysis of the investment portfolio[48] which would

[46] https://betterfinance.eu/publication/better-finance-cfa-institute-report-on-sustainable-value-for-money/

[47] The analysis shows that the preparedness of pension schemes to integrate sustainability factors is widely dispersed and seems correlated to how advanced national frameworks were. IORP II directive sets minimum harmonisation and was expected to be transposed in national law by January 2019 (and hence could not necessarily be expected to be implemented by end-2018 for the EIOPA survey for the 2019 stress test).

[48] With almost 4 trillion Euros of assets under management, the EEA's Institutions for Occupational Retirement Provision (IORPs) sector is an important actor on financial markets.

indicate significant exposures of the IORPs in the sample to business sectors prone to high greenhouse gas emissions.

In 2017, the Commission established a High-level group of experts on pensions to provide policy advice on matters related to supplementary pensions. In its report, the group recommended that the EU, its Member States and the social partners further clarify how pension providers can take into account the impact of ESG factors on investment decisions and develop cost-effective tools and methodologies to assess the vulnerability of EU pension providers to long-term environmental and social sustainability risks. The group also pointed out that, in the case of IORPs which are collective schemes, it might be challenging to make investment decisions reconciling possibly diverging views of individual members and beneficiaries on ESG investment. Moreover, in 2019, EIOPA issued an opinion on the supervision of the management of ESG risks faced by IORPs.

Question 92: Should the EU explore options to improve ESG integration and reporting beyond what is currently required by the regulatory framework for pension providers?

- ✓ **Yes**
- No
- Do not know.

If yes, please specify what actions would be relevant in your view. [BOX max. 2000 characters]

BETTER FINANCE welcomes the inclusion of obligations concerning ESG-factoring in the PEPP Regulation. This constitutes a large step ahead as it would be – save other legislative developments – the first pan-EU product which will be explicitly required to take into account and consider risks and long-term implications on ESG factors.

However, PEPP Regulation's provisions regarding ESG-factoring in the investment process and the disclosure thereof are not well aligned and may lead to confusion among product manufacturers and consumers. EIOPA has the opportunity to temporarily clarify this topic through a proper reading of the Level 1 legislation. In our view, there is no doubt as to the fact that PEPPs will necessarily be sustainable long-term retirement provision products since Art. 41 demands compliance with ESG factors, rather than merely the comply or explain rule. However, Article 2(33) neither contains an organic, nor a functional definition of ESG, but only makes references as to what may be considered ESG. In the current context where a taxonomy or a definition in EU law does not exist, market participants (product manufacturers, issuers, rating agencies) have widely divergent understandings and screening processes of ESG or sustainability factoring. What is worse, on certain occasions many products are green washed.[49] Therefore, EIOPA should take the opportunity to at least harmonise – for the moment – an ESG definition by establishing one of the existing charters as a benchmark. This prescription, or other more ambitious, could be covered by a sunset

[49] https://scmdirect.com/wp-content/uploads/2019/11/SCM-Direct-Greenwashing-Report.pdf

clause effectively replacing it with any other taxonomy or definition adopted at EU level. In this sense, divergent labelling and risk considerations would be avoided and consumer understanding would be enhanced.[50]

Regarding IORP directive, the pension benefit statement should provide clear, adequate, concise and comparable information regarding ESG information. If the pension scheme incorporates ESG factoring the following information should be disclosed in the pension benefit statement:

- ESG investing process with mention of real impact goals if any and if yes how this impact will be measured, and a prominent warning if this ESG investing process has no real SG impact goal (like negative screening of stocks for example, which is pure greenwashing in BETTER FINANCE's view)
- Criteria for incorporating ESG factors

Question 93: More generally, how can pension providers contribute to the achievement of the EU's climate and environmental goals in a more proactive way, also in the interest of their own sustained long-term performance? How can the EU facilitate the participation of pension providers to such transition?

[BOX max. 2000 characters]

Investment and private pension products are persistently among the worst performing retail services markets of all throughout the EU according to the European Commission's Consumer Markets Scoreboard. In 2018 Retail Finance was yet again ranked as one of the worst performing consumer markets "where consumers suffer the highest detriment (financial loss or waste of time) in case of problems"[51]. Already years earlier the Commission pointed out that "other reasons for not saving long-term are the often-poor performance of financial intermediaries to deliver reasonable return and costs of intermediation"[52]. Pension savings also appear to be one of the few retail services where neither the customers nor the public supervisors are even properly informed about the real net performance of the services rendered to them (let alone ESG integration). Nevertheless, pension providers will have a great opportunity with PEPP. They must ensure that the PEPP truly represents an "EU quality label" product. The Pan-European Personal Pension (PEPP) product must create an EU quality label for retirement provision vehicles that will increase transparency and trust of consumers in capital markets. To this end PEPP provider must also diligently disclose details of how the investment policy takes ESG factors into account, as well as ESG performance information, where available. As previously explained, particular

[50] See our response to the consultation EIOPA- PEPP Consultation https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Response-EIOPA-PEPP-Consultation-final-02032020.pdf

[51] Based on the worrying findings of the newest 2018 edition of the "EU Consumer Markets Scoreboard"; See 2018 Consumer Markets Scoreboard "Making markets work for consumers" https://ec.europa.eu/info/sites/info/files/eujus15a-1816-i02_-_the_consumer_markets_scoreboard_2018_-_accessibility_final.pdf, page 9.

[52] European Commission - Staff Working Document on long term financing of the EU economy (2013)

attention should be given to stewardship and fiduciary duties in order to make prudent decisions in the best interest of the beneficiaries: considering all long-term values and interests that include environment and climate risks, social risks and governance issues.

Question 94: In view of the planned review of the IORP II Directive in 2023, should the EU further improve the integration of members' and beneficiaries' ESG preferences in the investment strategies and the management and governance of IORPs?

- Yes
- No
- Do not know.

If yes, how could this be achieved, taking into account that IORPs are collective schemes whose members may have different views on ESG integration? [BOX max. 2000 characters]

3.3 Credit rating agencies

Regulation 1060/2009 requires credit rating agencies (CRAs) to take into account all factors that are 'material' for the probability of default of the issuer or financial instrument when issuing or changing a credit rating or rating outlook. This covers also ESG factors. According to ESMA's advice on credit rating sustainability issues and disclosure requirements, the extent to which ESG factors are being considered can vary significantly across asset classes, based on each CRA's methodology.

Following the 2018 Action Plan on Financing Sustainable Growth, and in response to concerns about the extent to which ESG factors were considered by CRAs, ESMA adopted guidelines on disclosure requirements for credit ratings and rating outlooks. ESMA's Guidelines on these disclosure requirements will become applicable as of April 2020. Pursuant to the guidelines, CRAs should report in which cases ESG factors are key drivers behind the change to the credit rating or rating outlook. Consequently, the current landscape will change in the coming months. The Commission services intend to report on the progress regarding disclosure of ESG considerations by CRAs in 2021.

Question 95: How would you assess the transparency of the integration of ESG factors into credit ratings by CRAs?

Please express your view by using a scale of 1 (not transparent at all) to 5 (very transparent).

1	2	3	4	5

If necessary, please explain the reasons for your answer. [BOX max. 2000 characters]

Question 96: How would you assess the effectiveness of the integration of ESG factors into credit ratings by CRAs?

Please express your view by using a scale of 1 (very ineffective) to 5 (very effective).

1	2	3	4	5

If necessary, please explain the reasons for your answer. [BOX max. 2000 characters]

Question 97: Beyond the guidelines, in your opinion, should the EU take further actions in this area?

- Yes
- No
- Do not know.

If yes, please specify what kind of action you consider would address the identified problems. In particular should the EU consider regulatory intervention? [BOX max. 2000 characters]

3.4 Natural capital accounting or "environmental footprint"

Internal tools, such as the practice of natural capital accounting, can help inform companies' decision-making based on the impact of their activities on sustainability factors. ***Natural capital accounting or "environmental footprinting"*** *has the potential to feed into business performance management and decision-making by explicitly mapping out impacts (i.e. the company's environmental footprint across its value chain) and dependencies on natural capital resources and by placing a monetary value on them. In order to ensure appropriate management of environmental risks and mitigation opportunities, and reduce related transaction costs, the Commission will support businesses and other stakeholders in developing standardised* ***natural capital accounting*** *practices within the EU and internationally.*

Question 98: Are there any specific existing initiatives (e.g. private, public or other) you suggest the Commission should consider when supporting more businesses and other stakeholders in implementing standardised natural capital accounting/environmental footprinting practices within the EU and internationally?

- Yes
- No
- Do not know.

If yes, please list a maximum of three relevant initiatives. [BOX max. 2000 characters].

3.5 Improving resilience to adverse climate and environmental impacts[53]

Climate-related loss and physical risk data

Investors and asset owners, be they businesses, citizens or public authorities, can better navigate and manage the increased adverse impacts of a changing climate when given access to decision-relevant data. Although many non-life insurance undertakings have built up significant knowledge, most other financial institutions and economic actors have a limited understanding of (increasing) climate-related physical risks.

A wider-spread and more precise understanding of current losses arising from climate- and weather-related events is hence crucial to assess macro-economic impacts, which determine investment environments. It could also be helpful to better calibrate and customise climate-related physical risk models needed to inform investment decisions going forward, to unlock public and private adaptation and resilience investments and to enhance the resilience of the EU's economy and society to the unavoidable impacts of climate change.

Question 99: In your opinion, should the European Commission take action to enhance the availability, usability and comparability of climate-related loss and physical risk data across the EU?

- Yes
- No
- Do not know.

If yes, please select all that apply:

- Loss data, please explain why [BOX max. 2000 characters]

- Physical risk data, please explain why [BOX max. 2000 characters]

[53] Please note that the Commission is also preparing an upgraded EU Adaptation Strategy. A dedicated public consultation will be launched soon.

Financial management of physical risk

According to a report by the European Environmental Agency, during the period of 1980-2017, 65% of direct economic losses from climate disasters were not covered by insurance in EU and EFTA countries, with wide discrepancies between Member States, hazards and types of policyholders. The availability and affordability of natural catastrophe financial risk management tools differs widely across the EU, also due to different choices and cultural preferences with regards to ex-ante and ex-post financial management in case of disasters. While the financial industry (and in particular the insurance sector) can play a leading role in managing the financial risk arising from adverse climate impacts by absorbing losses and promoting resilience, EIOPA has warned that insurability is likely to become an increasing concern. Measures to maintain and broaden risk transfer mechanisms might hence require (potentially temporary) public policy solutions.

Furthermore, the ongoing COVID-19 outbreak is highlighting the growing risk arising from pandemics in particular, which will become more frequent with the reduction of biodiversity and wildlife habitat. UNEP's Frontiers 2016 Report on Emerging Issues of Environment Concern shows that such diseases can threaten economic development.

In this context, social and catastrophe bonds could play a crucial role: the former to orient use of proceeds towards the health system (e.g. IFFIM first vaccine bond issued in 2006), and the latter to broaden the financing options that are available to insurers when it comes to catastrophe reinsurance. Such instruments would help mobilise the broadest possible range of private finance alongside public budgets to contribute to the resilience of the EU's health and economic systems, via prevention and reinsurance.

Question 100: Is there a role for the EU to promote more equal access to climate-related financial risk management mechanisms for businesses and citizens across the EU?

- Yes
- No
- Do not know.

If yes, please indicate the degree to which you believe the following actions could be helpful, using a scale of 1 (not helpful at all) to 5 (very helpful) and substantiate your reasoning:

Financial support to the development of more accurate climate physical risk models. [BOX max. 2000 characters]

- Raise awareness about climate physical risk. [BOX max. 2000 characters].

1	2	3	4	5

- Promote ex-ante “build back better” requirements to improve future resilience of the affected regions and or/sectors after a natural catastrophe. [BOX max. 2000 characters].

1	2	3	4	5

- Facilitate public-private partnerships to expand affordable and comprehensive insurance coverage. [BOX max. 2000 characters].

1	2	3	4	5

- Reform EU post-disaster financial support. [BOX max. 2000 characters].

1	2	3	4	5

- Support the development of alternative financial products (e.g. catastrophe bonds) offering protection/hedging against financial losses stemming from climate- or environment-related events. [BOX max. 2000 characters]

1	2	3	4	5

- Advise Member States on their national natural disaster insurance and post disaster compensation and reconstruction frameworks. [BOX max. 2000 characters].

1	2	3	4	5

- Regulate by setting minimum performance features for national climate-related disaster financial management schemes. [BOX max. 2000 characters].

1	2	3	4	5

- Create a European climate-related disaster risk transfer mechanism. [BOX max. 2000 characters].

1	2	3	4	5

- Other, please specify. [BOX max. 2000 characters].

Question 101: Specifically, with regards to the insurability of climate-related risks, do you see a role for the EU in this area?

- Yes
- No
- Do not know

If yes, which actions you would consider to be useful? In particular, is there scope for EU action to improve the offer of products and services for climate-related disaster risk reduction, enhance insurers' potential to promote increased resilience of their policyholders beyond a mere compensatory role?[54]

- Yes
- No
- Do not know.

If yes, please explain which actions and the expected impact (high, medium, low). [BOX max. 2000 characters]

If no, please explain. [BOX max. 2000 characters]

Question 102: In your view, should investors and / or credit institutions, when they provide financing, be required to carry out an assessment of the potential long-term environmental and climate risks on the project, economic activity, or other assets?

- ✓ **Yes**
- No
- Do not know.

If yes, what action should the EU take? Please list a maximum of three actions. [BOX max. 2000 characters]

It is important to shift from short-termism to long-term perspective. Considering environmental issues means to consider the long-term implications of climate change and environmental risks but also the impact that an economic activity has on the environment or contribute to reduce increase the environmental/ climate issues. In order to achieve this, decisive may also be the overall strategy of the asset manager. A clear and precise definition of long-term investment and short-termism would be very helpful in this case.

[54] For instance, EIOPA in its opinion on sustainability on Solvency II talks about "impact underwriting which includes the development of new insurance products, adjustments in the design and pricing of the products and the engagement with public authorities without disregard for actuarial risk-based principles of risk selection and pricing".