

Finance Watch response to the public consultation on the Commission delegated act “XXX”, amending Delegated Regulation (EU) 2017/565 supplementing Directive 2014/65/EU

Brussels, 21st June 2018

Finance Watch is an independent non-profit Members’ association set up in 2011 to act as a public interest counterweight to the powerful financial lobby. Our mission is to strengthen the voice of society in the reform of financial regulation by conducting advocacy and presenting public interest arguments to lawmakers and citizens. Our Members are civil society organisations and expert individuals, supported by a full-time secretariat.

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We agree to the publication of this response.

Finance Watch welcomes the EC proposal to review the articles 2, 47, 48, 52 and 54 of the Delegated Regulation (EU) 2017/565, with a purpose of clarifying that Environment Social and Governance (ESG) considerations should be taken into account in the investment and advisory process as part of investments’ firms duties towards their clients.

Firstly, we would like to highlight that we believe that, the concept of “*best interest*” - as mentioned in the art. 24 (paragraph 1) of MIFID II and art. 54 of Delegated Regulation (EU) 2017/565, should be defined at the EU level to include both financial and non-financial benefits. In other words, we believe that it should be made clear that the utility of investors can depend on both financial and non-financial returns. This is particularly critical if we think about the long-term impacts of climate change on future generations and the weaknesses in the current environmental legislations, which do not adequately price the negative externalities (CO2 emissions in first place).

However, our contribution is focused on the articles that are in the scope of this consultation and our feedback to is as follows:

- 1) The definitions of ESG preference (point 7) and ESG considerations (point 8) under the article 2, should be further clarified and expanded. We would like to highlight that using the same words to explain what is trying to be defined is risking to be a major source of legal uncertainty. In particular we believe that:
 - a. In the definition of “ESG preference”, the word “preference” should be avoided. Moreover, we think that the definition of “preference” should imply the existence of different options being offered to the clients. We would suggest to the Commission to further expand the definition to clearly state that the ESG preference cannot be assessed unless the clients are informed about the trade-offs associated with an adequate number of financial instruments (risk, return and ESG profile of the investment).

- b. In the definition of “ESG consideration”, the word consideration should be avoided for the same reason indicated above. It should be made clear that ESG factors shall be systematically taken into account for two reasons:
 - i. Because they can offer risk and opportunities to clients (from a purely financial perspective) and
 - ii. Because their consideration might be critical, on the basis of the additional non-financial objectives of the clients.
- 2) It should also be made clear that the investment firms shall proactively investigate clients’ ESG preferences. We believe that the wording under 54 should be more explicit on this point. If the requirement to proactively investigate clients’ ESG preference is not made obligatory, there is the risk that clients that have specific ESG preferences will not invest according to their objectives, because they are not aware of the possibility to do so. In line with the proposed definition of preference, a proactive investigation implies the requirement for the investments’ firms to inform the clients about the trade-offs associated with an adequate number of financial instruments (risk, return and ESG profile of the investment), when conducting suitability assessment.
- 3) We would like also to highlight that investment firms, when assessing ESG preferences, should, whenever possible, rely on the upcoming EU sustainability taxonomy. If the clients know that they have the possibility to invest in assets considered sustainable according to the EU taxonomy, they might be more incentivised to invest in those assets. Since the main purpose of the upcoming EU taxonomy is to create a common language about what is sustainable, we believe that it is important to make most of its use to further create the confidence among the investors and stimulate the demand for sustainable assets.
- 4) We also believe that the information related to the environmental investment objective should also refer to the EU low carbon and positive carbon benchmark, whenever possible and relevant.
- 5) We believe that under the paragraph 9, the investment firms should also be required to offer an adequate number of financial instruments from which it is possible to understand clients’ ESG preferences (which - as indicated above - should be defined as greater liking for one alternative over another).