**BRIEFING PAPER**

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# NGO recommendations for a sustainable EU retail investment policy

This briefing focuses on the **retail[1] investment aspects of the Renewed Sustainable Finance Strategy and on the sustainability aspects of the Retail Investment Strategy. It does not aim to cover all retail finance related issues.**

The Commission's Action Plan on sustainable finance from March 2018, building on the final report of the High Level Expert Group on sustainable finance (HLEG) included Action 4 '*Incorporating sustainability when providing financial advice'*. On that basis, amendments were introduced to delegated acts (Level 2) of the Markets in Financial Instruments Directive (MiFID II) and Insurance Distribution Directive (IDD). They require investment firms to ask retail investors about their sustainability preferences: this is a positive step forward.

However, they only represent a first step that should be complemented: sustainability preferences in retail investments is an issue that is both too complex and too significant (35 trillion euros at stake according to Eurostat) to be addressed by these two delegated acts alone. Ensuring financial markets respond appropriately to retail investor sustainability preferences requires further policy changes.

In addition, the new Capital Markets Union (CMU) Action Plan from September 2020 developed retail investment issues in Actions 7 and 8; it also referred to European long-term investment funds (ELTIFs) in Action 3, stating that they should help to "*ultimately channel more funding, including from retail investors, into the EU's real economy*".

**This is why it is very welcome that the Commission prepares both a Renewed Sustainable Finance Strategy for July 2021, and an unprecedented, horizontal Retail Investment Strategy for early 2022.**

[1] The retail investor is defined in this paper as an individual, non-professional investor.

**For that purpose, we have set up ten complementary recommendations to incorporate sustainability aspects in EU retail investment policy**: they should be part of both the Renewed Sustainable Finance Strategy and the Retail Investment Strategy to ensure an integrated, comprehensive EU approach mainstreaming sustainability in retail investment.

**Our ten complementary recommendations are structured in two parts:**

## A. Focus on distributors: sales and distribution process

1. Monitor whether financial “advisors” properly ask retail clients about their sustainability preferences
2. Require minimum sustainability competencies of financial “advisors”
3. Align the interests of financial “advisors” with those of their retail clients
4. Require that sustainably denominated funds are systematically proposed as a default retail option (subject to the adoption of recommendations 7 and 10)
5. Ensure that fintech safely empowers retail investors to identify financial products that best match their sustainability preferences

## B. Focus on financial market participants: origination of financial products and product features

6. Disclose sustainability information in a clear, standardised and accessible manner to non-expert retail investors
7. Establish minimum standard for sustainability denominated funds
8. Ensure retail investor engagement
9. Adequately finalise the EU Ecolabel for financial products
10. Require that sustainability impacts of sustainability denominated financial products on the real economy are evidenced.

# A. Focus on distributors: sales and distribution process

## 1. Monitor whether financial "advisors"[2] properly ask retail clients about their sustainability preferences

This recommendation concerns the suitability assessment performed for "advised services" under MiFID II (Art. 25.2) and IDD (Art. 30.1). Unfortunately, the appropriateness test (performed for "non-advised services", except execution-only) only requires the client to disclose information about their knowledge and experience in the field relevant to the product in question: as such, it seems that so far the sustainability preferences cannot be taken into account for non-advised services.

We fear that the amendments introduced in the MiFID II and IDD Delegated Acts are not granular enough to ensure that retail investor sustainability preferences are properly accounted for in the financial "advisor"'s financial product recommendation. Recent research[3] shows that properly eliciting a retail client's sustainability preferences is a complex task. ESMA will be releasing revised guidance on the suitability assessment to take account of the changes implemented through the Delegated Acts: this revised guidance should be as detailed as possible to provide a useful source of guidance for financial "advisors". Indeed, the majority of stakeholders (61%) in the Commission's public consultation on the Renewed Sustainable Finance Strategy agreed that financial "advisors" should have detailed guidance when they ask questions to retail investors. **We also recommend that ESMA produce a template questionnaire to provide more granular guidance to financial "advisors"**, in order to improve compliance and reduce risks of liabilities.

In addition, the new requirements in the MiFID II and IDD Delegated Acts will have to be implemented by financial "advisors". Another question relates to regulatory oversight of record keeping obligations in respect of a client's sustainability preferences and the suitability assessment more generally. ESMA should review the regulatory oversight practices of national competent authorities (NCAs) to assess if supervision is sufficient to ensure proper implementation of the changes implemented through the Delegated Act and coordinate supervisory actions with NCAs. **For that purpose, ESMA should carry out a mystery shopping exercise** to assess how financial "advisors" implement the new requirements and to assess the types of ESG products that are advised to clients.

The ultimate outcome should be threefold:

(i) the retail client is asked in a meaningful way about its sustainability preferences, building on the ESMA template questionnaire;
(ii) retail client's preferences are recorded and supervised adequately;
(iii) retail client's preferences are dully considered and reflected in the product selection.

➔ File: ESMA oversight.

[2] The EU legislation does not refer to advisors but to the "advice" which is regulated as a marketing practice. The 2018 Commission's study on the distribution systems of retail investment product confirmed BETTER FINANCE findings, i.e. that investment products are not bought but sold, and that an average individual investor is not able to differentiate between the benefits and risks of different types of advice or sales. In reality, many non-independent advisors are sellers of in-house products. The 2018 Commission's study confirmed that an average retail investor seeking personal advice would tend to go to non-independent advisors via banks and insurers (believing it's "free" advice and being unaware of incentive schemes and potential conflicts of interests) and end up with relatively similar investments "recommendations" across Member States in terms of product types, i.e. in-house investment funds and life insurance policies. https://ec.europa.eu/info/sites/default/files/180425-retail-investment-products-distribution-systems_en.pdf.

[3] 2° Investing Initiative (2020), A Large Majority of Retail Clients Want to Invest Sustainably.

# 2. Require minimum sustainability competencies of financial "advisors"

The MiFID II and IDD Delegated Acts require financial "advisors" to ask retail investors about their sustainability preferences, and shall take them into account for offering suitable financial products.

**This unavoidably requires that financial "advisors" have a certain level of sustainability expertise**, to be able to (i) ask their retail clients the right questions and (ii) properly understand their retail clients' response and process it to provide the right financial product recommendation.

Quite problematically, research from Aviva Investors[4] from September 2020 showed **45% of "advisors" admitted to having "no ESG training at all"**. Despite the fact that most "advisors" (92%) believed ESG investing would constitute a larger part of their business in two years' time, this was not translating to their current day-to-day practice. Just over a third (35%) said they took ESG into consideration every time they discussed investment options with their clients.

At the national level, the French financial market supervisor AMF decided in February 2021 to create a specific module to verify the sustainability-related competences of financial professionals, and to give more weight to sustainability issues in the general AMF certification for financial professionals, by almost quadrupling the number of sustainability questions in the general exam (from 4 to 15)[5].

At EU level, in the new CMU Action Plan[6] the Commission announced that it would seek to improve the level of professional qualifications of "advisors" in the EU and assess the feasibility of setting up a certificate to prove their level of knowledge and qualifications. In the Commission's public consultation on the Renewed Sustainable Finance Strategy, integrating sustainable finance literacy in the training of financial professionals and in the curricula of schools were indicated to be prominent actions for the EU to develop. **We recommend that this certificate is also set up to prove the sustainability-related knowledge of financial "advisors" in relation to the financial products they sell**. This could be addressed by specific and continuous trainings: sustainability training should be a requirement for professional qualifications for "advisors" under the IDD and MiFID II.

In addition, retail distributor companies and trade organizations should also consider developing tools to help their constituency to analyze the sustainability features of the investment products they intend to promote to their clients.

➔ Files: MiFID II (review of MiFID II in 2022) and IDD (review of IDD in 2023); EIOPA work on IDD review and consultation being launched soon.

[4] https://www.ftadviser.com/investments/2020/10/21/half-of-advisers-untrained-in-esg-despite-looming-rule-change/.
[5] https://www.amf-france.org/fr/actualites-publications/communiques/communiques-de-lamf/lamf-renforce-les-exigences-de-certification-professionnelle-en-matiere-de-finance-durable.
[6] Action 8 : « *Finally, it will seek to improve the level of professional qualifications for advisors in the EU and assess the feasibility of setting up a pan-EU label for financial advisors* » ; https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2020:590:FIN

# 3. Align the interests of financial “advisors” with those of their retail clients

The payment of inducements to financial “advisors” leads to biased financial advice, and has played a key role in many recent mis-selling scandals, as shown by BEUC[7] and BETTER FINANCE[8]. **Conflicts of interests in the distribution channels of retail investment products should be eliminated, by banning the receipt and retaining of monetary or non-monetary remuneration of financial “advisors”.** Certain practices adopted by investment professionals (“advisors” or sellers of financial products) give rise to conflicts of interests and lead to a breach of their general duty of care, i.e. to act in the best interest of the client. One major source for such conflicts of interests is the receipt and retaining of commissions or fees ("inducements", paid by third-parties not on behalf of the client, such as manufacturers of investment products). In such situations, the interest of the investment professional cannot be perceived as to be aligned anymore with the interest of the client. Therefore, as done in the UK and in the Netherlands, a full prohibition for investment “advisors” or sellers of investment products (including in insurance markets) from receiving and retaining fees should be enacted.

At the very least, the payment of inducements to financial intermediaries should be banned in the case of execution-only services in MiFID II, while the MiFID II rules applicable to “independent advice” and to portfolio management should be replicated under IDD. In the absence of a full ban on inducements, investor protection rules between MiFID II and IDD should be aligned to ensure full transparency of inducements for clients, and a requirement for all financial “advisors” to provide a quality-enhancing service to their clients should be ensured.[9]

- ➔ Files: MiFID II (review of MiFID II in 2022) and IDD (review of IDD in 2023).

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[7] https://www.thepriceofbadadvice.eu/.

[8] https://betterfinance.eu/wp-content/uploads/publications/Misselling_of_Financial_Products_in_the_EU_-_Briefing_Paper_2017.pdf.

[9] Current MiFID II rules include inducement disclosure and requirement to provide a quality enhancing service and duty to act in best interest of the client. These rules in principle ban the receipt and retaining of inducements (any monetary or non-monetary benefits, except minor ones) for “independent advice” and portfolio management. But the exceptions have allowed investment firms to re-orient to services where inducements are allowed (non-advised services and execution-only), circumventing the spirit of the law. On the other hand, IDD (which covers a much larger share of EU households’ financial savings) allows inducements as a general rule and only exceptionally bans them.

# 4. Require that sustainably denominated funds are systematically proposed as a default retail option (subject to the adoption of recommendations 7 and 10)

An overwhelming majority of 70% or more of retail investors want their money to be invested in a sustainable way, as found by many studies very consistently over the last years[10]. **Such a strong majority should reverse the current 'opt in' system (in which the retail investor needs to explicitly express its demand to invest in a sustainable way) to an 'opt out' system (in which the retail investor is proposed by default a sustainable investment option and needs to opt out in case of disagreement).** This would be more consistent with the evidence about sustainability preferences of retail investors: in the new system, proposing sustainable financial products should become the new normal for financial "advisors". In the Commission's public consultation on the Renewed Sustainable Finance Strategy, the majority of stakeholders (61%) agreed that retail investors should be systematically offered sustainable investment products, while only a small minority disagreed (16%).

**Investing sustainably must become the 'easy choice'** for consumers when investing their money as long as protective measures against greenwashing are put in place (see recommendations 7 and 10). For instance, in future, ESG investments should be offered by default to consumers when choosing to invest in the default option (the Basic PEPP) of the new pan-European Pension Product (PEPP) that will become available to consumers in March 2022.

However, it is very important to ensure that the financial profile of sustainable investment products is not compromised: sustainable funds' financial risks (especially the two key risk components for the retail investor: the probability of loss and the magnitude of loss) and financial performance must still be carefully assessed, considered and disclosed to the retail investor. The retail investor must be crystal clear on what the underlying risks and returns of the selected products are, both in terms of product's sustainability and financial aspects.

➔ Files: MiFID II (review of MiFID II in 2022) and IDD (review of IDD in 2023).

[10] For example Natixis (2016), Mind shift: getting past the screens of responsible investing; Schroeders (2017), Global Perspectives on sustainable investing; Maastricht University (2019), "Get Real, Individuals Prefer More Sustainable Investments; University of Cambridge (2019), "Walking the talk: Understanding consumer demand for sustainable investing" or see overview in 2° Investing Initiative (2020a), "A Large Majority of Retail Clients Want to Invest Sustainably".

# 5. Ensure that fintech safely empowers retail investors to identify financial products that best match their sustainability preferences

The development of fintech will very likely play an increasingly important role in retail investment. Consumers need access to independent comparison tools when making investment decisions, allowing retail investors to easily compare the cost and features of investment products (including how sustainable they are). In its final report, the CMU High Level Forum Report issued a recommendation that the European Commission should "*consider ways to promote the development of independent digital comparison tools*" for retail investors[11]. **It should be ensured that these developments follow minimum requirements (e.g. for transparency, sustainability criteria, suitability questionnaire, matching algorithm, impact claims, data quality) to enable retail investors better compare financial products and identify those that best correspond to their sustainability preferences, e.g. through online robo-advisors and apps.** If those minimum requirements will not be established, there is a high risk that financial products will be misallocated since they might not fit to retail investors actual preferences.[12]

Several non-commercial initiatives show best practices in terms of transparency, sustainability criteria, suitability questionnaire and data quality and financial product universe:

- 2° Investing Initiative launched the responsible investing online platform **Mein Fair Mögen**[13] ('My Fair Money')[14] which will be made available for 28 EU countries this year with the objective of helping retail investors to better integrate sustainability into their investment decisions;
- The Finansportalen website[15] in Norway allows retail investors to easily compare life insurance, investment funds and pension products
- The Fair Finance Guide[16] promotes consumer awareness by ranking financial institutions according to sustainability criteria.

We make the following difference between non-commercial independent comparison tools and fintech / robo-advisers services:

- Independent comparison tools do not receive any revenues from product providers, and offer impartial/objective comparisons to consumers about investment products available on the market. They are a disclosure tool for consumers, and do not offer any regulated investment advice to clients;
- Fintech and robo-advice services offer regulated investment advice to consumers. They either charge fees or could potentially receive inducements for the advice that they give - although BETTER FINANCE has not found publicly available evidence of robo-advisor receiving any monetary or non-monetary benefit ("inducements") for recommending a certain financial instrument or product.[17] [18]

[11] https://ec.europa.eu/info/sites/default/files/business_economy_euro/growth_and_investment/documents/200610-cmu-high-level-forum-final-report_en.pdf.
[12] 2° Investing initiative (2020). "Swipe Left" Warum es bei nachhaltigen Finanzprodukten keine Matches gibt.
[13] https://www.meinfairmögen.de.
[14] https://2degrees-investing.org/2-investing-initiative-launches-first-of-its-kind-responsible-investing-platform/.
[15] https://www.finansportalen.no/.
[16] https://fairfinanceguide.org/. Fair Finance International is an international civil society network of over 100 CSOs and allies, coordinated by Oxfam, that assesses the sustainability policies and practices of private banks and other financial institutions. In the EU specific analysis is available for financial institutions in Belgium, Germany, Netherlands and Sweden.
[17] https://betterfinance.eu/publication/robo-advice-5-0-can-consumers-trust-robots/.
[18] BETTER FINANCE analysed whether the robo-advisors selected for "mystery shopping" provide independent advice or not based on their regulatory disclosures and on the disclosures on their websites. However, in the last report, it has been observed that 2 out of 12 platforms do not adequately disclose whether the investment advice is provided on an independent basis or not pursuant to Art. 24(4)(a)(i) MiFID II. Unfortunately, four others (of those who do make a reference to non-receipt of commissions) do not adequately indicate that advice is independent and what this entails, as required by Art. 52 MiFID II DR.

In addition, there is a need to establish dedicated sustainable regulatory sandboxes to test and identify inefficiencies of financial product innovations for retail investors and to set out minimum requirements (e.g. for transparency, sustainability criteria, suitability questionnaire, matching algorithm, impact claims, data quality) to minimize the risks stemming from for-profit fintech business models that could result in breaches of investor protection and ethical rules. According to BETTER FINANCE research on Robo-advisors[19], **the European platforms under scope that offer sustainable financial products fail to ask about retail client's sustainability preferences**, and thus fail to advise retail clients about suitable sustainable financial products (also in terms of asset allocation and risk level). ESMA should consider policy actions to improve these processes, such as developing more detailed guidelines on investor questionnaires, on asset allocations or risk profiles (see Recommendation 1).

➔ Files: MiFID II (review of MiFID II in 2022) and IDD (review of IDD in 2023).

# B. Focus on financial market participants: origination of financial products and product features

## 6. Disclose sustainability information in a clear, standardised and accessible manner to non-expert retail investors

Retail investors need access to clear, concise and understandable sustainability information in order to make use of this information for investment decisions.

**Critical sustainability information about financial products for retail investors should be integrated in a standardised manner in their Key Information Document (KID).** This means that it is necessary to be more specific than what is currently required under Art. 8(3)(c)(ii) of the Packaged Retail Investment and Insurance-Based Products (PRIIPs) Regulation[20]. As seen in the delegated act of the PRIIPs Regulation[21], there is no further indication on what the "*specific environmental or social objectives*" mean or should encompass.

**Sustainability information should be incorporated in two sub-sections of the KID:**

- First, in the "*description of the type of retail investor to whom the PRIIP is intended to be marketed*" (Art. 8(3)(c)(iii) PRIIPs Regulation and Art. 2(3) of the Delegated Act) – here the manufacturer or distributor (depending on who is drafting the KID) must specify whether the product is designed to cater (also) the sustainability preferences of retail investors;
- Second, in the description of the investment objectives, policy, and underlying assets (Art. 8(3)(c)(ii)

[19] https://betterfinance.eu/wp-content/uploads/Robo-Advice-Report-2020-25012021.pdf.
[20] "The key information document shall contain the following information: (…) where applicable, specific environmental or social objectives targeted by the product".
[21] Commission Delegated Regulation (EU) 2017/653.

PRIIPs Regulation and Art. 2(2) Delegated Act) where specific sustainability information should be disclosed.
- In addition, for Multi-Option PRIIPs (MOPs) the generic KID should specify:
  - the two above-mentioned aspects, at a general level;
  - whether any of the possible underlying instruments or products may not satisfy sustainability preferences;
  - the specific KID for the underlying option should be drafted under the same rules as the first two points above, specifying (if applicable) how the sustainability target of the instrument is aligned with that of the MOP.

**Regarding the PEPP KID**, the Level 1 regulation requires PEPP manufacturers to include "*information, where available, related to the performance of the PEPP provider's investments in terms of ESG factors*" (Art. 28(3)(c)(xii) PEPP Regulation). We believe such information is insufficient and should be also complemented by more granular aspects in terms of sustainability aspects.

**The climate alignment score of a given fund should be systematically presented to retail investors** in the KID based on a simple disclosure label. For example, simple disclosures could provide an indication about whether the fund is aligned with international climate scenarios such as a Paris-compliant 1,5°C or well below 2°C pathway, or is heading towards climate chaos above +4°C. Alternatively, a coloured rating system similar to the well-known energy label[22] (dark green category A is the most sustainable while red G category the least sustainable) should be provided to investors. There are now tools in the market enabling such analysis, and several investors provide it. However, to date the various methodologies and metrics results in a broad range of scorings and ratings that can be inconsistent, which make minimum requirements for such ratings and scorings necessary. It would be positive that the Commission assesses how to help accelerate methodological innovation and improvement of such tools[23]. The HLEG, in its priority recommendation on retail investment, recommended: "*The objective is to help retail investors to understand the impact of their savings through a small range of metrics that should remain simple and understandable. (…) To help the industry in overcoming methodological obstacles, the Commission should support and encourage the development of a common set of sustainability impact metrics and proxies*"[24].

**It should be made transparent in the KID if a given product is sustainable and why, but also if a given product does not take sustainability factors into account: a warning should be introduced in the KID**. Such a provision has already been introduced in the Articles 6 and 7 of the Taxonomy Regulation, requiring that for financial products subject to Article 8 or not subject to Article 8 or 9 of the Disclosure Regulation for investors (hereafter SFDR, see below), the following statement shall be mentioned:
- Article 6 Taxonomy Regulation (for Art 8 products under SFDR): '*The "do no significant harm" principle applies only to those investments underlying the financial product that take into account the EU criteria for environmentally sustainable economic activities. The investments underlying the remaining portion of this financial product do not take into account the EU criteria for environmentally sustainable economic activities.*'
- Article 7 Taxonomy Regulation (for products not subject to Art 8 or Art 9 under SFDR): '*The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities'* (though less technical and more understandable wording should be provided for retail investors).

Another source of inspiration could be the PRIIPs "comprehension alert"[25], which warns consumers for complex financial products with a higher risk of biased payouts and hidden fee structures, discouraging

[22] See for example BEUC recommendation: https://www.beuc.eu/publications/beuc-x-2020-102_how_to_make_sustainable_finance_real_for_consumers.pdf. Another alternative could be a thermometer-shaped indicator.
[23] Building for example on these assessments : https://www.tcfdhub.org/wp-content/uploads/2020/10/PAT-Report-20201109-Final.pdf, and https://www.louisbachelier.org/wp-content/uploads/2020/07/rapport-0607.pdf.
[24] HLEG Final report, p28-29.
[25] More details at https://www.bettereurope.eu/2017/03/blog-priips-comprehension-alert/.

getting involved in such products: "*You are about to purchase a product that is not simple and may be difficult to understand*".

Ultimately, the taxonomy alignment of a given fund should also be systematically presented to retail investors in a simply way.

**In addition, it is critical to clarify the different categories of financial product articulated in Article 8 and 9 of SFDR.** An Article 8 products "*promote, among other characteristics, environmental or social characteristics*", while an Article 9 product "*has sustainable investment as its objective*": Article 8 products are understood as 'light green' and Article 9 products as 'dark green'. The ESA's letter to the Commission dated 7 January 2021 articulated the need for (broader) clarification in this area. Currently the market does not have a uniform interpretation, which risks being to the detriment of retail investor understanding of the financial products they are investing in. It is critical that this is addressed in order to ensure clarity and consistency, and for retail investors to be able to properly distinguish between these two categories of financial product - notably through the forthcoming Regulatory Technical Standards from ESAs.

➔ Files: Undertakings for Collective Investments in Transferable Securities (UCITS), PRIIPs, PEPP, ELTIFs.

# 7. Establish minimum standard for sustainability denominated funds

Promoting retail investor confidence in the financial products they are investing in is a crucial issue to be tackled by regulatory authorities. This problem is particularly acute in relation to financial products which claim to have an impact in the real economy[26] (see Recommendation 10) but is apparent for all financial products with sustainability aspects.

The HLEG, in its priority recommendation on retail investment, recommended: "*The Commission should protect retail investors by preparing an analysis of minimum SRI standards, in line with the EU sustainability taxonomy, to be respected by manufacturers and targeting all funds (…). Such analysis could later on feed into the PRIIPs and potentially the UCITS V regulations*."[27]

While the enhanced disclosure requirements introduced in the SFDR are a positive step, disclosure alone cannot be sufficient to ensure a minimum playing field for sustainably denominated funds. There is no evidence so far to what extent transparency on e.g. positive and negative screening criteria or voting behavior and greenwashing practices have improved so far. **It should be assessed whether the framework of SFDR disclosure requirements can provide a basis for establishing minimum standards for sustainably denominated funds**. This would have the benefit of ensuring consistency and not overly complexify the EU agenda on sustainably denominated funds (see also the separate section 9 on the EU ecolabel).

➔ Files: UCITS, PRIIPs, PEPP, ELTIFs.

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[26] 2° Investing Initiative, EU Retail Funds' Environmental Impact Claims Do Not Comply with Regulatory Guidance.
[27] HLEG Final report, p29.

# 8. Ensure retail investor engagement

Individual investors by nature are usually long-term oriented as their investing horizon and savings needs such as pension, housing, child education, transmission of wealth are long term. Accordingly, more than 80% of their total assets (including real estate) and more than 60% of their financial assets are long-term ones (i.e. retirement, housing, children's studies, transmission of wealth) according to BETTER FINANCE. But **retail investors are most often prevented from engaging into investee companies, in particular cross-border**. For example, individual investors still encounter barriers when it comes to exercise their voting rights (in particular at cross-border), propose resolutions and ask questions at annual general meetings (AGM); they often do not receive the necessary information for participation and voting from e.g. brokers or are required to pay far higher costs than for voting at national level despite Shareholder Rights Directive II obligations. In addition, legislation in some Member States sets a minimum threshold of shares for tabling resolutions that is completely out of reach for retail investors, which de facto sidelines them and makes the tool of investors resolutions reserved for large investors only.

The existing barriers for retail investors to engage with investee companies should be eliminated: this can be done by amending the Shareholder Rights Directive II. Given their well evidenced overwhelming support for sustainable investments, the involvement of retail investors can be critical, for example, for climate, environmental, decent wages or human rights resolutions. In addition, AGMs should remain open fora for retail investors too, and the development of online AGMs (started by the pandemic) should lead to an improvement not a weakening of retail investors' rights to access AGMs[28].

**The Shareholder Rights Directive II should be turned into a regulation and adequate and harmonized supervision should be mandated. In addition, provisions should ensure that requirements to table AGM resolutions are not impossible to meet for retail investors.**

Furthermore, when retail clients invest through a financial product, structural barriers in the financial system such as intermediation in the investment chain[29] means that retail investor preferences on environmental and social issues are not reflected in votes cast at company general meetings. Individual shareholders should be able to vote on the sustainability reporting of the company in the same way as it is possible to vote on the annual report of the company. In addition, individual shareholders should be given the possibility to ask questions (more than one) at the general meetings. Thus, a better governance should ensure that companies take into consideration and reply to all the questions asked during the shareholder meeting. The weak governance of EU-domiciled intermediated investment products (pension plans, investment funds, etc.) should also be addressed to better ensure that the voice and preferences of the end investors are better taken into account (for example the US have recently required all mutual funds to include independent directors in their boards to represent the interests of fund investors).

**Addressing misaligned voting practice is a critical step to achieving the EU's environmental objectives and securing a financial system which is accountable to its citizens.[30]**

➔ File: Shareholder Rights Directive II, MiFID II.

[28] ShareAction developed specific recommendations for the future of AGMs: https://shareaction.org/wp-content/uploads/2021/01/Future-of-the-AGM.pdf.
[29] ShareAction study on proxy-voting: https://shareaction.org/research-resources/voting-matters-2020/.
[30] 2° Investing Initiative, Retail Clients Want to Vote for Paris.

# 9. Adequately finalise the EU Ecolabel for financial products

The EU Ecolabel is positioned as the label of excellence. Its rules must match the sustainability expectations of retail investors and meet the ambition of the European Green Deal.

The latest version of the EU Ecolabel rules are a step in the right direction, but they should be tightened, in particular for specific exclusion criteria, and for assessment and verification mechanisms by national competent authorities to assess compliance with the detailed Ecolabel rules. In addition, in due time, the European Commission should expand the EU Ecolabel to cover more product groups, such as pension schemes. Finally, the EU Ecolabel should also have a clear approach on the actual impact of labelled investment products (see recommendation 10).

➔ File: EU Ecolabel for financial products (on-going).

# 10. Require that sustainability impacts of sustainability denominated financial products on the real economy are evidenced

Addressing greenwashing requires a sophisticated approach to the concept of investor impact (to be differentiated with the concept of investee company impact). Ben Caldecott, founding director of the Oxford Sustainable Finance Programme and senior advisor to the chair and CEO of the Green Finance Institute, stated: "*You can have lots of green in a portfolio and have little or even no impact*"[31]. He concludes: "*If a product is claiming – explicitly or implicitly – it will make a difference, it should be clear how it will do it and there should be an accountable and transparent way of measuring the claimed contribution over time*."

With the rapid development of sustainably-denominated financial products, it is becoming increasingly important to assess the impact they have on making the real economy more sustainable. This is critical for retail investors, who expect positive impact in the real economy if they chose a sustainability-denominated financial product.

While at macroeconomic level taxonomy alignment is a very useful and relevant indicator, it is more complex to assess the investor impact at fund level[32]: this requires several metrics. For example, it is acknowledged that investing in illiquid private equity can have more impact on the ground than investing the same amount in very liquid public equity. In addition, issues like fund's capacity to make a positive change, stewardship, shareholder engagement, AGM voting are issues that must be assessed and measured to determine the real impact of a given investor and of a given fund. For example, the FinanceMap[33] from InfluenceMap calculates a climate engagement score for large investors that relies on a methodology with eleven indicators[34].

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[31] https://www.ipe.com/viewpoint-investing-in-green-doesnt-equal-greening-the-world/10043518.article.
[32] 2° Investing Initiative, A Climate Impact Management System for Financial Institutions (for consultation)
[33] https://www.financemap.org/.
[34] https://www.financemap.org/site/data/007/768/FinanceMap_Methodology_Jan_2021(1).pdf. The eleven indicators are as follows : 1 Engagement Transparency, 2 Climate Engagement Framework, 3 Milestones for Success, 4 Escalation Strategy, 5 Engagement on Paris Aligned Business Models, 6 Engagement on Climate Lobbying, 7 Climate Engagement Impact, 8 Collaborative Engagement, 9 Resolutions: Voting Transparency, 10 Resolutions: Climate-Relevant Voting, 11 Use of Shareholder Authority.

In the Commission's public consultation on the Renewed Sustainable Finance Strategy, a very large majority of stakeholders (75%) agreed that it is important to better measure the impacts of financial products on sustainability factors. Actions that the EU should take on the issue include the establishment of clear and simpler indicators, ensuring a harmonised framework, improving public and private compliance and transparency (e.g. considering coherent disclosure requirements, and including impact monitoring along the entire value chain).

**There is an urgent need to build evidence on the environmental impact of different investment strategies and techniques and to ensure that the regulatory and policy framework is designed to reflect the scientific evidence.**

Currently there is no specific regulatory guidance governing the content of environmental impact claims in the finance sector. 2° Investing Initiative has conducted several reviews of the marketing claims of 'sustainable funds' available to European retail investors and found that most environmental impact claims reviewed were misaligned with generally applicable regulatory guidance.[35]

**Alongside building the evidence on the environmental impact of different investment strategies, a responsible marketing framework for the finance sector is required for consumer protection, legal certainty and developing best practices.**

[35] 2° Investing Initiative, EU Retail Funds' Environmental Impact Claims Do Not Comply with Regulatory Guidance.

## For further information

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