ESMA Call for Evidence

Integration of sustainability preferences in the suitability assessment and product governance arrangements – Fédération Bancaire Française (FBF)'s response

The FBF thanks ESMA for taking the initiative of publishing this Call for Evidence, which allows us to present the implementation difficulties encountered by investment firms in applying the new requirements of the Delegated regulation (EU) 2021/1253 and the Guidelines 35-43-3172.

We believe that these difficulties may have affected the expected wide distribution of ESG products to retail investors and we hope that ESMA, through its Q&As, will provide some flexibility in its guidelines.

We draw ESMA's attention to the suggestions of Q&As we make in our responses to questions 8 and 20.

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Q1: What actions did firms implement within their organisation to take into account the new requirements related to sustainability preferences? Please elaborate especially on the following:

• What proportion of firms' employees (differentiating between client facing staff and the other staff) have received training on sustainability topics? What did these trainings consisted of? Was any test or exam put in place?

FBF members told us that many of their staff have received training on sustainable topics.
But *all staff who provide information or advice on financial instruments have received such training*, including how to ask clients about their sustainability preferences, as recommended in ESMA guidelines. These employees are also trained in how to ask clients about their sustainability preferences when distributing insurance-based investment products (IBIPs), in accordance with EIOPA guidance[1].

These courses (on-site or online) generally end by a test or a quiz.

In France, the AMF (the competent national authority) has introduced a certified examination on sustainable finance (optional) which many employees of investment firms have taken or intend to take.

• Which conflicts of interest relating to the integration of clients' sustainability preferences did firms identify and which measures did firms take to ensure that these conflicts of interest do not damage the interest of clients?

[1] See Guidance EIOPA-BOS-22-391

Any conflict of interest relating to the integration of clients' sustainability preferences would be dealt with under the existing system for managing conflicts of interest implemented in investment firms.

Q2: Are there specific aspects of sustainable finance that retail investors struggle to understand? For example:

- **Understanding of general aspects such as why it is important to consider sustainability risks and factors when investing?**

  Investment firms' clients generally have no difficulty understanding the environmental issues that are widely reported in the media.

- **Understanding differences between sustainable products and products without sustainability features?**

  Retail clients understand why it is important to take sustainability risks and factors into account their investments and have a quite good understanding of the differences between "sustainable products" and "products without sustainability features."

- **Understanding that sustainability characteristics and (expected) return are two separate issues?**

  Clients know that sustainability features and returns are two different concepts, but they sometimes worry that sustainable investments will be less profitable than others.

  In a recent survey conducted by Opinion Way for the AMF, based on a representative sample of 2001 people aged 18 and over, 71% of respondents said they give priority to the security of an investment/a product, 60% to its profitability, 53% to its futures availability and only 26% to its ESG/SRI dimension[2].

  This could explain the relatively slow start to investment in sustainable products by retail clients since the second half of 2022.

- **Understanding the new legal definition of "sustainability preferences" and its components (e.g., categories a), b) and c), minimum proportion, principal adverse impact indicators (PAIs) etc.)?**

  Retail clients find it very difficult to understand the legal definition of sustainability preferences and especially the distinction between categories a) and b). As a result, when financial advisors ask them about the minimum proportions of a) or b) products they want, they do not always know what to say.

  They seem to have less difficulty understanding the category c) thanks to the subcategories understandable (environment, social, governance), which are more meaningful. Nevertheless, the concept of PAI (the individual PAI indicators) remains difficult to understand for retail clients.

  In all case, before asking the client for his preferences, explanations are provided to him/her on all the concepts mentioned in the above points.

Q3: Are there specific financial education initiatives on sustainable finance developed by consumer associations, trade associations or other organisations and that are used by investment firms that you can bring to ESMA's attention? Please accompany your reply with any relevant background information on the initiative and/or with details on its effectiveness/usefulness.

[2] Please, refer to page 14 of the survey : https://www.amf-france.org/sites/institutionnel/files/private/2023-07/The%20French%20and%20Responsible%20investments%20-%20OpinionWay%20for%20AMF%20-%20July%202023_0.pdf

Our members tell us that all the content of their brochures, web pages, webinars etc. on sustainable finance has been developed in-house.

In France, financial education initiatives are often taken by professionals themselves, by their professional associations[3] or by public entities: Banque de France, AMF, Institute for Public Financial Education, etc.

Q4: What is the main way firms currently provide information to retail clients about sustainable finance? For example:
- **Orally during the meetings with clients**
- **Through educational brochures or other (paper) documents**
- **Through dedicated website and apps**
- **A combination of the above**
- **Other**

A combination of the above.
During the meeting with clients, when firms asking them for their sustainability preferences, some of them use information brochures as well as videos.

In your opinion, are these approaches effective? Please provide details. Are retail clients satisfied with the quality of information provided?

Yes, we believe that these approaches are effective and that clients are satisfied with information provided.

In the survey mentioned above, 80% of respondents said they are satisfied or somewhat satisfied with the information provided by their bank or financial adviser on their environmental, social and governance (ESG) preferences[4].

However, retail clients still have much difficulty of comprehension with the concepts introduced under Article 2(7) of the MiFID II delegated regulation, such as "sustainable investment", "taxonomy" (and the difference between a and b products).

In the survey mentioned above, 74% of those questioned admitted that they did not know what the taxonomy was (76% for SFDR). We can therefore imagine that it will probably take a long time for clients to understand all the concepts and topics linked to sustainable finance.

Q5: What are clients' experiences/reactions to the new questionnaires including questions on "sustainability preferences"? (e.g. do they require guidance to be able to answer to the questions? Do they show interest in the topic?)

Clients find the questionnaire difficult to understand and do not have a clear enough idea of the minimum proportion of product a) or b) they want. This difficulty is an obstacle to the expression of detailed preferences.

Q6: Are there practical examples of questions used to collect information from clients on their sustainability preferences that you can share with ESMA? (as for other parts of this CfE, respondents can opt for their input to ESMA not to be made public)

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[3] For instance, the FBF notably participated to the creation of *l'Observatoire de la finance durable* with other financial professional associations with the contribution of the LIFE program of the European Union. This Observatory disseminates information on sustainable finance (see its website [Home - Finance durable (observatoiredelafinancedurable.com)](https://observatoiredelafinancedurable.com)

[4] Please refer to page 69 of the survey : https://www.amf-france.org/sites/institutionnel/files/private/2023-07/The%20French%20and%20Responsible%20investments%20-%20OpinionWay%20for%20AMF%20-%20July%202023_0.pdf

For these specific questions, we let our members answer individually, because a global answer would make no sense, since each of our members has implemented its own system, depending on its organisation, the type of clients its serves or the functionalities of its IT system.

Q7: Which of the sustainable investment definitions do clients most often opt for? (EU Taxonomy alignment? Sustainable investment within the meaning of SFDR? Consideration of PAI? All of them?) Please provide any statistics, where available.

It seems that a majority of clients indicate that they do not wish to express preferences in terms of sustainability. Of those who do, the majority say they cannot choose between a), b) and PAIs and opt for standardized preferences proposed by the firms. According to our members, less than 5% of their retail clients, of those asked about their sustainability preferences, expressed specific preferences. Of these, the majority has opted for products in category b) and/or PAIs.

Q8: How are firms collecting information from clients on their preferences concerning the minimum proportion? With regards to the use of standardised minimum proportions, which standardised minimum proportions are presented to clients?

Many clients who express an interest in sustainable products are unable to say whether they want product a) or b) and in what minimum proportion. They often don't know what to ask and ask the advisor in turn.

FBF members have sometimes adopted slightly wider minimum proportions than those suggested in paragraph 27 of the guideline 2 (minimum 20%, minimum 25%, minimum 30%) because clients are not able to express their preferences with such precision. However, they have presented percentages in a neutral manner as required by this paragraph.

Paragraph 26 of the guideline also mentions that information on the sustainability preferences of the client should be sufficiently granular to allow for a matching of the client's sustainability preferences with the sustainability-related features of financial instruments.

It is therefore important that the "minimum proportions" are compatible with existing products.

However, for a large proportion of products, the degree of alignment with the taxonomy is zero or very low and according to asset managers, the taxonomy's commitment rates should only be available in the second half of 2024. This is therefore sometimes difficult to explain to clients, when investment firms ask them about their preferences in products a) that they have few or no suitable products to offer them.

It would then be welcomed if ESMA could clarify in the Q&A:

> **- that it is not necessary to offer the full range of products a) and b) from 5% to 95% and that is more appropriate to take account of the market situation**
>
> **- that the rates offered may be different for products a) and b), as the offer is very different for these 2 product categories.**
>
> **- that the 5% jumps indicated in paragraph 27 of the guideline 2 are only indicative and, as indicated above, covering the entire 0-100% spectrum would be pointless (particularly for products a), given the current state of the offer.**

Such clarifications would provide flexibility in terms of procedures and operational approaches, as expected by respondents to the consultation on the ESMA suitability guidelines (see paragraph 17 of the ESMA Call for evidence).

ESMA could also indicate in its Q&As that investment firms are allowed for a transitional period (2023 to 2024) to give their clients guidance on the actual state of the market of certain financial instruments when they are asked about their sustainability preferences (for example, indicating that the range of instruments aligned with the taxonomy is still limited)[5].

Q9: What is approximately the average minimum proportion of sustainable investments requested by clients? Please provide details, where available.

These minimal proportions differ from one firm to another, but they appear to be fairly low.

Q10: Are firms currently able to satisfy the sustainability preferences expressed by clients (in particular in relation to the three categories (Taxonomy, SFDR, PAI))? If so, for which categories and/or types of financial instruments do firms find it most difficult to satisfy clients' preferences?

As mentioned above, investment firms find it difficult to offer a wide range of products and therefore to satisfy, when taking into consideration the other suitability requirements, including level of risk and diversification, the client's preference when he/she has expressed a wish to invest in a high minimum proportion of this product category.
The most difficult preferences to satisfy are those relating to products aligned with the taxonomy.

Q11: How often has the adaptation of clients' sustainability preferences been necessary during these first months of application of the rules (e.g. in terms of percentage considering new clients and existing clients whose profiles have already been updated to include information on sustainability preferences)?

Our members tell us that it is too early to answer this question because the data they have is insufficient to be meaningful.

Q12: What kind of operational arrangements have firms put in place to allow clients to adapt their sustainability preferences?

When a client adapts his/her sustainability preferences, this request is documented in the suitability report as requested in paragraph 83 of the guideline 8 of the ESMA guidelines.

Q13: How were clients informed about the possibility to adapt their preferences?

The information can be provided to the client for instance when his/her questionnaire is being fulfilled, with the provision of the suitability report, by the sales team or during the discussion with the financial advisor, when the latter finds that he cannot offer a suitable product corresponding to the preferences the client has expressed.

Q14: Have firms imposed limits on how frequently a client can adapt its sustainability preferences during the investment advice?

No, firms do not impose limits in theory, but they implement monitoring process; in practice, it is likely that client's preferences and the range of products offered will match so that the client will not have to change his/her preferences multiple times.

[5] The AMF itself formulated this type of warning in its educational guide published in July 2022: "Warning: the criteria for alignment with the Taxonomy are very precise and demanding. As companies are only just beginning to provide information on this subject, we can expect the percentage of alignment to be very low, especially at the beginning". Please, refer to : https://www.amf-france.org/fr/espace-epargnants/actualites-mises-en-garde/vos-preferences-en-matiere-de-developpement-durable-ce-qui-change-pour-vos-placements (*in French only)*

Q15: If available: what percentage of those who adapted decided to (1) lower the level of ambition within an option (i.e. reducing the "minimum proportion" or lowering the threshold of sustainable investments in a portfolio), (2) change between the three options (i.e. categories a, b and c) (3) opt for a combination/ for a different combination between the three options (i.e. categories a, b and c) (4) express no sustainability preferences anymore.

Our members do not have such accurate information or data.
But they have noted that most clients do not know what type of product a) b) or c) they want and in what minimum proportion and therefore ask their advisor to help them for making this choice. This requirement from the clients is complicated to articulate with the one from the regulation requiring not to influence the client.

Q16: How often did clients refrain from adapting their sustainability preferences, accepting that the firm could not recommend any financial instruments or invest on their behalf?

Our members do not have such accurate information or data. This question is premature. The implementation of regulation related to sustainable preferences is too recent for our members to be able to give a precise answer to this question.

Q17: In relation to the update of clients' profiles:

- **Which percentage/average proportion of clients have updated their (MiFID) profiles following the entry into application of the new regime on 2 August 2022?**

  These percentages vary from one company to another and depend on how the company is organised. Within the same group, these percentages may also differ from one subsidiary to another.

- **On average, taking into account the number of clients whose profile has already been updated, what is the proportion of clients who express sustainability preferences in your firm/jurisdiction?**

  Same answer.

- **On average, taking into account the number of clients who express sustainability preferences, what is the proportion of clients that have expressed a specific preference for one or more of the three categories (Taxonomy, SFDR, PAI) in your firm/jurisdiction? (How many clients are only expressing whether or not they have sustainability preferences i.e. yes, no?).**

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Q18: Do you have any comment on the above practical examples?

No.

Q19: Have firms implemented an approach similar to the one described in examples 1 and 2? If yes, which of the two approaches have firms implemented? If firms have implemented a different approach, please provide further details.

Most of our members have implemented an approach similar to the that described in example 2.

Q20: What are the issues that firms encountered in the application of the requirements at portfolio level?

In the context of the provision of an advised service using a portfolio approach, our members would like ESMA to clarify that each financial instrument advised does not necessarily have to correspond to all the PAIs selected by the client.

Indeed, paragraph 88 of ESMA guideline 8 clearly states that: *"When a firm conducts a suitability assessment based on the consideration of the client's portfolio as a whole it could assess suitability as regards the sustainability preferences, for example, by applying those preferences (…) on average at the level of the portfolio as a whole or at the level of the part/percentage of the portfolio the client wants".*(see also paragraph 38 of the ESMA final report of 23 September 2022)

In addition, under an alternative approach (see paragraph 28 of guideline 2), the proportion of sustainable assets in the portfolio can be allocated to the different categories a), b) or c) chosen by the client. Consequently, there should no obligation for all sustainable financial instruments to comply with the PAIs defined by the client, since they may be either a) or b) products. This would otherwise be a cumulative approach.

We would appreciate it if ESMA could clarify this point in its Q&As.

Q21: How are clients' sustainability preferences gathered on the consideration of PAIs? Do firms refer to the PAI indicators listed in Annex I of the SFDR Delegated Regulation exclusively, or may clients express their preferences based on other PAIs? If clients may express their preferences based on other PAIs: what are those PAIs and how were they identified?

Our members only refer to PAI listed in Annex 1 of the SFDR delegated regulation.
Some of them have grouped PAIs into families, as authorized in ESMA guidelines (see guideline 2, paragraph 27). As soon as the client ticks one of a PAI included in a family, any advised financial product from that family is considered to meet his/her preferences.

Q22: May clients determine qualitative elements in order to demonstrate the consideration of PAIs?
How are clients' sustainability preferences gathered on the consideration of PAIs?

- **If so, what are these qualitative elements and how were they identified, how is the information on qualitative elements gathered?**

- **If not, what are the challenges preventing you from offering such possibility to clients? How could these challenges be overcome?**

We would like to point out that for certain PAIs, a qualitative approach does not really make sense (for example, for the criterion of excluding companies that manufacture controversial weapons).

In addition, given the complexity of the subject, customers do not express an opinion on the qualitative elements to be taken into account in PAIs. Customers are not at interested in the question and would be unable to answer if asked.

Q23: What are the issues that firms encountered in the consideration of PAIs from clients?

The concept of PAI is quite difficult to understand for retail clients.
At this stage, our members do not see how they can move from a quantitative to a qualitative approach and explain this new approach in a simple manner to the client.

Q24: Does this correspond to practices adopted by firms? If firms have implemented a different approach, please provide further details.

Yes, some of our members have adopted the alternative approach and where this is the case, it is clearly explained to them, including in the questionnaire on their sustainability preferences.

Q25: How do firms ensure the consistency of the investment advice or portfolio management service provided when conducting suitability assessment with respect to the sustainability preferences expressed by a group of natural persons when no representative has been designated?

In the case of a group of natural persons, all the clients in this group sign a single questionnaire for the joint securities account.

In this case, the sustainability preferences are based on the answers provided in the questionnaire with reference to the single "common profile" (there is no difference with the other criteria of the suitability assessment such as investment objectives, investment horizon, etc. for which a single answer is specified on behalf of the whole group).

Q26: What approach and criteria have firms adopted for the mapping of products' ESG features in view of their matching with clients' sustainability preferences?

Our members use the Findatex EET templates, which provide very precise information on ESG features of the SFDR financial products in particular on their classification in categories a), b) or c) of Article 2(7) of the MIFID 2 delegated regulation.

Q27: How do firms apply sustainability-related concepts of Taxonomy Regulation and SFDR to MiFID II financial instruments that are outside the scope of SFDR (e.g., shares, bonds, certificates, etc.)? How do firms apply the "minimum proportion" concept to such instruments? In particular, how is the "minimum proportion" calculated?

The AMF has recently carried out an in-depth study of this topic.
When providing advice on non-SFDR financial instruments, our members use internal methodologies that have already been exposed to the AMF.

Q28: Are firms making use of ESG rating/scoring systems for products mapping in terms of sustainability? If yes, please provide details.

Yes, some of our members use scoring systems for certain products, based on internal methodologies.

Q29: In case of a positive reply to Q28, how do these interrelate with information gathered from manufacturers (or other sources)?

Our members which have developed their own rating systems use information provided directly by manufacturers for funds, ETFs, alternative funds, private equity and private real estate, via questionnaires sent to them. For corporate issuers, the information comes from ESG data and rating providers.

Q30: How are firms, in their capacity as manufacturers and/or distributors, defining the target market for products with sustainability-related objectives, in terms of granularity? Please specify the elements that are defined for this purpose. Do firms adopt one single approach for all products, irrespective of whether they are in scope of SFDR? In case approaches differ, please explain why and how.

The a), b) and c) features of the financial instruments provided as part of the EET or via the internal asset managers are used to define the target markets, on the understanding that no negative target market has to be defined.

For funds, market analysis and market demand on sustainable requirements are carried out prior to the commercial launch of a new fund. The sustainability objectives of the product are taken into consideration from the inception of the fund and are fully integrated into the product governance process.

The approach to using information collected by manufacturers for SFDR products or through asset managers for non-SFDR products is identical in terms of determining target markets.

Q31: What are the factors that firms, in their capacity as manufacturers and/or distributors, would consider for the periodic product reviews with respect to sustainability-related objectives?

Each firm has its own internal process for taking into account any information relevant to this periodic review of products (for example, controversies or any information expected to have an impact on the sustainability rating of a financial instrument).

Q32: How are firms, in their capacity as distributors, collecting relevant information from manufacturers on sustainability-related objectives of the target market? Is the information received from manufacturers sufficient, or are firms considering other inputs? If so, please explain why and describe such additional inputs.

Firms use data from the Findatex EET and external data providers. This information may be supplemented by data from due diligences or reviews carried out by their asset managers.

Q33: How are firms, in their capacity as manufacturers and/or distributors, treating products that do not consider sustainability factors in their product governance processes, specifically concerning the target market assessment related to the sustainability-related objectives (e.g. are sustainability-objectives considered in the negative target market assessment for such products? If so, please explain how).

For manufacturers and distributors, products that do not take sustainability factors into account in their governance process are considered 'neutral'.

Such products may be recommended to a client who has expressed sustainability preferences, only if the client has adapted his/her preferences (and this adaptation makes it possible to subscribe to these products).

Q34: Have firms noticed increased demand by clients of financial instruments with sustainability features? Please provide any relevant available statistics on this topic (e.g. percentage of clients asking information about these products; trends over time). Furthermore, please explain if factors such as age, gender, level of education or level of income/wealth play a role in the demand for financial instruments with sustainability features.

No, for the time being, firms have not seen an increase in demand for instruments with durability features. Most clients are turning to standardized preferences proposed by the firms because they have no idea what type of sustainable instruments they want to invest in and in what proportion (Remember that according to our members, less than 5% of their retail clients, of those asked about their sustainability preferences, have expressed specific preferences (i.e. have expressed a choice between a), b) products and/or products with PAIs).

However, some of our members have noticed a slight increase in demand from youngest customers.

It would seem that youngest clients have a greater appetite for sustainable products. This, at any rate, is what emerges from the survey carried out by Opinion Way for the AMF, which shows that 32% of under-35s (compared with 25% of all respondents) say they hold responsible investments[6].

However, a recent study by Allianz shows that only 10% of a total sample of residents in 7 major OECD countries consider ESG responsibility as one of the main criteria for long-term financial investment, and there is homogeneity in the responses, regardless of age, as regards relative indifference to ESG[7].

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[6] Please, see page 42 of the survey : https://www.amf-france.org/sites/institutionnel/files/private/2023-07/The%20French%20and%20Responsible%20investments%20-%20OpinionWay%20for%20AMF%20-%20July%202023_0.pdf

[7] See 2023-07-27-Financial-Literacy.pdf (allianz.com) ; the sample comprised a total of 7095 people living in Australia, France, Germany, Italy, Spain, UK and USA corresponding to the characteristics of the total population age 18 and over in these seven countries

Q35: Which percentage of products in firms' offering have sustainability features? Please provide breakdowns and details, where available. Are retail clients satisfied with the availability of products with sustainability features (number, type, characteristics)?

We let our members answer this question directly to ESMA (some of them will respond individually to the Call for evidence).
In addition, the AMF carries out detailed annual monitoring of sustainable products offered by all French investment services providers.

Our members believe that their clients are satisfied with the availability of sustainable products. In any case, they note that they have received few or no remarks or complaints from them on this subject.

Q36: Are firms facing specific issues related to data availability/data quality with respect to financial instruments with sustainability features? If yes, how are firms dealing with these issues?

Firms were faced with the problem of a virtual absence of products a) (taxonomy-compliant products) in August 2022 and to date, the commitment rates for sustainable investments for all products remain low. This inevitably had a disappointing effect on the most enthusiastic clients for green products.

Our members also tell us that:

- EETs are not yet fully filled by manufacturers of products
- investment calculation methodologies are not homogeneous, leading to a comparison between sensitive products and a lack of attractiveness and confidence in this product typology for clients.
- they also face with a certain lack of availability, quality, accuracy, homogeneity of data from manufacturers and with high cost of data; they communicate with product manufacturers and data providers when lacking the data or doubting about its accuracy after quality controls. They also ask asset managers for details on taxonomy, sustainable investments and PAI methodologies, in order to better understand figures in the EET and try to be able to compare all asset managers.