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BANKING AND FINANCE

Public consultation on institutional investors and asset managers' duties regarding sustainability

Fields marked with * are mandatory.

Introduction

At the end of 2015, governments from around the world chose a more sustainable path for our planet and our economy by adopting the Paris agreement on climate change and the UN 2030 Agenda for Sustainable Development.

Sustainability has since long been at the heart of the European project. The EU is committed to development that meets the needs of the present without compromising the ability of future generations to meet their own needs (Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions 'Next steps for a sustainable European future European action for sustainability' {SWD(2016) 390 final}).

The EU wants its financial system to be aligned with its sustainability objectives. The commitment to incorporating sustainability elements into EU financial services policies and cross cutting initiatives is ingrained in the Mid-Term Review of the Capital Markets Union Action Plan (Mid-Term Review of the Capital Markets Union Action Plan - COM(2017) 292 final).

To develop the overall vision of sustainable finance that this requires, the Commission decided last year to appoint a High-Level Expert Group (HLEG) on sustainable finance under the chairmanship of Christian Thimann. This group is supporting the Commission to develop an overarching and comprehensive EU strategy on sustainable finance.

On 13 July 2017, the HLEG published its interim report which provided a comprehensive vision on sustainable finance. It identified two imperatives for Europe's financial system. "The first is to strengthen financial stability and asset pricing, by improving the assessment and management of long term risks and intangible factors of value creation. The second is to improve the contribution of the financial sector to sustainable and inclusive growth by financing long-term needs and accelerating the shift to a sustainable economy".

In its interim report (EU High-Level Expert Group on Sustainable Finance, 'Financing a sustainable European economy' Interim report, July 2017), the HLEG proposed eight early recommendations for policy action on sustainable finance. The third recommendation focused on establishing a "fiduciary duty" that encompasses sustainability. The HLEG suggested clarifying that the duties of institutional investors and asset managers explicitly integrate material environmental, social and governance (ESG) factors and long term sustainability.

Given the maturity and the interest of the HLEG recommendation, the Commission has decided to start work on an impact assessment to assess whether and how a clarification of the duties of institutional investors and asset managers in terms of sustainability could contribute to a more efficient allocation of capital, and to sustainable and inclusive growth.

The duties of care, loyalty and prudence are embedded in the EU's financial framework governing obligations that institutional investors and asset managers owe to their end-investors/scheme members. These duties are the foundation of investment process.

The implementation of these duties implies fulfillment of various obligations for asset managers and institutional investors that include, for instance, the duty to act in the best interest of beneficiaries /investors, with due care, skill and diligence in performing their activities, including the identification and management of conflict of interests. They are also required to act honestly, and ensure adequate and proportionate performance of their activities.

Although these duties are embedded in the EU financial legal framework, it appears unclear that they require institutional investors and asset managers to assess the materiality of sustainability risks (i.e risks relating to environmental, social and governance issues). Market practices indicate that institutional investors and asset managers generally understand these duties as requiring a focus on maximising short-term financial returns and disregard long-term effects on performance due to sustainability factors and risks. This can lead to misallocation of capital and might give rise to concerns about financial stability since markets can be vulnerable to abrupt corrections, such as those associated with the delayed transition to low carbon economies.

This consultation will help the Commission gather and analyse the necessary evidence to determine possible action to improve the assessment and integration of sustainability factors in the relevant investment entities' decision-making process.

Please note: In order to ensure a fair and transparent consultation process **only responses received through our online questionnaire will be taken into account** and included in the report summarising the responses. Should you have a problem completing this questionnaire or if you require particular assistance, please contact fisma-investors-duties-sustainability@ec.europa.eu.

More information:

- on this consultation
- on the protection of personal data regime for this consultation

Glossary

Relevant investment entities: entities managing assets entrusted to them

Sustainability factors: for the purpose of this consultation, sustainability factors refer to environmental, social and governance issues as defined by the United Nations Environment Programme (UNEP) (*UNEP Inquiry, Definitions and Concepts: Background Note, 2016*). The exact scope of sustainability factors to be addressed is also the object of this consultation.

Environmental issues relate to the quality and functioning of the natural environment and natural systems including biodiversity loss; greenhouse gas emissions, renewable energy, energy efficiency, natural resource depletion or pollution; waste management; ozone depletion; changes in land use; ocean acidification and changes to the nitrogen and phosphorus cycles

Social issues relate to rights, well-being and interests of people and communities including human rights, labour standards, health and safety, relations with local communities, activities in conflict zones, health and access to medicine, consumer protection; and controversial weapons.

Governance issues relate to the management of investee entities. Issues include board structure, size, diversity, skills and independence; executive pay; shareholder rights; stakeholder interaction; disclosure of information; business ethics; bribery and corruption; internal controls and risk management; and, in general, issues dealing with the relationship between a company's management, its board, its shareholders and its other stakeholders.

1. Information about you

* Are you replying as:

- ○ a private individual
- ● an organisation or a company
- ○ a public authority or an international organisation

* Name of your organisation:

ShareAction

Contact email address:

The information you provide here is for administrative purposes only and will not be published

eleni.choidas@shareaction.org

* Is your organisation included in the Transparency Register?
(If your organisation is not registered, we invite you to register here, although it is not compulsory to be registered to reply to this consultation. Why a transparency register?)

- ● Yes
- ○ No

* If so, please indicate your Register ID number:

75791956264-20

* Type of organisation:

- ○ Academic institution
- ○ Company, SME, micro-enterprise, sole trader
- ○ Institutional investor
- ○ Consultancy, law firm
- ○ Consumer association
- ○ Industry association
- ○ Media
- ● Non-governmental organisation
- ○ Think tank
- ○ Trade union
- ○ Other

* Where are you based and/or where do you carry out your activity?

Belgium

* Field of activity or sector (*if applicable*):

at least 1 choice(s)

- [ ] Accounting
- [ ] Auditing
- [ ] Banking
- [ ] Credit rating agencies
- [ ] Insurance
- [ ] Occupational pension provision
- [ ] Personal pension provision
- [ ] Collective Investment Management
- [ ] Individual portfolio management
- [ ] Financial advice
- [ ] Market infrastructure operation (e.g. CCPs, CSDs, Stock exchanges)
- [ ] Service provider (e.g. index provider, research providers)
- [x] Other
- [x] Not applicable

* Please specify your activity field(s) or sector(s):

Non-governmental organisation working on responsible investment

Important notice on the publication of responses

* Contributions received are intended for publication on the Commission's website. Do you agree to your contribution being published?
(see specific privacy statement)

- (x) Yes, I agree to my response being published under the name I indicate (*name of your organisation /company/public authority or your name if your reply as an individual*)
- ( ) No, I do not want my response to be published

2. Your opinion

2.1 Questions addressed to all respondents:

I. General overview

1) Do you think relevant investment entities should consider sustainability factors in their investment decision-making?

- (x) Yes
- ( ) No

No opinion

Please explain the reasons:

(please note that links to all references are provided in an attached file)

Financial risk mitigation: 1) Idiosyncratic risk: investors should consider ESG factors in order to protect loss of value of a portfolio due to drops in share price through, inter alia, potential litigation, reputational damage, higher costs of capital, etc. Evidence shows that all these may result from a failure to properly consider ESG factors in the decision-making process, with notable cases being the VW emissions scandal and the Deepwater Horizon explosion. 2) Systemic risk: this risk is macroeconomic in nature and cannot be mitigated through diversification. Recent work by the ESRB has identified exposure to fossil-fuel reserves and stranded assets as particularly conducive to this kind of risk. (1)

Long-term value creation: by investing in companies with strong ESG performance, investors encourage companies to invest more themselves, create more jobs and contribute to the real economy, as well as mitigate environmental and social damage in their operations. Evidence shows that ESG performance and stock price are positively correlated in the long-term. (2)

Compliance with regulation/soft law standards/meeting public commitments: these include elements of IORPS II, SRD II, France's Art 173, as well as the aspirations of the Paris Agreement, Agenda 2030, the UNGPs on Business and Human Rights (argued to be binding on investors), the OECD Guidelines for Multinational Enterprises (through which complaints have been brought against investors) and more. (3)

Influence and leverage: The UN has recognised that investors are responsible for not incentivising illicit corporate and governmental behaviour, which may occur by not incorporating ESG factors in their portfolio construction, stewardship, and more activities. (4)

Fiduciary duty: Jurisdictional legal analyses have shown that there are no legal barriers to the integration of ESG factors in fiduciary duty. (5)

Client demand: Evidence shows that not only is there increasing demand for ESG amongst retail investors but also misalignment between what clients are interested in and what is currently offered to them in terms of products. (6)

Evolving industry practice: Surveys show that EU pension funds expect their ESG asset allocation approaches to increase and that engagement and voting practices related to ESG are also showing an upward trend.As such, investors should consider ESG factors in order to maintain or develop their competitive edge. (7)

2) What are the sustainability factors that the relevant investment entities should consider? (Please make a choice and indicate the importance of the different factors (1 is not important and 5 is very important). (Please refer to the definition in the Glossary).

	Yes	No	No opinion
Climate factors (these include climate mitigation factors as well as climate resilience factors)	●	○	○

Other environmental factors	●	○	○
Social factors	●	○	○
Governance factors	●	○	○
Others	○	○	●

Importance for climate factors:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Importance for other environmental factors:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Importance for social factors:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Importance for governance factors:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Please specify, which specific factors within the above categories you are considering, if any:

We believe that a categorisation of ESG factors according to importance does not give due regard to their interrelation in the creation of a sustainable financial system as a whole.

Instead, investors should consider all factors which are material to their operations, as well as those non-financially significant to their beneficiaries, which may be equally material across the aforementioned categories.It is impossible to develop an exhaustive list of specific factors which would correspond to each category, as this would depend on asset class, investment strategy, industry, country and client segment (8). In addition, the concept of materiality itself is ever-evolving and subject to, amongst others, changing stakeholder norms (9).

Nonetheless, the absence of a clear definition of specific factors has been mentioned as an impediment to the sustainability of the financial system by both industry (10) and civil society actors (11). As such, we recommend that the Commission propose a minimum set of factors against which due diligence should be performed, an approach which would allow discretion to investors while also mitigating major potential risks to both the investment and the environment/society. This approach to materiality is consistent with the approach in the Non-Financial Reporting Directive, which designates potential risk through the effect to the business activity to society and the environment, not just the effect of a societal and environmental factor on the performance of the business. Harmonising the two approaches to materiality should be a priority for the Commission.

Such minimum standards could be developed using the UN PRI's definition, the UNEP FI definition mentioned in this consultation document, as well as the scientific evidence proposed by the concept of planetary boundaries. We note that a similar approach is already present in the Non-Financial Reporting Directive, which stipulates that information should be provided in relation to matters "most likely" to be material (12). As such, by considering factors "most likely" (recital 8) to be material in different asset classes, as well as those relevant from a systemic perspective, we believe the Commission (in consultation with academia and civil society) is well-placed to develop such a set of factors which should then be explicitly inserted in all financial legislation.

3) Based on which criteria should the relevant investment entities consider sustainability factors in their investment decision making?

Please explain:

This question is adequately addressed from the evidence provided in Q1. Financial risk mitigation (both idiosyncratic and systemic), long-term value creation, alignment with regulatory, soft law and public policy developments, compatibility with non-financial interests of beneficiaries and clients, increasing industry practice and client demand, as well as responsible discharging of influence and leverage over corporate and government behaviour are all important criteria to consider when investors and their intermediaries construct portfolios, extend mandates, select stocks and value securities.

4) Which of the following entities should consider sustainability factors in their investment decision-making? (Possibility to select several answers). If so, please indicate the level of impact that this would have (1 is the smallest impact and 5 is the highest impact).

	Yes	No	No opinion
Occupational pension providers	●	○	○
Personal pension providers	●	○	○
Life insurance providers	●	○	○
Non-life insurance providers	●	○	○
Collective investment funds (UCITS, AIF, EuVECA, EuSEF, ELTIF)	●	○	○
Individual portfolio managers	●	○	○

Please explain:

All of the aforementioned investment entities should consider sustainability factors in their investment decision-making, as they all exercise direct or indirect discretion over an end-investors' capital, as well provide that capital to companies and governments whose use of it is directly correlated with the health of the environment, communities and the planet as a whole. Nonetheless, the process of consideration and integration may be influenced depending on asset class and investment strategy as tied to the particular class of investor.

We believe that institutional asset owners are in a special position in this regard, as they sit at the top of the capital market chain and are directly accountable to beneficiaries and clients. The mandates they draw towards subsequent intermediaries can have a multiplying effect across the investment chain. As a recent report by the UN PRI (13) concluded: the signals sent by these actors determines the willingness of investment consultants and managers in integrating sustainability factors in their subsequent functions.

We would also like to note that asset managers, despite not having beneficiaries whose liabilities may be inserted into their balance sheets, may in certain cases be more influential over investment governance than asset owners, due to their advice, product offerings and resources.

We recommend that the Commission not limit the scope of which actors should consider ESG factors, but rather focus on the problem of ensuring transmission of appropriate mandates concerning sustainability between the aforementioned entities. This applies both to the appropriate selection of asset managers, investment consultants and proxy advisers as well as to a process of ongoing due diligence as to how those subsequent intermediaries are performing in relation to ESG. This is necessary in order to mitigate the remoteness created by increasingly lengthy and complex investment chains and to ensure that all actors operate under clear expectations vis-a-vis their stance towards sustainability. Such model mandates could be prepared by the ESAs.

We would like to note the importance of proxy advisors in this context as well.

Level of impact for occupational pension providers:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Level of impact for personal pension providers:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Level of impact for life insurance providers:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Level of impact non-life insurance providers:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Level of impact for collective investment funds (UCITS, AIF, EuVECA, EuSEF, ELTIF):

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

Level of impact for individual portfolio managers:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ● 5

II. Problem

5) To your knowledge, what share of investment entities active in the EEA (European Economic Area) currently consider sustainability factors in their investment decisions?

	All or almost all	More than two thirds	More than half	More than a third	None or almost none	No opinion
Occupational pension providers	○	○	○	○	●	○
Personal pension providers	○	○	○	○	●	○
Life insurance providers	○	○	○	○	●	○
Non-life insurance providers	○	○	○	○	●	○
Collective investment funds (UCITS, AIF, EuVECA, EuSEF, ELTIF)	○	○	○	○	●	○
Individual portfolio managers	○	○	○	○	●	○

6) To your knowledge, which is the level of integration of sustainability factors by the different investment entities (active in the EEA)?

	High integration	Medium integration	Low integration	No integration	No opinion
Occupational pension providers	○	○	○	○	●
Personal pension providers	○	○	○	○	●
Life insurance providers	○	○	○	○	●
Non-life insurance providers	○	○	○	○	●
Collective investment funds (UCITS, AIF, EuVECA, EuSEF, ELTIF)	○	○	○	○	●
Individual portfolio managers	○	○	○	○	●

7) Which constraints prevent relevant investment entities from integrating sustainability factors or facilitate their disregard. Please provide the importance of the different constraints that you consider relevant (1 is not important and 5 is very important).

	1	2	3	4	5	No opinion
Lack of expertise and experience	○	○	○	●	○	○
Lack of data/research	○	○	○	●	○	○
Lack of impact on asset performance	○	○	●	○	○	○
Inadequate methodologies for the calculation of sustainability risks	○	○	○	●	○	○
Inadequate sustainable impact metrics	○	○	○	●	○	○
Excessive costs for the scale of your company	○	○	●	○	○	○
No interest from financial intermediaries	○	●	○	○	○	○
No interest from beneficiaries/clients	○	●	○	○	○	○
European regulatory barriers	○	○	○	○	●	○
National regulatory barriers	○	○	○	○	●	○
Lack of fiscal incentives	○	○	○	●	○	○
Lack of eligible entities	○	○	●	○	○	○
Others	○	○	○	○	○	●

Please provide more details on what the constraints/reasons are and how they limit the integration of sustainability factors:

Prudential regulation (both at macro and micro levels and both at EU and domestic levels) does not typically explicitly include ESG factors in macroeconomic forecasting, the assessment of systemic risk, or consider them central to consumer protection in the offering of appropriate products or in how individual investment firms consult with their clients on their investment preferences. The Commission must ensure that both macro and micro prudential standards send the correct signals to banks and investors, most notably through the proposed ESAs sustainability mandate and the review of barriers to equity investments under Solvency II. In addition, accounting standards should lessen triennial valuation pressures for short-term nominal returns, identified as a key barrier to ESG integration according to a recent survey Hermes Asset Management (13).The valuation of assets and liabilities under accounting standards should consider long-term characteristics when determining "fair value" under mark-to-market valuation. Policymakers and regulators have to ensure they send the correct signals to investors, as lack of incentives are not just prevalent within investment and lending chains but also exist between regulatory frameworks and investment practice. At the level of individual investors, evidence shows that few contract ESG expertise or incorporate ESG factors in the selection of managers, in setting fiscal incentives and in the drawing of mandates (14). The lack of a standardised approach to corporate reporting results in the production of incomparable data, which is then accentuated by the multiple formats used by data providers in distributing this information (15). The forthcoming review of the Non-Financial Reporting Directive poses an important opportunity for increased harmonisation of corporate reporting. Finally, inadequate consultation with beneficiaries/retail clients on their financial and non-financial interests as those relate to sustainability allows investors to be insulated from having an informed opinion of what constitutes "the best interests" of their end-investors (16).

8) How challenging is it for relevant investment entities to integrate the different sustainability factors? (1 is not challenging and 5 is very challenging) - Please refer to the definition in the Glossary).

	1	2	3	4	5	No opinion
Climate factors (*these include climate mitigation factors as well as climate resilience factors*)			X			
Other Environment factors		X				
Social factors		X				
Governance factors			X			
Others						X

Please explain:

We cannot accurately determine the exact level of difficulty in integrating these different sustainability factors, as the question does not adequately clarify the level of integration required. For example, In a general sense, research shows that climate-related factors are most readily quantifiable and incorporated in the investment decision-making, possibly because of the connection made between climate and systemic risk. This has resulted in a proliferation of standards-based, performance oriented measurements (CDP, Newsweek's Green Rankings, etc) which set industry standards and allow comparability, facilitating integration.A recent article in the Economist outlined the difficulties in integrating S factors in decision-making, citing a well-known study by NYU Stern, which outlines the multitude of frameworks and unhelpful approach to ascertaining the materiality of these factors (focusing primarily on commitments and processes, rather than on the real-life effects of these commitments), producing voluminous data which may not be useful to investors. Governance factors are also relatively well developed. A recent survey by the CFA institute, addressed towards its members, reported that governance factors, primarily board accountability, rank as the highest incorporated sustainability consideration in 2017 (17).As such, evidence would show that social factors tend to be the hardest to incorporate in investment decision-making. Nonetheless, we note that this is not the result of inadequate frameworks, as a multitude does exist. We believe that social factors, especially those pertaining to human rights, are often deemed "subjective" and "culturally determined". While to a certain extent this is true, human rights obligations of states and non-state actors are codified both in binding international human rights instruments as well as soft law, which, as explained in the answer to Q1, has been interpreted as binding to investors. Reporting frameworks resulting from these obligations, such as the UN Guiding Principles Reporting Framework, could be used as an indicator for the development of a pan-European framework setting out minimum requirements for their integration in investment decision-making.

III. Policy options

9) In which area should relevant investment entities consider sustainability factors within their investment decision-making? Please make a choice and indicate the relevance of the different areas (1 is minor relevance and 5 is very high relevance).

	Yes	No	No opinion
Governance	◉	○	○
Investment strategy	◉	○	○
Asset allocation	◉	○	○
Risk management	◉	○	○
Others	◉	○	○

Please specify others:

Investment entities should incorporate sustainability considerations in all of the aforementioned areas, including in stewardship. Risk management is a potentially significant departure point in order to effect change across the rest of the functions. In a recent survey by BNP Paribas Securities Services, 23% of investors view risk management as their biggest concern, leading them to review asset allocation strategies twice a year (18).Yet, a survey by Allianz Global Investors showed that risk management strategies have barely evolved since the outbreak of the financial crisis, focusing on intense diversification by asset class, geography or duration management (19). Diversification, nonetheless, is an not a technique which may account for ESG-related concerns resulting from systemic risk, such as climate change. This indicates that investors routinely do not take systemic risk into account in their risk management procedures.

By encouraging investors to take account of systemic and long-term risk in their risk management processes, policymakers can thus incentivise them to review governance structures, investment strategies and asset allocation with a long-term perspective. An area not explicitly mentioned is stewardship, which can also be influenced by a long-term view to risk management. Investment entities must ensure that sustainability factors are incorporated in their selection of proxy advisors and engagement with companies.

Relevance for governance:

○ 1

○

2
○ 3
○ 4
◉ 5

Relevance for investment strategy:

○ 1
○ 2
○ 3
○ 4
◉ 5

Relevance for asset allocation:

○ 1
○ 2
○ 3
○ 4
◉ 5

Relevance for risk management:

○ 1
○ 2
○ 3
○ 4
◉ 5

Relevance for others:

○ 1
○ 2
○ 3
○ 4
◉ 5

10) Within the area of governance, which arrangements would be most appropriate to enable the integration of sustainability factors? (1 is the not appropriate and 5 is the very appropriate).

	1	2	3	4	5	No opinion
Specific sustainability investment Committee	◉	○	○	○	○	○
Specific sustainability member of the Board	○	○	○	○	◉	○
Sustainability performance as part of remuneration criteria	○	○	○	○	◉	○
Integration of sustainability factors in the investment decision process	○	○	○	○	◉	○
Integration of sustainability checks in the control process	○	○	○	○	◉	○

Periodic reporting to senior management/board	○	○	○	○	●	○
Others	○	○	○	○	○	●

11) Should insurance and pension providers consult their beneficiaries on an annual/periodic basis on their preference as regards sustainability factors?

- ● Yes
- ○ No
- ○ No opinion

Please explain:

Consultation with beneficiaries is a necessary tool in ensuring that investors align their investment horizons and liabilities with those whose capital they manage. This is particularly important in the context of the proliferation of Defined Contribution pension schemes, where beneficiaries both provide the capital and bear the investment risk. The need for consultation is further underlined by an abundance of evidence showing misalignment between client preferences and product offerings. In addition, the beneficiaries of pension funds and insurance policies often have the long-term liabilities which are compatible with long-term sustainable investment, as such, by consulting with beneficiaries and ascertaining these liabilities, investors can truly say in practice that they are acting in the best interests of their beneficiaries/clients. In addition, case law on the interpretation of fiduciary duties has concluded that the "best interest" of beneficiaries is not exclusively confined to profit maximisation over any time horizon - non-financial, including ethical concerns, can only be ascertained if they are consulted on.This is true particularly in cases where the incorporation of sustainability factors may have a neutral or negative impact on the performance of a portfolio, beneficiaries should be consulted in order for their providers and trustees to ascertain consensus, risk appetite and approval of the investment. Many investors have taken a pragmatic approach and consult beneficiaries through their elected representatives, or by determining simple majorities. Ways of consulting with beneficiaries include webinars, open meetings, roadshows, etc.

12) Within the portfolio's asset allocation, should relevant investment entities consider sustainability factors even if the consideration of these factors would lead to lower returns to beneficiaries/clients in the medium/short term?

- ● Yes
- ○ No
- ○ No opinion

Please explain:

Sustainability factors should normally be assessed over the long-term, not in the medium/short term. As such, when investors align their investment windows with the liabilities of their beneficiaries and focus on long-term returns, lower returns in the medium/short-term may be acceptable. A recent study by Harvard Law School indicated that 47% of asset owners and 43% of asset managers recognise that sustainability factors produce tangible returns and exhibit outperformance after five years or more, not discounting possible reductions in returns in a shorter timeframe (20). Divestment and negative screening are a case in point. Recent academic work on "sin stocks" has shown that by their exclusion, investors cannot always offset a short-term dip in portfolio performance (21. Nonetheless, the rationale followed is one of mitigating long-term liabilities. In addition, lower returns may be acceptable when considering that financial benefit is not the only component of the beneficiary interest to be considered, even in the long-term. By providing legal clarity that the best interest of beneficiaries does not lend itself simply to financial interests, investors should have the confidence to pursue investment strategies that may provide lower returns, to a certain extent, without fear of liability, as long as beneficiaries have been adequately consulted. Guidance to this effect was released by the UK's Law Commission in its review of the fiduciary duties of investment intermediaries, which proposes a two-part test for ascertaining the admissibility of losses to a portfolio: those losses should not cause too high of a financial detriment to the fund and trustees should have good reason to believe that beneficiaries would approve of the lower returns, for example, through adequate direct consultation or consultation with their elected representatives (22). It was recently announced that this review may become law in the UK. In addition, in order to ensure the principle of impartiality, the issue is not just whether there are lowered returns but how the loss is distributed amongst classes of beneficiaries, if applicable. If by accepting a lower return in the short-term, investors are safeguarding the longer-term liabilities of the same class of beneficiaries, as well as those of future beneficiaries, then the loss may be acceptable.

13) Within the area of risk management, does the current set of corporate disclosures provide the relevant investment entities with adequate information to perform sustainability risk assessments in respect of investee companies?

- ○ Yes
- ◉ No
- ○ No opinion

Please explain where the possible gaps are, if any:

The current state of corporate reporting presents a number of gaps which may impede the quality and usefulness of data provided to investors, leading to inadequate risk assessments. The overarching limitation is a lack of standardisation of reporting frameworks, which discourages comparability and impedes stock selection and securities valuation based on sustainability factors. A 2016 survey by PwC concluded that 92% of the investors participating believe that companies are not disclosing information which is useful and comparable, a stark contrast with the 60% of companies who think their data is comparable (23). The same survey found that only 29% are confident in the quality of ESG data as provided, and prefer it verified by an independent third party. In addition, a study by NYU Stern called "Putting the S in ESG proposed evidence that corporate reporting on social factors is predominantly characterised by reporting on commitments and processes, rather than the real-world effects of these commitments .The upcoming review of the Non-Financial Reporting Directive is an important opportunity to ensure that these limitations are mitigated by promoting harmonisation and coherence of reporting frameworks.On climate reporting, a way to promote harmonisation is through the integration of the TCFD Recommendations as a component of the reporting requirements of the Directive.

14) Do the overall information or risk metrics available enable the relevant investment entities to adequately perform sustainability risk assessments?

- ○ Yes
- ◉ No
- ○ No opinion

Please explain where the possible gaps are, if any:

We believe that available risk metrics are not adequate to perform sustainability risk assessments properly. As the responses to the Commission's consultation on long term and sustainable investment concluded, the emphasis on backward-looking analysis focused on financial factors is a major impediment in proper integration of sustainability factors in the investment decision-making process. The development of forwardlooking scenario analysis would fill a very important gap in the current state of ESG data, possibly through the use of analytics, computer science and big data. The TCFD's technical supplement on the issue could be used as important guidance in the development of such analyses at EU level. In addition, there is a particular absence of risk metrics to accurately measure physical and transition risks resulting from climate change. A 2017 white paper by Deutsche Bank Asset Management called this absence a "major data gap" (24). Finally, an analysis of 12 leading ESG frameworks measuring social factors has concluded that social measurement tends to measure what is convenient, not meaningful, that current approaches to disclosure are not likely to help identify leaders in best practice, that differing standards create "noisiness" and "data fatigue", and, finally, that current risk metrics and measurements do not equip investors to respond to the demand for socially responsible products and investing strategies (25). Nonetheless, it is important to note that gaps in risk metrics should not be used as an impediment from performing sustainability risk assessments - stewardship activities may be used as a way to influence corporate behaviour not adequately or usefully accounted for by risk metrics.

15) Do you think that uniform criteria to perform sustainability risk assessments should be developed at EU level?

- (•) Yes
- ( ) No
- ( ) No opinion

Please explain:

We believe that a "minimum standards" approach would satisfy the need for flexibility as well as respond the confusion created by lack of cohesive guidance, the latter having been identified as a barrier to sustainable investment (26). We propose a basic methodology of sustainability risk assessments which could be developed at EU level. These assessments would still allow discretion to investors while setting minimum standards on the processes and metrics used to integrate sustainability in their investment decision-making, perhaps customised to different asset classes. Both quantitative ESG data as well as qualitative processes (such as stakeholder engagement) should inform these assessments. We believe that useful guidance on the development of such baseline risk assessments could be provided by the UN Guiding Principles Reporting Framework, a comprehensive framework for the identification and reporting of human rights issues related to corporate activity and which investors can use as guidance for due diligence towards investee companies. In addition, the OECD Guidelines for Responsible Business Conduct for Institutional Investors provide guidance on the assessment of risks related to human and labour rights, the environment and corruption in investment portfolios. The TCFD guidance on scenario analysis could be used as a framework for the development of such an approach as well. While concerns may be raised as to the competency of the EU to develop and mandate such assessments, we believe that this would be compatible with the exclusive competences of the EU in the conservation of marine biological resources, commercial policy, and the shared competencies covering the environment, consumer protection, energy, agriculture and fisheries, as well as economic and social cohesion (Art 3 and 4, TFEU).All of these areas are potentially significantly impacted by the absence of appropriate risk assessments by both corporates and investors.

16) In case material exposure to sustainability factors is identified, what are the most appropriate actions to be performed by the relevant investment entity?

In terms of overall investment strategy and In the case of positive material exposure (by either investing or refraining from investing in a particular entity) research has shown that the investment technique which is most likely to fully capitalise on opportunities connected to ESG factors as well as mitigate ESG-related risks is full ESG integration (27) Full ESG integration refers to a systematic and explicit inclusion of ESG risks and opportunities in all facets of investment analysis, as opposed to excluding certain industries or engaging in thematic/impact investment (which should also be a possibilities).If the material exposure is negative to the performance of the portfolio, investors should consult with beneficiaries to determine risk appetite and consensus in proceeding with the investment.In a practical sense, prioritisation according to expected magnitude and determination of whether portfolio companies are able to respond to these risks are practical steps identified by Robeco as resulting from materiality assessments (28). Determining the ability of portfolio companies to respond may result in leveraging change through the exercise of shareholder rights, including through investor coalitions, and may conclude in divestment if in line with the overall investment strategy.

17) Should relevant investment entities disclose how they consider sustainability factors within their investment decision-making?

- (selected) Yes
- No
- No opinion

Please explain:

Mandatory disclosure has been identified as one of the most effective ways to ensure that sustainability factors form part of the investment decision-making process, more so than adherence to stewardship codes (30).Disclosure would vary depending on audience: beneficiaries, regulators, and the public. In terms of beneficiaries, the Statement of Investment Policy should be used to disclose which ESG factors are identified and taken into account, which are not and the reasoning behind this decision, as well how financial and non-financial interests are ascertained. Sustainability factors can also be reflected through information on major holdings, the use of shareholder rights and information on the use of passive investment vehicles - especially about the extent to which those allow a true valuation of stocks based on company performance on ESG. Past ESG performance should also be mandated in pre-contractual disclosure to beneficiaries, with clear indication of it not being a predictor of future performance, as well as information on development of an ESG investment strategy if it has been absent.The public should have access to annual accounts and non-commercially sensitive information on major shareholdings and the exercise of voting rights. This kind of disclosure is necessary so that civil society organisations and academics may be able to scrutinise investment practices and provide much-needed analysis to aid in the developed of best practices and other aspects of sustainable investment (29). Finally, for supervisory purposes, investors should disclose their governance structures and how those relate to sustainability risk assessment and management, their general risk assessment procedures as well as ongoing supervision and mitigation of ESG risks. This information is necessary in order to provide a holistic view of how sustainability considerations relate to consumer protection. Under the proposed sustainability mandate of the ESAs, the authorities could be tasked with releasing best practices in the identification and mitigation of ESG risks.

If yes, what areas should the disclosure cover? Please make a choice and indicate the relevance of disclosure within the different areas (1 is minor relevance and 5 is high relevance):

	Yes	No	No opinion
Governance	(selected)		
Investment strategy	(selected)		
Asset allocation	(selected)		

Risk management	◉	○	○
Other	○	○	◉

Relevance for governance:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ◉ 5

Relevance for investment strategy:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ◉ 5

Relevance for asset allocation:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ◉ 5

Relevance for risk management:

- ○ 1
- ○ 2
- ○ 3
- ○ 4
- ◉ 5

If yes, where?

	Yes	No	No opinion
Pre-contractual disclosure (e.g. prospectuses)	◉	○	○
Semi-annual/annual reports	◉	○	○
Periodic reports	◉	○	○
Website	◉	○	○
Newsletters	◉	○	○
Factsheets	◉	○	○

Marketing materials	○	●	○
Others	○	○	●

IV. Impacts for stakeholders

18) Which stakeholder groups would incur costs and which would benefit from integrating sustainability factors within investment decision-making by relevant investment entities?

	Benefits	Costs
Occupational pension providers	☑	☑
Personal pension providers	☑	☑
Life insurance providers	☑	☑
Non-life insurance providers	☑	☑
Collective investment funds (UCITS, AIF, EuVECA, EuSEF, ELTIF)	☑	☑
Individual portfolio managers	☑	☐
General public	☑	☐
Retail investors	☑	☑
Financial advisors	☑	☐
Service providers (index provider, research providers…)	☑	☐
Other stakeholders (please specify)	☐	☐

Please explain:

The incursion of costs on behalf of investors has been identified as significant barrier in the pursuance of sustainable investment practice . Research by BNP Paribas has shown that both asset owners and asset managers expect costs to becoming an increasing barrier to sustainable investment in the future (30).It is true that considering ESG factors in investment decision making does create additional out-of-pocket costs through the acquisition of appropriate expertise and provision of data and analytics. Additionally, ensuring adequate internal training to existing staff in different functions may also bear costs. These costs are not always distributed evenly across the investment chain. For example, the incursion of sell-side investment research costs under MiFID II may put additional cost burdens on investors but create opportunities for financial advisors and service providers. In addition, the long-term window in which outperformance based on sustainable investment is expected may imply tolerance of short-term dips in returns.Evidence has shown that the majority of investors face a J-curve in terms of the costs incurred, meaning that they are borne upfront but tend to even out as integration of ESG factors in the decision-making process intensifies (31).At a more micro level, it has been argued that investors may incur costs by employing ESG integration techniques that limit diversification within a portfolio, such as negative screening. Nonetheless, evidence has shown that while negative screening may result in short-term dips in risk-adjusted returns, these dips diminish as the intensity of screens applied increase (32).As such, costs incurred may also depend on the strategy used, adding more nuance to whether and how costs related to sustainable investment materialize and how.These costs are likely to be offset by both sustainable investment returns in terms of the performance of individual portfolios, and by the promotion of corporate activity that fuels the real economy, promotes job creation and healthy productivity, as well as contributes to social and environmental resilience (33).All of these factors can be adversely influenced if investors don't integrate ESG factors in their decision-making, creating an environment in which market failures and other macroeconomic conditions may adversely impact the health of the economy as a whole.In the short term, smaller funds may offset costs by pooling resources and consolidating their ESG expertise and research provision.

2.2 Questions addressed to end-investors

1) Do you take into account sustainability factors when you choose your investment products or investment entity?

- Yes
- No

3. Additional information

Should you wish to provide additional information (e.g. a position paper, report) or raise specific points not covered by the questionnaire, you can upload your additional document(s) here:

c7d30ee5-5e5f-49e6-8ad3-cc0a757f9a78/ShareAction_-_References_-_Investors_duties_Consultation.pdf

Useful links

More on the Transparency register (http://ec.europa.eu/transparencyregister/public/homePage.do?locale=en)

Consultation details (https://ec.europa.eu/info/consultations/finance-2017-investors-duties-sustainability_en)

Specific privacy statement (https://ec.europa.eu/info/files/specific-privacy-statement-institutional-investors-and-asset-managers-duties-regarding-sustainability_en)

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