



## CONSULTATION ON INTEGRATING SUSTAINABILITY RISKS AND FACTORS IN MIFID II

Brussels, 19/02/2019

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*We agree to the publication of this response.*

1. We support including sustainability factors in article **21(1)** of the MIFID II Delegated Regulation on organizational requirement, but we believe that the proposed approach could be further clarified.

In particular, we would like to highlight that in the proposed paragraph:

- the wording “ESG considerations” is ambiguous and could be a source of major legal uncertainty and so we would propose to use the wording: “ESG factors, or sustainability factors”;
- it is also not clear what investment services the new paragraph refers to, and;
- how the concept: “relevant” should be interpreted in that context.

We would propose instead the following wording, which also better reflects the content of paragraph 6 on page 6, in which ESMA clarifies the purpose of the amendment to the article 21(1).

***“Investment firms shall establish, implement and maintain appropriate policies to incorporate ESG factors within their processes, systems and controls in order to ensure that investment and advisory processes correctly take them into account”.***

Finally, we would also like to highlight that while the focus is now mainly on environmental risks (and in particular on climate risks), we believe that the sustainability risks should be considered as part of a broader set of risks, given that, for example, governance risks often lead to social and/or environmental risks.

2. Article **23** shall clarify that for the purpose of the risk management the firms shall take into account sustainability factors, by specifying the time horizon taken into account and the perspective from which the sustainability factors are considered. This clarification is very important because what might not be a source of risk for an investment firm could be a risk that is transferred to the society.

We would also like to point out, that based on the scope of the Taxonomy Regulation, it is not clear how ESMA links the taxonomy with the sustainability risks discussed in paragraph 9 on page 9. The taxonomy will be a positive list of criteria which will allow identification of economic activities which substantially contribute to one of the environmental objectives listed in the Taxonomy Regulation and could potentially identify “E” opportunities. On the other hand, financial sustainability risks concern those sustainability factors, which could become financially material as a consequence of, among other things, regulatory developments (such as more stringent environmental policies), technological developments, transition to low carbon economy, reputational issues from involvements in socially controversial activities, etc. In this sense, when referring to sustainability risks in finance, we implicitly refer to unsustainable economic activities, which unfortunately are not in the scope of the Commission’s proposal.

We would like to highlight that ideally a complete Taxonomy should be able to classify all economic activities as green or non-green. And that is key for identifying and so managing of ESG risks and opportunities.

Moreover, ESG risks and opportunities shall be adequately disclosed (as climate related financial information should be disclosed in line with the TCFD recommendations).

Regarding point 10 on page 11, we would like to raise the attention to the fact that currently there are no low carbon benchmarks. What we can see as being offered by FTSE, Euronext, MSCI are indices which have a carbon intensity lower than their parent indices. So, we have only what we should call “lower” or “reduced” carbon benchmarks, but they should not be called “low carbon benchmarks” given that they are not aligned with any emission reduction target goal and are based on relative and non-science-based indicators.

Any benchmark which claims to be low carbon should be aligned with the Paris Agreement goals and specifically with the EU long-term reduction targets<sup>1</sup>.

3. With regard to the proposal for the recital **59**, we support the proposed approach, but we do not believe that a recital is enough.

Therefore, we would recommend that the first paragraph of the proposed recital 59: “When identifying the types of conflicts of interest whose existence may damage the interests of a client, investment firms should include those that may stem from the distribution of

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<sup>1</sup> [https://ec.europa.eu/clima/policies/strategies/2050\\_en](https://ec.europa.eu/clima/policies/strategies/2050_en)

environmentally sustainable investments, social investments or good governance investments”, is included in article 33 of the concerned Delegated Regulation, given that article 33 is specifically on the identification of the types of conflicts of interest.

Moreover, in order to better link the concept of best interest to the sustainable finance goals, we propose the following wording for recital 59:

*“Firms should have in place appropriate arrangements to ensure that the inclusion of ESG considerations in the advisory process and portfolio management does not lead to mis-selling practices **and that the best interest of the client is pursued. The best interest shall not be assumed to be limited to the maximization of risk adjusted financial returns.**”*

4. NO.

5. With regard to the current market standards or “labels”, we see several sources of concern:

- a. lack of harmonization with regard to the criteria used for assessing whether an economic activity (and so an investment) is sustainable;
- b. arbitrary choices when selecting weights (in case of labels relying on a point system);
- c. lack of transparency with regard to the reasons behind the choices of the minimum percentage of the fund’s total assets that needs to be invested in environmentally friendly activity in order to be awarded a certain label;
- d. terminology used for the different labels, for example: LuxFlag offers different types of labels: Environment, ESG, Climate and Green bond labels. It is obvious that the environmental component is key in each of the four labels and so it is important that the concept of environmental sustainability is defined in a consistent and scientific way, independently of the specific label. In this sense, we hope that the upcoming Taxonomy will bring certain level of clarity as to when an economic activity can be deemed to be environmentally sustainable;
- e. lack of harmonization in defining investee companies’ level of involvement in socially controversial activities.

In any case, we believe that minimum ESG standards should be foreseen for products marketed as ESG.

6. Overall, we are supportive of the approach and the proposed amendments to the MiFID II Delegated Directive Articles on product governance.

7. We agree with the proposed changes to the ESMA guidelines on MiFID II product governance.

However, with regard to the proposed case study, we would like to highlight that the carbon footprint measures a negative impact on the environment and not positive impact.

Also, we would suggest the following amendments: The fund aims to provide explicit positive impact on the environment, to **be identified – whenever possible – according to the upcoming EU Taxonomy.....** More than 70% of the fund is invested in projects certified as “green projects”, **according to the EU Taxonomy. The share of 70% was chosen on the basis.... The remaining 30% is invested in.... No % of the fund is invested in.... (list of excluded sectors shall be provided, for example coal equities shall be always excluded).**

8. We agree with the proposed approach.
9. First, we believe that the good governance should be the general case and should be promoted through appropriate legislations.

We also believe that the EU Taxonomy Regulation will provide the approach on how environmental criteria shall be considered separately, while however respecting some minimum social clauses. In the same time the EU Ecolabel - which should be very ambitious - could provide an approach for how both the environmental and social criteria shall be considered together.

10. See response to question 5.
11. With regard to the proposed amendments to paragraph 28 of the ESMA guidelines on aspects of the MiFID II suitability requirements: we believe that paragraph 28 should specify that investment firms should also proactively ask questions to identify the types of investments that shall be excluded according to the sustainability preferences of their clients. The latter is particularly important because the overarching goal of the sustainable finance agenda is to re-orient capital flows towards sustainable investments and not only support the demand for green assets.

Therefore, clients should be informed by the investment firms about how investments in unsustainable economic activities have negative environmental and/or social impacts. In order to express their sustainability preferences, the clients need to be provided with full information which can allow them to understand the possible trade-offs (in both financial and non-financial terms) between the different types of investments.

12. See response to question 9.
13. We agree with the amendments to the paragraph 70.
14. FW is not in a position to provide any estimate of the compliance cost for the private sector. However, for the purpose of this consultation we do not believe that it is a relevant question given that any measure aimed at promoting the capital shift towards sustainable investments would greatly benefit society as a whole (and many of those benefits cannot be and should not be monetized, like the benefits to the society of avoiding CO2 emissions). So, in this sense it can be assumed that any compliance costs, expected to be borne by the investment firms, would be certainly offset by benefits to society and so the measures in question comply with the Kaldor–Hicks criterion and would certainly lead to an improvement in the net societal welfare.