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

BETTER FINANCE'S FEEDBACK ON THE COMMISSION'S PROPOSAL TO AMEND DELEGATED REGULATION (EU) 2017/2359 WITH REGARD TO ENVIRONMENTAL, SOCIAL AND GOVERNANCE PREFERENCES IN THE DISTRIBUTION OF INSURANCE-BASED INVESTMENT PRODUCTS

***BETTER FINANCE**, the European Federation of Investors and Financial Services Users, is the dedicated representative of financial services users at European level. It counts about fifty national and international members and sub-member organizations in turn comprising about 4.5 million individual members. Our organization acts as an independent financial expertise centre to the direct benefit of the European financial services users (shareholders, other investors, savers, pension fund participants, life insurance policy holders, borrowers, etc.) and other stakeholders of the European financial services who are independent from the financial industry. As such its activities are supported by the European Union since 2012.*

***BETTER FINANCE** is the most involved European end user and civil society organisation in the EU Authorities' financial advisory groups, with experts participating in the Securities & Markets, the Banking, the Occupational Pensions and Insurance and Reinsurance Stakeholder Groups of the European Supervisory Authorities; as well as in the European Commission's Financial Services User Group (FSUG), and in the European Financial Reporting advisory Group (EFRAG). Its national members also participate in national financial regulators and supervisors bodies when possible.*

For further details please see our website: http://betterfinance.eu/

I. Summary of the proposal

This Regulation amends Delegated Regulation (EU) 2017/2359 to include the customer's ESG preferences in the criteria and practical details to be taken into account by insurance intermediaries and insurance undertakings when assessing the suitability of insurance-based investment products for their customers.

IDD (Insurance Distribution Directive) 2016/97:

- insurance intermediaries and insurance undertakings distributing insurance-based investment products must collect, as part of the **assessment of suitability, information about their customers' knowledge and experience of the relevant investment field, their financial situation including the ability to bear loss and their investment objectives including the risk tolerance**.
- no further clarifications are provided regarding the term "investment objective" and requirements are not tailored to encompass the customers' ESG preferences.
- Investment advice typically consists of 2 elements:
    - Customers profiling to understand a customer's risk preference, investment objectives, financial situation and investment experience

- Product selection in order to assure that the insurance-based investment products recommended to the customer are in line with the customer's profiling.

In practice, product selection appears to be primarily driven by **a customer's risk profile**, but **ESG preferences are not systematically assessed**:

- A customer might therefore not be able to communicate his/her ESG expectations clearly as they are not integrated in the customer profiling and product selection process.
- The evidence also points to a regulatory failure in terms of implementation regarding the consideration of ESG preferences/factors in the investment and advisory process
- Main other obstacles to consider ESG as part of the duties towards investors and beneficiaries:
    - Possible heterogeneity of beneficiaries' ESG preferences
    - Lack of reliable and comparable ESG information
    - Lack of data and tools to analyze ESG risks
    - The impact on costs and risk-adjusted performance

Objective of this initiative: to create a **mandatory requirement to take into account ESG preferences in the advisory process** (both in the customer profiling and product selection).

The targeted questionnaire on the integration of environmental, social and governance considerations in the suitability assessment raised that **only a minority of the clients proactively raise ESG issues during the advisory process.** Some of the reasons for this are:

- the available **information on ESG products is not transparent**
- the risk of **'greenwashing' in existing documentation is high**
- there is a **lack of education** on the impact of ESG factors on risk and performance. Only in rare cases, clients seem to systematically raise ESG issues during the advisory process.

Respondents had divergent views on the need for providing more information to clients (e.g. in the prospectus, KID PRIIP or on an asset manager's website) on ESG factors and sustainable finance:

- Some believed **that investors have sufficient information to take informed investment decisions.** These respondents were concerned that harmonising the type of ESG information in product documentation might bring **large discrepancies in understanding the reality of ESG risk management policies**.

The European Federation of Investors and Financial Services Users
76, rue du Lombard, 1000 Brussels - Belgium
Tel. (+32) 02 514 37 77 - Fax. (+32) 02 514 36 66
E-mail: info@betterfinance.eu -

- Other believed that **the provision of further ESG information - would be useful for investors, especially individual investors who are by nature mostly long-term driven and therefore have a great need for sustainable finance products.**

Current legislative framework:

- Insurance intermediaries and insurance undertakings are required to obtain the necessary information about the customer's knowledge and experience in the investment field, that person's ability to bear losses, and the objectives including the risk tolerance (suitability assessment).

- Information to be obtained with regard to the investment objectives of the client includes:
  - the length of time for which the client wishes to hold the investment,
  - preferences regarding risk taking,
  - risk profile
  - the purposes of the investment.

- However, **investment objectives and risks are often associated with financial objectives and insurance intermediaries/insurance undertakings do not always consider non-financial aspects such as environmental, social or ethical impact of the insurance-based investment products**. In addition, the ESG awareness among customers, in particular retail investors, is relatively low and, as a consequence, customers do not point to ESG in suitability questionnaires as a factor for a firm to consider.

The proposed Delegated Regulation:

⇨ Clarifies that insurance intermediaries and insurance undertakings are obliged to conduct, as part of the suitability assessment, an assessment of **sustainable preferences** of their customers both in the selection process and the questionnaire to collect customers' information.

⇨ Insurance intermediaries and insurance undertakings have to **include information on the ESG preferences in the sustainability statement explaining** how the recommendation meets the customer's objectives, risk profile, capacity for loss and ESG preferences (ex-post information).

II. BETTER FINANCE's position

BETTER FINANCE welcomes this opportunity to comment on the proposal amending Delegated Regulation (EU) 2017/2359 to include the customer's ESG preferences in the criteria and practical details to be taken into account by insurance intermediaries and insurance undertakings when assessing the suitability of insurance-based investment products for their customers.

Investment firms shall act in accordance with the best interest of their clients and as such, when providing investment advice and portfolio management, they must disclose information on the ESG of each financial product offered to the client before providing investment services.

The asset managers must explain to the client how his or her ESG preferences for each financial instrument is taken into consideration during the advice process.

BETTER FINANCE fully supports this proposal to include ESG considerations during the advisory and product suitability process. However, we have some concerns regarding the proposal.

Firstly, and as raised at several occasions by BETTER FINANCE[1], before requesting institutional investors and assets managers to include ESG's client's preferences in the advisory and product suitability process, we must have an internationally agreed taxonomy in order to determine, for instance, what is "green and what is not".

The Commission has chosen to follow a sequencing approach by first focusing on climate only. However, the proposed amendment to the IDD delegated regulation includes the three components: "E", "S" and "G".

Secondly, we believe that the Commission should make a clearer reference between the proposed Regulation on disclosures relating to sustainable investments and suitability risks (Proposal COM (2018) 354) 354 and the advisory and product suitability process.

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[1] BETTER FINANCE's press release " BETTER FINANCE welcomes EC roadmap towards a more sustainable economy but once again deplores failure to take the interests of EU citizens as pension savers and individual investors into account" http://betterfinance.eu/fileadmin/user_upload/documents/Press_Releases/en/Other_investors/PR_-_HLEG_Final_Report_-_020218.pdfhttp://betterfinance.eu/fileadmin/user_upload/documents/Press_Releases/en/Other_investors/PR_-_HLEG_Final_Report_-_020218.pdf

BETTER FINANCE's press release "BETTER FINANCE welcomes the Sustainable Finance Action Plan but warns the Commission against its plans regarding taxonomy, benchmarking and an eco-label" http://betterfinance.eu/fileadmin/user_upload/documents/Press_Releases/en/Other_investors/PR_-_Sustainable_Finance_-_210318.pdf

Thirdly, we warn the Commission that the inclusion of ESG considerations/ preferences should not lead providers to comply with the delegated regulation just by constructing funds corresponding to the client ESG preferences without addressing ESG consideration for the rest of the portfolio.

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76, rue du Lombard, 1000 Brussels - Belgium
Tel. (+32) 02 514 37 77 - Fax. (+32) 02 514 36 66
E-mail: info@betterfinance.eu -