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Feedback Statement

Public Consultation on Institutional Investors' and Asset Managers' Duties regarding Sustainability

I. Introduction

On 13 November 2017 the Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA) of the European Commission launched a Public Consultation on Institutional Investors' and Asset Managers' Duties regarding Sustainability.

The purpose of the consultation was to seek views on how institutional investors and asset managers (could) include environmental, social and governance (ESG) factors when taking decisions. This would help them allocate capital more efficiently by taking into account sustainability risks, rather than merely seeking to maximise short-term financial returns. Respondents were invited to provide concise and operational suggestions on measures that can be enhanced or on complementary actions to deliver the policy goals.

The consultation forms part of the Commission's efforts to mobilise private capital towards green and sustainable investments to enable the transition to a low-carbon economy and shows the European Union's (EU) strong commitment to mitigate risks posed by climate change and environmental challenges. The EU has taken the lead in building a financial system that supports sustainable growth, and sustainable finance continues to be one of the Commission's main priorities. The consultation further underlines the EU's commitment to the Paris Climate Agreement and the UN 2030 Agenda for Sustainable Development. As announced in its 2018 Work Programme, the Commission published an Action Plan on Sustainable Finance on 8 March 2018.

The consultation followed up on two of the eight early recommendations delivered by the High-Level Expert Group on Sustainable Finance (HLEG) in its interim report of July 2017. One 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 ESG factors and long-term sustainability. Another recommendation focused on strengthening "disclosure" on all sustainability dimensions. The final HLEG report was published on 31 January 2018.

The consultation document provided for 37 questions in total including sub-questions. The first section was addressed to all respondents and provided for (i) general overview, (ii) problem, (iii) policy options and (iv) impacts for stakeholders. The second section was specifically addressed to end-investors and the third section to relevant investment entities. The questions focussed on several issues such as *inter alia* the relevance of ESG factors in the investment decision-making process, the consideration and level of integration of sustainability factors, possible constraints and risks/opportunities related to sustainability factors, disclosure of information on sustainability factors and costs/benefits due to the integration of sustainability factors.

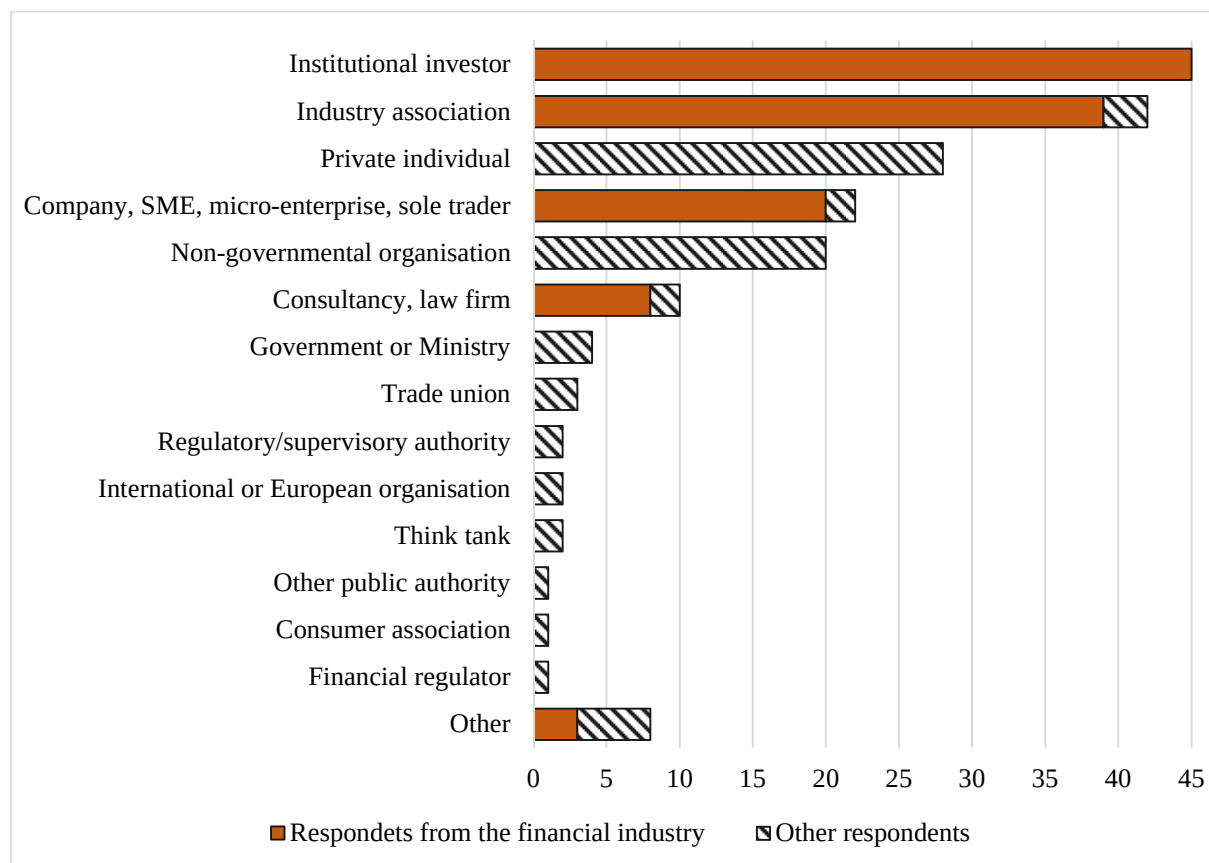
DG FISMA received 191 responses to the consultation that ended on 29 January 2018. Contributions were made by a broad variety of stakeholder groups (see Figure 1). In particular, we looked at the category of respondents from the financial industry, henceforth referred to as the "industry" (see Figure 2 for a more detailed breakdown of respondents from the financial industry). Replies originated in 14 EU Member States, 3 other European countries and 5 non-European countries (see Figure 3 for the breakdown by location).

This feedback statement summarises the answers received for each of the 37 questions (18 questions to all respondents, 3 addressed to end-investors and 16 addressed to relevant investment entities). It does not aim to be exhaustive or provide detailed statistical data, but rather seeks to give a qualitative representation of the contributions received and identify some specific messages related to possible actions to improve the assessment and integration of sustainability factors in the relevant investment entities' decision-making process in order to align the financial system with the overall EU sustainability objectives.

The summary of the responses provides particular insight into new perspectives on existing measures and new areas for action proposed by the respondents.

This feedback statement does not give any indication of potential initiatives, which the European Commission may or may not undertake in the future in this area.

Figure 1 – Replies by type of stakeholder¹



¹ Respondents in the category „other“ include stock exchanges (2 respondents), discussion fora (2), one asset manager, one financial advisor, one advocacy organisation and one accounting association.

Figure 2 – Breakdown of respondents from the financial industry by sector²

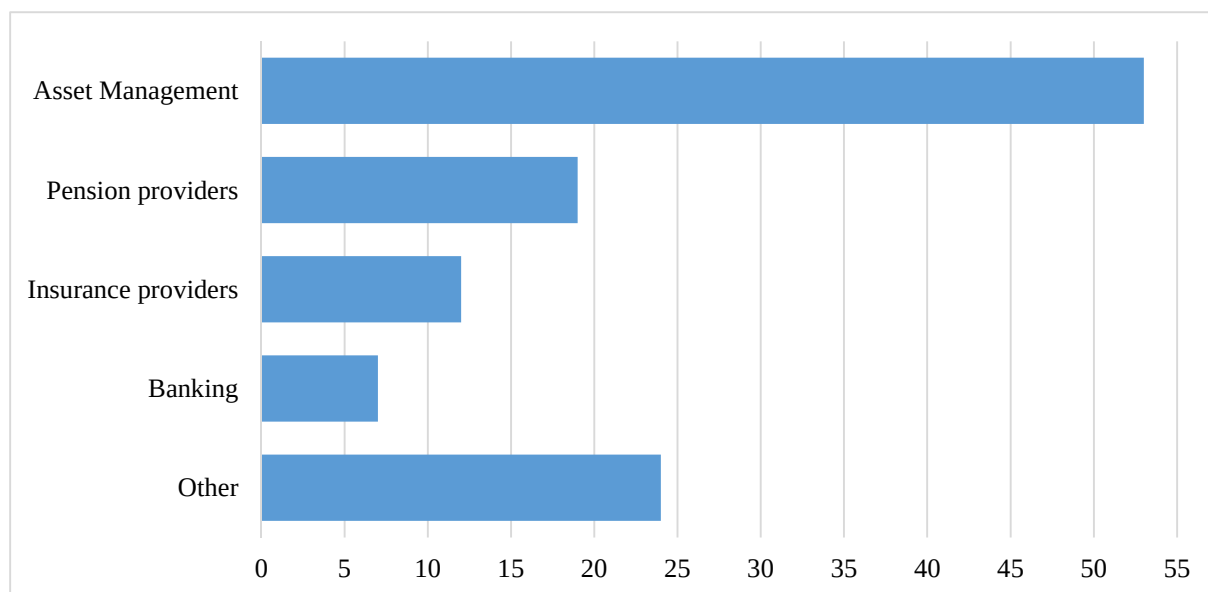
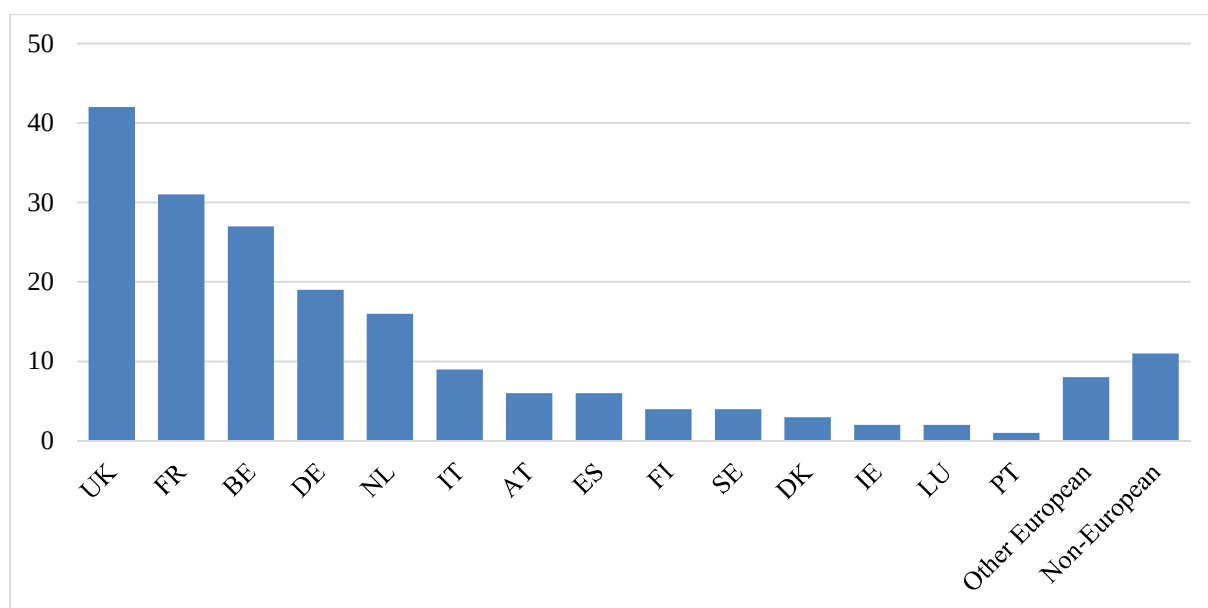


Figure 3 – Replies by country³



² Other respondents from the industry include service providers (9 respondents), investment fora and other industry-related associations (7), consultancies focused on sustainable investment (6) and market infrastructure providers/stock exchanges (2).

³ Other European countries represented are Switzerland (6 respondents), Norway (1) and Liechtenstein (1). Non-European respondents are based in the USA (7 respondents), Australia (1), Canada (1), India (1) and Bermuda (1).

II. Summary of individual responses

2.1 Questions addressed to all respondents

Section 2.1 I: General overview

Question 1) – Do you think relevant investment entities should consider sustainability factors in their investment decision-making?
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The overwhelming majority of respondents across all categories agreed that relevant investment entities should consider sustainability factors in their investment decision-making process.

The vast majority of respondents supported the consideration of sustainability factors in the investment decision-making process of relevant investment entities as these factors can have a material impact on the long-term risk and return profile of investment portfolios. Integrating ESG factors in the investment decision-making process would help institutional investors and asset managers mitigate risks and enhance long-term value creation.

Taking ESG factors into account also contributes to making capital markets more responsible and increases the flow of capital towards a more sustainable economy which is in the interest of the ultimate beneficiaries of institutional investors. There is also an obvious "public good" as consideration of ESG factors is likely to lead to improved sustainability performance by investee companies.

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. There is also an increasing demand for sustainable investments from end-investors.

There is some evidence that ESG performance and stock price are positively correlated in the long term. A report by the University of Oxford and Arabesque Partners analysed over 190 academic studies and sources on sustainability to assess how sustainable corporate practices can affect investment returns. 80% of the studies demonstrate that stock price performance of companies is positively influenced by good sustainability practices.

Another reason for taking ESG factors into account is the EU commitments to align its financial system with the Paris Climate Agreement and the UN 2030 Agenda for Sustainable Development and its Sustainable Development Goals (SDGs).

Several stakeholders called on the European Commission to bring forward legislation which embeds this duty in law and provides clarity for investors on their duties. They recommended that the EU introduces omnibus regulation which requires the integration and disclosure of sustainability factors within the investment decision-making process of European financial institutions, which is then incorporated in relevant financial legislation.

These stakeholders believed that such legislation should have three main aims: i) remove the still widely held misconception that an investor's duty is to "maximise returns" and therefore schemes cannot consider ESG or ethical factors in investment decisions; ii) make clear the expectation that all financially material factors should be considered by schemes, including where these arise from ESG considerations; and iii) make clear that, under certain circumstances, non-financially material considerations may be considered.

A few stakeholders encouraged the Commission to refrain from altering the well-established and understood interpretation of 'fiduciary duty'. Doing so may lead to overestimating ESG risks by investment entities while underestimating more immediate risks that issuers manage every day.

Question 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). Please specify others.

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

A very large majority of respondents supported the consideration of each listed sustainability factor (i.e. climate, other environmental, social and governance).

When asked for the level of importance, there was also a widespread agreement on the high relevance of all mentioned factors – over three-quarters of respondents marked all factors as either important (4) or very important (5). Climate factors in particular stood out, with over three-quarters of respondents considering them very important. The respondents from the industry considered governance factors as the most important, closely followed by climate factors, while other environmental factors and social factors received a slightly lower score.

Stakeholders replying to this question specified several other sustainability-related factors that should be considered by relevant investment entities. These factors include cultural and ethical issues, reputational risks arising from the way a company treats its customers, suppliers and/or employees, supply chain risks, strategy, accounting, regulation, capacity to generate innovation, cybersecurity/cyberwarfare and impacts of artificial intelligence.

A belief was expressed that investors should also consider the sustainability of the financial system as a whole. Another emerging factor to take into account is fiscal transparency, especially in light of the stricter approach to taxation that has been adopted in some jurisdictions. In the case of sovereigns, political factors may also be relevant to consider. If material to the investee companies, investment entities should consider economic factors too such as market presence, procurement practices and anti-competitive behaviour.

Investment decision makers should be left with the discretion to decide on the way and extent to which ESG factors are taken into account in the investment decision-making process. The reason for this is that materiality is a dynamic concept that will need to be considered differently by different investment entities depending on the relevant investment strategy, asset class, market, country and company.

Many respondents considered all factors within the above categories, with some preference for the climate and governance ones. Consideration of climate factors is the most developed because there is a global agreement on what should be done and a constant progress in relevant data disclosure. A strong governance function is also taken into account as it will facilitate the identification and management of other sustainability factors that are relevant for a certain investment.

Beneficiaries' preferences need to be considered too as they will differ from an ethical or otherwise non-financial perspective.

Question 3) – Based on which criteria should the relevant investment entities consider sustainability factors in their investment decision making? Please explain.

Stakeholders deemed materiality and relevance as the key criteria to be considered by relevant investment entities when making investment decisions. In particular financial materiality needs to be taken into account. The relevance of a sustainability factor for the

financial interests of the ultimate beneficiary should be assessed over a time horizon consistent with the beneficiary's interests.

In addition, stakeholders noted that the following should be considered: investment preferences of the beneficiary; strength, stability and sustainability of the economy and financial system as a whole; and alignment with internationally agreed sustainability and development objectives (e.g. the Paris Climate Agreement and the UN Sustainable Development Goals).

Other criteria of relevance include risks of value diminution or stranded assets due to breach of (social or environmental) law, changes or implementation of social and environmental regulations, financial systemic risks, and broader environmental and societal systemic risks.

It is also important to take into account the following: i) the inclusion or not of an investee company in a sustainability index; ii) its ability to manage and mitigate material ESG risks through the strength of management of ESG issues and track record in addressing risk factors; iii) its disclosure of ESG initiatives and data (e.g. publication of an integrated report including non-financial reporting/sustainability report); and iv) its engagement with ethical investors and, more in general, with its stakeholders (e.g. presence of an ESG or a CSR department).

Some stakeholders pointed out that the expertise and judgment of investment managers are essential when considering sustainability factors. Asset managers ought to address ESG factors in their investment activities at least to the extent to which the law and regulatory framework in place require them. It is highly recommendable that investment entities anticipate forthcoming regulatory requirements and trends in order to best service their clients and fulfil their duties.

Other criteria recommended by respondents include long-term value creation, physical impacts, transition risks, reputational risk management, long-term growth prospects, expert opinions (e.g. external analysts), ratings and rankings, legal liabilities, penalties for environmental damages and litigation for social/environmental issues.

**Question 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). Please explain.**

A great majority of respondents believed that all of the mentioned investment entities⁴ should consider sustainability factors in their investment decision-making process. This also applies to respondents from the industry, where more than three-quarters supported implementation of the factors by all mentioned entities. The largest agreement was reached for occupational pension providers. Each relevant sector also supported the idea that entities within its sector should consider ESG factors.

Most respondents to this question stated that all of the mentioned investment entities should consider sustainability factors in their investment decision-making process, advice and stewardship practices. These entities exercise direct or indirect discretion over end-investors' capital and provide this capital to companies and governments whose projects

⁴ Occupational pension providers, personal pension providers, life insurance providers, non-life insurance providers, collective investment funds (UCITS, AIF, EuVECA, EuSEF, ELTIF) and individual portfolio managers

and activities directly impact on the environment, workers, communities and beneficiaries/clients.

Service providers and other actors across the investment chain should also take into account sustainability factors in their investment decision-making process.

Integrating sustainability factors in this process can help mitigate risks, identify opportunities and prevent social and environmental impacts associated with investments. It should be done in a transparent and defensible way, based on materiality and, where relevant, on clients' preferences. Costs and technical feasibility (i.e. availability and reliability of information) should also be factored in when considering sustainability factors. In this respect it should be noted that each investment entity has its own financial objectives, time horizon, liabilities and investor profile; therefore, the manner in which ESG factors should be considered cannot be uniform.

Some stakeholders stressed that there should be a level-playing field with no unfair arbitrage/competition by some entities that have to implement more ESG factors than others.

Several stakeholders highlighted the important role of asset owners who are uniquely positioned to drive sustainable and responsible investment. Insufficient consideration of sustainability factors by these owners sends signals to the market as a whole that ESG factors are not a priority for them, which in turn limits the willingness of investment managers and consultants to consider ESG factors in their advice and products.

The difficulty of assessing the impact of ESG integration was recognised by several respondents. The impact will vary depending on the means dedicated to this integration and the scope of implementation, as well as on market structure, investment practice and policy and regulation.

The size of the investment manager will also play a role. To have the most impact, any duties of considering sustainability factors should be applied consistently, appropriately and proportionately across the investment chain.

As for collective investment funds or individual portfolio managers, they should follow their investment guidelines which may or may not include sustainability factors, as these factors are not necessarily relevant for shorter term investment horizons. However, in any case the policy of the investment entity must be disclosed.

Section 2.1 II: Problem

Question 5) – To your knowledge, what share of investment entities active in the EEA (European Economic Area) currently consider sustainability factors in their investment decisions?
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The majority of respondents believed that less than half of the investment entities currently active in the EEA consider sustainability factors in their investment decisions, with over one-third stating that there are none or a few such companies. The answers from the relevant sectors are, however, more optimistic compared to all respondents, particularly for pension providers and collective investment funds. Across the relevant sectors, about one-third of respondents believed that more than half of investment entities in their sector consider ESG factors.

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

The majority of respondents considered the level of integration of sustainability factors as not very high across different investment entities. On average, a large majority of respondents claimed that there is low or no integration by the mentioned investment entities⁵. Respondents from the industry were only slightly more optimistic about the level of integration. Respondents believed that the level of integration is somewhat higher for occupational pension providers (nearly half of the respondents mentioned a high or medium level of integration) and lower for individual portfolio managers (only a minority saw medium or higher level of integration).

Question 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). Please specify others.

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

Respondents from the industry viewed the issues related to data/research, sustainability methodology and metrics, and lack of expertise as the most serious constraints (more than half of the respondents marked them as important or very important). In contrast, a vast majority of respondents did not view European or national regulation as a barrier to incorporating ESG factors in their investment decisions. More than half of the respondents also did not consider the lack of fiscal incentives and/or eligible entities, as well as excessive costs for the scale of their company as an issue. Other issues, especially the answer to “lack of impact on asset performance”, seemed more controversial, with one group of respondents from the industry considering it (very)/important and another one – as not/slightly important.

When specifying other constraints, many additional challenges were mentioned with several emerging themes: i) challenges on the side of the relevant investment entities; ii) obstacles related to the accounting or disclosure standards on the side of companies; and iii) lack of public debate, regulatory clarity and alignment.

Firstly, some respondents identified many challenges on the side of the relevant investment entities. These include for instance decision-making processes and remuneration based on short-term performance or mistrust over lack of transparency and greenwashing. Some respondents remarked that ESG factors may be seen at odds with performance, as traditional financial models do not work sufficiently with forward-looking scenario analysis. Lack of sustainable indices which could serve as an ESG benchmark might be an additional challenge.

Secondly, some respondents believed that a lack of consistent corporate disclosure regime at the international level leads to a lack of available information for the investors. Some respondents reported that current accounting standards also may be in conflict with the integration of ESG factors.

⁵ Occupational pension providers, personal pension providers, life insurance providers, non-life insurance providers, collective investment funds (UCITS, AIF, EuVECA, EuSEF, ELTIF) and individual portfolio managers

Thirdly, several respondents identified the lack of public debate about the impact of investor behaviour, as well as inadequate or unclear regulatory frameworks (e.g. prudential, accounting, disclosure) as significant challenges to ESG integration. Specifically, several respondents mentioned that their legal duties related to sustainability are unclear and that there is a lack of guidance or enforcement by the regulators concerning this topic. Some respondents also identified a lack of common terminology, which is needed to make ESG factors more tangible for investors. Some respondents claimed that the signals from public authorities towards the industry are sometimes absent, weak or contradictory.

With regard to providing more details on what the constraints/reasons are and how they limit the integration of sustainability factors, most respondents perceived ESG factors as difficult and expensive to track, analyse, compare and report. This goes hand in hand with the main challenges such as a lack of high-quality data, commonly-accepted measurement standards and regulatory clarity over fiduciary duty, as well as of disclosure or demand by end-investors.

At the top of the list of constraints, respondents typically named issues with data/research on the topic⁶. Many respondents declared that costs of ESG research are perceived as high and not compensated by sufficient benefits. Some respondents mentioned that existing sustainable investments do not yet have a long enough history to prove their performance. While recent research suggests that the effect of considering ESG factors on performance in the medium or long term is positive, or at least not negative, many market participants might not be aware of this research and/or more concerned about short-term performance, which often drives compensation. Many companies seem to face challenges or lack incentives to develop ESG expertise⁷. They sometimes purchase services of ESG-oriented companies, although investment teams are reportedly not receptive to their advice.

On the demand side, respondents generally saw a growing interest of end-investors in ESG factors, but many of them still see it as insufficient to develop a bigger product offer. Unclear benefits of ESG investing, unclear terminology and a lack of data/disclosure are all detrimental to the demand for investments considering ESG factors. Some respondents stressed the role of financial advisors in encouraging or discouraging the interest of end-investors. Without convincing and easily available data clearly showing the importance of ESG factors, financial advisors are likely to leave them out of the discussion with their clients.

Question 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). Please specify others. Please explain.

Social factors were rated by the industry as the most difficult to integrate, while governance factors were considered the easiest to implement. Climate factors and other environmental factors were rated as rather challenging (with a slight majority of respondents considering their implementation challenging or very challenging). Respondents from outside the industry viewed ESG factors as somewhat less challenging to consider, especially in the case of climate factors.

⁶ Most commonly mentioned issues were that data are often not comparable, industry specific, high quality, cost effective or decision useful.

⁷ A suggestion was made that investment firms can internalise ESG expertise by drawing the talent focused on ESG factors/sustainability from external organisations and universities. Hence, the lack of this expertise within the industry may as well be a result of the lack of demand for it.

Stakeholders that decided to specify other mentioned various other factors, which they see as challenging to integrate, such as cultural factors, ethics/reputation, cybersecurity/cyberwarfare, impacts of artificial intelligence, biodiversity tipping points or some form of economic/business sustainability (e.g. market presence, procurement practices, and anti-competitive behaviour).

Respondents saw diverse challenges to incorporate these factors in investment decisions. Some challenges relate to taxonomy – for instance, existence of too many methods without a single, commonly accepted framework. Others relate to disclosure of information by companies – such as unclear measurement of financial impact or necessity to work with non-public information to assess potential impacts of factors related to issues such as organisational behaviour. As economic externalities, ESG factors are difficult to measure in financial terms (according to respondents, this applies particularly to social factors). Respondents in particular mentioned issues with data comparability and consistency. Some also stressed the challenge to assess which data is financially material. This applies also to cultural factors, which are typically too intangible.

When explaining the different difficulties of integrating specific sustainability factors by relevant investment entities, respondents mentioned diverse factors. Several common themes emerged: i) ESG factors differ in the number of years investment entities were aware of them; ii) maturity of methods for measuring and evaluating impact of different factors varies; and iii) the willingness to integrate different factors differs as relevant entities deem some of them less relevant for their business outcomes than others (for instance, social vs. governance factors). Furthermore, each element consists of subcategories and the level of integration may depend on whether these are traditionally accepted or emerging only in the last years.

Respondents that answered the qualitative questions often disagreed on the ease of integration of climate factors. A significant part considered it difficult, citing the difficulty of estimating the impact of climate risks and the long horizon over which these risks could materialise. Another relatively large group of respondents believed that the integration is not very difficult anymore due to the enhanced focus of regulators and the public on this topic over the last years and the introduction of carbon trading.

According to most respondents, other environmental factors are quite difficult to integrate in the investment decision-making process. The impact and practice differ greatly by sector, and the particular factors are often hard to grasp quantitatively (e.g. biodiversity, water risks).

According to most respondents, social factors are the most difficult to define and hence to integrate in the investment decision-making process. Some also did not consider these factors as important as other sustainability factors⁸, suggesting that the willingness to integrate them may be lower. Social factors include many themes, which differ greatly in the level of awareness and ease to tie them to business outcomes.

In contrast, governance is generally considered easier to integrate as i) the majority of investors recognises the importance of this factor, ii) data are widely available and more harmonised compared to E and S factors, and iii) the outcome of non-compliance is usually clearer (i.e. prosecution). Within governance, it might be harder to integrate some new features such as cybersecurity, anti-bribery actions and data protection.

⁸ In contrast to these views, two respondents noted that human capital and its effective deployment (reflected in social factors such as employee satisfaction, turnover or training) belong to the largest costs and most important drivers of business outcomes; hence, this area could also receive more attention.

Section 2.1 III: Policy options

Question 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). Please specify others.

A very large majority of respondents (including public authorities and industry) agreed that relevant investment entities should consider sustainability factors within their investment decision-making process in the areas of governance, investment strategy, asset allocation and risk management. Nearly three-quarters of respondents considered these areas as very important or important. When comparing the different areas, most importance was given to the area of investment strategy, followed by risk management, governance and asset allocation. There was a strong support for all areas by all stakeholder groups.

As potential further areas for consideration of sustainability factors some industry stakeholders mentioned the fields of active ownership, manager selection, value creation and benchmarking. Some respondents from the industry also stressed investment stewardship as an important area (within governance) to better take account of sustainability factors.

Investment entities should consider sustainability factors in all phases – not only in the pre-investment stage, but also in the post-investment stage – through monitoring engagement and reporting/disclosure during ownership activities, and through due diligence and disclosure in the exit process. A clear reporting on sustainability factors would help redirect capital flows towards sustainable investments/assets.

Stewardship 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.

Question 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). Please specify others.

Within the area of governance the majority of respondents considered four out of six arrangements as very appropriate/appropriate to enable the integration of sustainability factors: i) sustainability performance as part of remuneration criteria, ii) integration of sustainability factors in the investment decision process, iii) integration of sustainability checks in the control process, and iv) periodic reporting to senior management/board.

When comparing these four arrangements, the highest commitment was towards the integration of sustainability factors in the investment decision process. Almost all respondents considered this arrangement as very appropriate/appropriate with the same strong support also expressed from the industry.

A large of majority of respondents considered the integration of sustainability checks in the control process and the periodic reporting to senior management/board as very appropriate/appropriate and a majority – the sustainability performance as part of remuneration criteria.

However, less than half of the respondents considered the other two mentioned arrangements – specific sustainability investment committee and specific sustainability member of the board – as very appropriate/appropriate. Other arrangements in the area of governance were considered as very appropriate/appropriate only by a minority of

stakeholders. In this context, a few stakeholders mentioned sustainability expertise of the board and ongoing training/development of investment professionals as necessary to build capacity and promote ownership and integration of sustainability factors.

Finally, a few industry participants highlighted that governance arrangements vary with investor types and the legal structures employed in each Member State, as well as that the appropriateness of possible governance instruments depends very much on the investment firm's structure and business strategy.

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

About two-thirds of all respondents across all sectors agreed that insurance and pension providers should consult their beneficiaries on an annual/periodic basis on their preference as regards sustainability factors. This also includes most respondents from the industry. However, the replies from insurance and pension providers are roughly split, as about one half supports this approach and the other half rejects it.

Many stakeholders stressed the issue of transparency. A consultation would improve the dialogue between insurance/pension providers and their beneficiaries on ESG issues, providing on the one hand the investor with an opportunity to explain the investment strategy in place, and on the other hand the beneficiaries with an opportunity to express their ESG preferences. Beneficiaries should be better informed about the investment decisions and portfolios in order to better understand what types of businesses or projects their savings support.

Furthermore, many stakeholders also considered that the suitability assessment should be part of fiduciary duties to understand beneficiaries' preferences regarding sustainability and to be able to implement these preferences in the investment decision-making process.

On the supply side, some respondents explained that this consultation can lead to a prominent role of ESG factors in the investment process and a higher level of expertise on sustainability factors that could be used as an element of differentiation and communicated to beneficiaries. On the demand side, some respondents argued that it would raise the awareness of beneficiaries on sustainability and thus improve the demand for ESG instruments. However, several respondents mentioned that education is key to ensure that beneficiaries understand the impact of sustainability factors on risk and performance. They also argued that inadequate consultation of beneficiaries/retail clients could lead to a misunderstanding of what constitutes "the best interests" of their end-investors.

In this regard, some respondents underlined that such consultation would be challenging and complex, and called for guidance and tools to be produced by regulatory authorities to improve the sustainability knowledge/awareness and facilitate the consultation process. One respondent mentioned that investors/financial advisors often refrain from discussing sustainability topics as this increases the complexity of their advisory work whilst incentives are perceived to be low.

The respondents who did not believe that insurance and pension providers should consult their beneficiaries on an annual/periodic basis on their preferences as regards sustainability factors were of the opinion that the costs of running a fully-fledged consultation process are likely to outweigh the benefits. Furthermore, a few stakeholders mentioned that there is no need to do this as the board of trustees of insurance and pension funds already represents the preferences of the individual investors. In addition, they highlighted the risk that such a consultation would focus on individuals' ethical concerns rather than address

the more complex issues around sustainability. Some of them would however agree with a flexible and voluntary consultation. They also considered that it would be more effective to improve transparency and offer choice to beneficiaries than consult them on their preferences as regards sustainability.

Question 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? Please explain.

Nearly three-quarters of all respondents agreed that within the portfolio's asset allocation relevant investment entities should consider sustainability factors even if this leads to lower returns to beneficiaries/clients in the medium/short term. Respondents from the industry and asset managers also supported this approach, but less so than actors outside the industry. Financial market regulators were also supportive.

The majority of respondents highlighted that despite possible risks of lower returns in the short term this could lead to positive impacts on long-term returns. At the same time, it could also help in identifying critical sustainability issues and risks within the portfolio in the short/medium term. However, a paradigm shift should be made from a model where profits are reviewed over a short-term period to a model where focus is on longer term periods. To that extent, some respondents mentioned that it is important that beneficiaries understand economic benefits and sustainability of positive returns over the longer term. It was also argued that this approach would reduce reputational risks and increase the transparency *vis-a-vis* clients.

Some stakeholders believed that performance should remain the main driver for asset managers to preserve a competitive environment. They still considered that the primary objective of fiduciary duty is to achieve investment returns. In this regard, the inclusion of sustainability factors as part of a portfolio's asset allocation criteria does not always reflect the interests of beneficiaries, depending on the strategy of the funds.

Question 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? Please explain where the possible gaps are, if any.

About three-quarters of all respondents stated that the current set of corporate disclosures on sustainability factors is insufficient. These disclosures therefore do not provide adequate information to investment entities which would allow them to perform sustainability risk assessments of investee companies. Less than one-quarter of respondents agreed that the relevant information is in place and a few stakeholders did not have an opinion.

When explaining possible gaps, there was a clear request by stakeholders for more disclosure of high-quality data by companies in order to perform sustainability risk assessments. The available level of corporate sustainability disclosure does not necessarily match the risk assessment needs of investors. Moreover, there are no common/consistent disclosure standards and aligned metrics on sustainability information which is therefore hardly comparable. Furthermore, there is a strong need for forward-looking data which is currently not provided by companies. In addition, some stakeholders pointed out the discrepant time horizon between the disclosed information and the investors' needs.

According to a minority of respondents, there is already a set of disclosure obligations in place, which should be used in the first instance but also further developed. Finally, public

authorities argued that there is a lack of decision-useful information (i.e. data, metrics and forward-looking analysis) and that this gap needs to be addressed.

Question 14) – Do the overall information or risk metrics available enable the relevant investment entities to adequately perform sustainability risk assessments? Please explain where the possible gaps are, if any.

About two-thirds of all respondents to this question stated that the overall information or risk metrics available are insufficient. They do not enable the relevant investment entities to adequately perform sustainability risk assessments. About less than one-third of respondents agreed that this information is sufficient and a few respondents did not have an opinion. Several replies referred to the answer to the previous question.

When explaining possible gaps, many stakeholders mentioned that risk metrics are available for investor entities, but there is a need for standardisation and a set of acknowledged metrics to perform sustainability risk assessments. Established best practices or a defined number of performance indicators on which the assessment of sustainability risk could be made were also mentioned.

Some stakeholders from organisations/companies mentioned that the social dimensions of sustainability are not given equal consideration within ratings' products.

A minority of stakeholders from organisations/companies noted that a lot of data relevant for sustainability risk assessments is already available today. Existing data on carbon footprinting and climate impact assessments can be used for a risk assessment of a portfolio's sustainability. Reference was also made to a few large companies that provide specific data on sustainability, but their methodologies may vary.

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

A solid majority of all respondents agreed that uniform criteria to perform sustainability risk assessments should be developed at EU level. However, this topic seems to be controversial for organisations and companies, but not for those outside the industry where nearly three-quarters are in favour of uniform criteria at EU level. The industry is roughly split in half and overall not very positive about the policy. A majority in the asset management industry opposed the policy and the pension industry was also moderately against it. Nevertheless, the positive responses highlighted that uniform criteria would increase comparability and lead to better decision making by investors, if they incorporate sector-specific criteria.

When explaining, the majority of stakeholders from organisations/companies agreed that uniform criteria at EU level would provide a helpful base for the evaluation of sustainability risks. This would facilitate more transparent measurement and reporting, as well as enhance comparability in the investment decision-making process. Some stakeholders went even beyond that and preferred uniform criteria at international/global level. Others put forward that this framework should be developed at EU level, but in close cooperation/consultation with the various relevant stakeholders, including from the industry and asset management in particular.

Several stakeholders highlighted that the selected uniform criteria and indicators need to incorporate sector-specific issues. Different areas of risk factors need to be considered in different situations and the diversity of investment strategies should be taken into account.

Respondents from the industry furthermore noted that the policy should be proportionate to size, capacity, type of industry and type of investment entity.

A few respondents noted that risk factors can change and new risk factors can emerge over time, which needs to be taken into account. According to some public authorities or international organisations, uniform criteria at EU level would be useful as investors often act very unevenly.

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

According to some public authorities or international organisations, material exposure by entities to sustainability factors should be analysed and taken into account in the entities' risk management models and procedures. Exposure could be tackled through the established risk-based approach. Sustainability risks could be identified and managed coherently with other material risks to which the investment entity may be exposed. The investment entity has to make sure it possesses adequate skills and expertise in the area. The OECD guidance on due diligence for institutional investors was also mentioned.

Stakeholders noted various actions that should/could be undertaken if material exposures to sustainability factors are identified, which would also depend on the investment beliefs, strategy and resources. These include, among others, i) more in-depth analysis and assessment of sustainability risks, ii) engaging with the respective companies, iii) utilising voting rights to improve internal sustainability considerations, and iv) potentially divesting if sustainability factors are still not sufficiently taken into account by the entity.

Moreover, in practice and by law, asset managers disclose a shareholder/corporate governance policy which often includes when and how they will escalate engagement with investee companies to protect and enhance the value of their clients' investments.

Finally, it was also noted that if the material exposure is negative to the performance of the portfolio, investors should consult with beneficiaries to determine their risk appetite and reach consensus for proceeding with the investment.

Question 17) – Should relevant investment entities disclose how they consider sustainability factors within their investment decision-making? Please explain. 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). Please specify others. If yes, where? Please specify others.

For transparency reasons, the vast majority in all mentioned groups (banks, insurance and pension providers, other institutional investors) agreed on the need to disclose how investment entities consider sustainability factors within their investment decision-making process.

High-level disclosure on how sustainability factors are integrated in the investment decision-making process is key. More disclosure is needed both to identify systemic risks posed by sustainability issues and to ensure that end-investors' preferences have been suitably taken into account throughout the investment chain. Increased transparency can contribute to redirecting flows of capital towards sustainable investment options.

On the areas disclosure should cover, there was a very strong support for disclosure in all mentioned areas, especially with regard to governance and investment strategy.

When specifying others, stakeholders mentioned monitoring and control of investment strategy and sustainability performance, managers' selection, benchmarking and value creation, as well as the behaviour of enterprises in the social field.

With respect to the medium for disclosure, there was an overwhelming support to disclose this information in semi-annual/annual reports, pre-contractual disclosure (e.g. prospectuses) and on an entity's website. Insurance and pension providers supported disclosure only through some means such as semi-annual/annual reports, websites or prospectuses. But they were split about disclosure in newsletters, factsheets, periodic reports or marketing materials.

When specifying others, stakeholders mentioned dedicated sustainability investment reports, as well as any material where clients expect to receive material facts about their investments. One stakeholder mentioned that reporting and disclosure of sustainability information needs to remain proportionate.

Section 2.1 IV: Impacts for stakeholders

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

In their quantitative replies respondents stated that all mentioned stakeholder groups⁹ would incur both costs and benefits. However, for each of these groups the share of respondents indicating that it would incur benefits only was higher than the share of respondents stating that it would incur costs only. Among the stakeholder groups mentioned, respondents indicated that the general public and service providers would be the groups to benefit most from such integration of sustainability factors, followed by retail investors and financial advisors.

When asked to explain, respondents stated that considering sustainability factors is part of the fiduciary duty, as all material factors in the investment decision-making process have to be considered. Integrating sustainability factors in this process has merit as the benefits (e.g. better risk management of a portfolio and better long-term performance) outweigh the costs incurred in the process of obtaining information. In the long run, sustainability data can help deliver better returns.

The integration of sustainability factors has a clear benefit for clients through improved risk management. Costs may be incurred by purchasing relevant sustainability data from service providers. Active ownership activities such as voting are also costly.

In general, most of the respondents stated that all of the stakeholder groups mentioned would incur both benefits and costs. However, respondents expressed the view that costs are more likely to be incurred in the short term (such as costs for data analysis, external vendors and additional investments in human resources) while the benefits are only expected in the long term (e.g. sustainable investments, better informed decision making, reductions in risks and volatility, and potential better returns).

Several respondents mentioned that the integration of sustainability factors should not be approached in terms of costs and/or benefits as these factors are among the many factors

⁹ Stakeholder groups mentioned by this question include 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 and service providers (index providers, research providers, etc.).

that can or should be considered in the course of the investment decision-making process. In this context, no additional costs are incurred and consideration of these factors is part of the regular investment considerations.

Some respondents mentioned that smaller companies would incur relatively high costs in the shorter term, but this disadvantage would even out in the longer term. On the other hand, some respondents mentioned data providers as stakeholders that stand to benefit. A few respondents expressed concerns about the opportunity costs of asset managers' reduced capacity to design a product capable of serving investors' heterogeneous preferences, especially when the duty to integrate sustainability factors is formulated rigidly.

2.2 Questions addressed to end-investors

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

If you don't consider sustainability factors, please explain why and what would change your mind? Please explain the reasons.

Almost all of the respondents stated that they consider sustainability factors when choosing investment products or investment entities.

Of those respondents that do not consider these factors, most explained that they do not consider themselves as end-investors. For example, one respondent noted that the national law does not provide end-investors (beneficiaries) with individual choice of investments, and another mentioned that they will only look at the (financial) return of an investment.

With regard to the reasons for considering sustainability factors, most respondents stated that they do it because it forms part of the considerations of long-term investing. Other respondents mentioned that companies with strong governance and whose products and services enhance social or environmental goals should meaningfully outperform other companies over time. Some respondents stated that they consider sustainability factors because they believe that this contributes to a better world.

Question 1a) – If you consider sustainability factors, indicate the importance of the following sustainability factors for your investment decision (1 is the smallest impact and 5 is the highest impact). Please specify others.

The overwhelming majority of respondents stated that all listed sustainability factors have a high impact. In particular, the climate factors stand out with almost all of the respondents indicating a high or very high importance. When specifying others, respondents mentioned that they consider the risk of controversial activities of investee companies and define exclusion criteria for their investments to address this risk (e.g. tobacco, arms).

The consideration of sustainability factors could also depend on the business model of a specific firm; for example, niche players such as companies focussing on the 'silver economy' could be affected more by a specific factor.

Question 1b) – If you consider sustainability factors, is there sufficient information on the different sustainability factors provided by asset managers and institutional investors to help you take informed investment decisions? Please specify others.

If you indicate that there is insufficient information, what kind of information would allow you to consider sustainability factors when you choose your investment products or investment entity? Please explain and indicate how you would like to receive it.

A majority of those that responded indicated that there is insufficient information on the different sustainability factors provided by asset managers and institutional investors. Respondents stated that in particular low level of information is provided on social and climate factors, while information on governance factors is relatively more available.

Only one respondent chose to specify others, stating that multiple ratings exist, but methodologies differ and those differences are hard to assess for them.

In the case of insufficient information, while some respondents mentioned that information provision is improving, there was a wide agreement that information provision should be enhanced. Respondents mentioned that some market participants provide detailed assessments of their sustainability-related activities to clients and some also produce public reporting of their activities associated with sustainability / ESG issues. However, others provide minimal information so there is an opportunity for additional guidance on appropriate disclosure to achieve better comparability. Respondents were split on whether this information should be provided on a mandatory or on a 'comply or explain' basis. Some respondents mentioned that the provision of information should also be linked to the SDGs.

2.3 Questions specifically addressed to relevant investment entities

Question 1) – As a relevant investment entity do you consider sustainability factors? Please explain why.
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More than half of the relevant investment entities (i.e. asset managers, institutional investors and investment advisors) did not respond to this question. From those that responded, an overwhelming majority stated that they consider sustainability factors.

Among the respondents that do not consider sustainability factors, national regulatory constraints and costs were mentioned as the main reasons.

Question 1a) – In which areas does your entity consider sustainability factors? Please specify others. Please explain.

An overwhelming majority of the relevant investment entities that responded to this question reported that they consider sustainability factors in the areas of governance, investment strategy, risk management and disclosure. A majority of respondents also considers sustainability factors in valuation and asset allocation.

With regard to others, value creation, ownership activities/engagement with companies and proxy voting were mentioned. Concerning explanation, all the factors indicated are kept in mind when looking for a specific investment. Respondents believed that ESG factors can have a material effect on a company's long-term fundamentals, in terms of both opportunity and risk. They therefore integrate relevant ESG factors into their investment decision-making process across all areas that are relevant.

Some respondents stressed that sustainability factors are perceived as a complementary way to know and mitigate a portfolio's risks. As long-term investors they see factors such as corporate culture, good governance, climate change strategy, hard and soft regulatory landscapes, resource availability, and employee and market place attitudes as core to the success of their investments. Setting ESG standards also enables the respondents to meet demand for sustainable products by clients.

Question 1b) – What kind of sustainability factors do you consider? (Please refer to the definitions provided in the Glossary). Please specify others. Please explain.

Almost all the respondents from the relevant investment entities focus on climate factors (i.e. climate mitigation factors and climate resilience factors), other environmental factors, social factors and governance factors.

With regard to others, only one response was received stating that investment entities should also focus on the analysis of controversies that could have short-term impact on ESG factors. Concerning explanations, the vast majority of respondents considers the above-mentioned ESG factors as they all can be financially material, depending on a range of other variables such as sector, country of operation, effectiveness of management systems already in place and investment horizon. Relevant ESG factors are also dynamic, changing as risks, customer expectations and legislation change. Some respondents highlighted that they had implemented a policy excluding companies based on E, S and G issues such as not investing in companies/sectors with a heavy carbon footprint, and that better disclosure is required to perform a more in-depth analysis.

Respondents also reported using external providers (e.g. MSCI) that cover a wide range of very detailed ESG factors (e.g. carbon emissions, pollution and toxic waste, palm oil, human rights, labour rights, child labour, supply chain, corporate governance, etc.).

Question 1c) – In case you have products targeting sustainability factors what time horizon do they target? (Several answers possible). Please explain others.

The vast majority of the respondents to this question has products targeting the medium (4-9 years) and long (>10 years) term.

Most of the respondents are long-term investors. However, when making an investment decision it is necessary to consider the time frames that are appropriate for the particular company being considered.

Question 1d) – In your view, what is the relevant time frame within which risks and opportunities related to sustainability factors typically materialize? Please specify others.

For climate factors (i.e. climate mitigation factors and climate resilience factors) the respondents from the relevant investment entities reported relevance for the medium (4-9 years) and long term (>10 years). For other environmental factors there is more relevance for the medium and short term (up to 3 years). Also social factors are more relevant in the medium and short term. Governance factors, risks and opportunities typically materialise in the short term. Other factors are evenly relevant for short, medium and long term.

Concerning others, respondents explained that there is no such thing as a “typical” period for ESG risks and opportunities to materialise. This will depend entirely on the nature of the risk/opportunity, as well as on the asset, its location and the quality of management of ESG issues. Some ESG “opportunities” have long and some shorter payback periods, although investment committees are unlikely to authorise any initiatives that take longer than, say, 3 years to pay back (and probably typically a shorter payback is required). Conversely, some ESG risks can materialise very quickly (e.g. an instance of bribery or corruption), whereas others can take years to manifest (e.g. environmental contamination).

Question 1e) – Within your governance policy, which measures/arrangements do you have in place? Please specify others.

All respondents from the relevant investment entities have in place integration of sustainability factors in the investment decision-making process. The vast majority also reports periodically to the senior management/board and integrates sustainability checks in the control process. The majority of respondents from the asset management sector has a specific sustainability investments committee, while only a few have specific sustainability members of the board.

When specifying other governance arrangements, a few respondents reported that they have in place the following: i) engagement meetings with companies, which are a vital source of sustainability information; ii) a portfolio ESG monitor; iii) a security ESG dashboard; iv) a climate risk analysis tool; and v) a responsible investment working group at group level.

Question 1f) – In integrating sustainability factors in your investment decisions, which elements do you consider? Please specify others.

In case you use external ratings of issuers, please indicate which ones. In case you use internal sustainability ratings, please explain how you get the relevant data. In case you use sustainability benchmarks, please describe these and explain how you get the relevant data.

In case you perform a due diligence analysis which elements do you consider? Please specify others.

In integrating sustainability factors in investment decisions, almost all the respondents from the relevant investment entities perform a due diligence analysis. The vast majority uses external and internal sustainability ratings. Only a few have sustainability benchmarks.

Concerning others, respondents explained that the area and issues are under-researched. This is important as the majority of investment managers uses sell-side analysis as a key input into their analysis of companies, but private companies are typically not externally rated.

As for external ratings, the vast majority of respondents uses MSCI. Other external rating providers are: Sustainalytics, GES Investment Services, PRI, Beyond Rating, Vigeo Eiris, OEKOM, Factiva and RepRisk (to track controversies), ISS-Ethix (to identify securities that produce controversial weapons), TRUCOST (data on carbon, fossil fuels and green energy), IMUG, Morningstar and Bloomberg.

With respect to internal sustainability ratings all respondents to this question have developed internal proprietary models. There is no standardised approach. Examples are: i) use of best-in-class external data alongside engagement and proxy voting insights as inputs into the proprietary rating; ii) for listed equity, the analysis draws on data communicated voluntarily by the companies as part of their financial disclosure or shareholder dialogue, as well as sector- or company-specific external data; iii) among the set of raw data from providers, they select and weigh those they reckon being the most material and countable, hence bringing them in a ranking system; iv) company meetings; and v) company reports.

As regards the usage of sustainability benchmarks, most of the respondents use external and conventional benchmarks. The most known are from the MSCI provider (e.g. MSCI ESG Leaders Equity indexes and MSCI Global Green Bond). One respondent mentioned external databases such as SASB.

Concerning the performance of a due diligence analysis, almost all of the respondents from the relevant investment entities consider governance arrangements. The vast majority considers also quality and frequency of available information and commitment of the management of the investment target to sustainability factors. The majority of the respondents from the asset management sector considers valuation and sustainability risk-adjusted performance. However, only a minority considers methodologies for the calculation of market and regulatory sustainability risks.

Regarding others, respondents added factors such as analysis on a sector basis in order to identify the key ESG drivers that impact the investee companies in those specific sectors, environmental studies/impacts, policies and procedures, and controversies.

Question 1g) – In your risk assessment how do you measure the impact of sustainability risks on your portfolio? Please specify others. Please explain.

The vast majority of the respondents from the relevant investment entities performs a qualitative fundamental analysis. The majority uses internal quantitative models, instead of third-party quantitative models.

Specifying others, one respondent explained that they base their analysis on the 10 principles of the United Nations Global Compact and in-house sector policies addressing specific ESG requirements for sensitive sectors and products. Another respondent stated that they perform a risk-return analysis of ESG indices versus traditional indices, as well as follow industry reports which conclude in most cases that companies with better ESG scores have a better performance in the long term.

With regard to explanations, respondents that do not assess sustainability in their risk assessment explained that a risk assessment model is not yet in place; therefore, they perform a fundamental analysis as they do not have quantitative models. There are no data on a “sustainability factor” that may lead to higher returns or lower volatilities. Furthermore, respondents that include sustainability in their risk assessment often rely on a third party to conduct analysis at the portfolio level. More sophisticated investors have committees, procedures and methodologies in place to assess sustainability risks.

Question 1h) – Do you disclose information on how you integrate sustainability factors in your investment decision making? Please explain.

If yes, where do you disclose such information? Please specify others.

Almost all respondents from the relevant investment entities disclose information on how they integrate sustainability factors in their investment decision-making process. The only respondent who does not disclose such information explained they do it only internally.

The respondents that disclose this information do so periodically informing both internally (management and staff) and externally (clients and others) on the evolution of the responsible investment process. All respondents disclose the process (i.e. how they integrate sustainability factors in the investment decision making), while only a few disclose publicly all direct holdings and voting. Almost all respondents from the asset management sector disclose such information on their website and in their semi-annual/annual reports. The majority does so also in the marketing materials, public reports, pre-contractual disclosure and factsheets. Newsletters are only used by a minority of respondents. Concerning other ways to disclose this information, respondents mentioned conferences, annual (group) reports or presentations to clients.

Question 1i) – Do you disclose information on the outcome of sustainability assessments? Please explain.

If yes, where do you disclose such information? Please specify others.

The majority of the respondents from the relevant investment entities discloses information on the outcome of sustainability assessments.

The majority of the respondents disclosing the information explained that they do so when it is appropriate in relation to the investment. The respondents who do not disclose such information explained that there is no generally accepted method for describing sustainability outcomes, so they are shared only with the clients.

The vast majority of the respondents from the relevant investment entities discloses such information on their website and in their semi-annual/annual reports. The majority also uses periodic reports and marketing materials for this purpose. Only a minority discloses such information in newsletters and factsheets. When specifying other ways of disclosure, respondents added regular road shows and clients' events.

Question 1j) – Do you take into account sustainability factors in your investment decisions due to related national legal requirements or related soft law provisions?

If yes, please specify the relevant provisions and describe the related costs (financial and non-financial) that you incur as well as the method by which you implement these.

The majority of the respondents from the relevant investment entities takes into account sustainability factors in their investment decisions due to related national legal requirements or related soft law provisions.

When specifying the relevant provisions, ESG soft law (e.g. UN Global Compact, Human Rights) was mentioned by most of the respondents.

French respondents mentioned Article 173 of France's Energy Transition for Green Growth Law¹⁰, which specifically requires large institutional investors to disclose how they factor ESG criteria and carbon-related issues into their investment policies. The 'comply or explain' approach gives freedom to shape the processes and methodologies around their contribution to the low-carbon economy, while enabling them to clarify their responsibilities in terms of climate change. Italian respondents mentioned the stewardship principles and Italian decree n.254/2016 on non-financial reporting (both documents require skilled ad-hoc resources to be fulfilled). A German respondent mentioned the investment associations' soft law "Wohlverhaltensrichtlinien" which has integrated ESG factors as of the beginning of 2017.

Question 1k) – Do you currently incur the following costs and benefits due to the integration of sustainability factors?

Potential benefits: Please specify others.

Ability to attract investors with specific sustainability requirements - please explain and, when possible, quantify in EUR.

Improved financial performance - please explain and, when possible, quantify in EUR.

¹⁰ Law no. 2015-992 of 17 August 2015

Reputational benefits/external communication - please explain and, when possible, quantify in EUR.

Internal communication/recruitment - please explain and, when possible, quantify in EUR.

Others - please explain and, when possible, quantify in EUR.

Potential costs: Please specify others.

Decreased financial performance - please explain and, when possible, quantify in EUR.

Loss of specific financial opportunities - please explain and, when possible, quantify in EUR.

Consultancy costs - please explain and, when possible, quantify in EUR.

Legal counsel costs - please explain and, when possible, quantify in EUR.

Compliance costs - please explain and, when possible, quantify in EUR.

Others - please explain and, when possible, quantify in EUR.

On potential benefits, among the respondents that considered themselves relevant investment entities, a large majority stated that they incur benefits due to the integration of sustainability factors. Among these, reputational benefits or external communication benefits were mentioned most frequently. A large majority also mentioned they experience improved financial performance as a result of integrating sustainability factors in their investment decisions.

When specifying other potential benefits, one respondent mentioned risk reduction and another avoidance of litigation. Some respondents mentioned that at this stage it is very difficult to quantify benefits in monetary terms.

Concerning the ability to attract investors with specific sustainability requirements, respondents mentioned an increased investor awareness of sustainability factors and success of sustainability-related products.

When looking at the potential benefits of improved financial performance, several respondents pointed to academic studies that have shown a link between improved financial performance and sustainability. Some stakeholders stressed the need to look at both performance and impact simultaneously over longer term horizons. A potential problem here is that downside risk exposure is not visible *ex ante*. In this sense, the integration of sustainability factors can help to reduce this risk. On the quantification of improved financial performance, most respondents mentioned that it is not easily quantifiable, but they believe that the integration of ESG factors improves performance over the long term.

When looking at reputational benefits/external communication, no quantifications were provided as respondents stated that this is hard to measure. On the other hand, almost all respondents mentioned positive effects of the integration of sustainability factors, including significant positive communication (e.g. general positive reputational effect and ability to attract the growing investor base requiring sustainable investing).

With regard to internal communication/recruitment, most respondents mentioned that an ESG profile is an important motivator from a human resources perspective, notably for recruitment of a younger cohort attracted by sustainability considerations.

When specifying other types of benefits, one respondent observed that the consideration of sustainability factors helps to improve risk management by assessing investments from different angles and increasing the likelihood of detecting potential risks.

With regard to the area of potential costs, a strong majority of respondents to this question does not experience decreased financial performance as a result of integrating sustainability factors. Respondents mentioned increased costs in integrating these factors, especially in the areas of consultancy and compliance costs. In contrast, legal counsel costs are incurred less often. In addition, when asked if integration of sustainability factors results in the loss of specific financial opportunities (for example, in the area of non-sustainable products or projects), respondents were split.

When specifying other potential costs, respondents mentioned costs for additional data analysis, change in operational processes, human resources, training and external advice.

Concerning a potential of decreased financial performance, several respondents mentioned concerns about the reduction of their investable universe or weaker short-term performance before pricing in externalities. Respondents considered these costs difficult to quantify due to, among other factors, a different impact of sustainability risks and opportunities on an investment based on its asset class, geography or time horizon.

With regard to a loss of specific financial opportunities, most respondents mentioned that they experience some opportunity costs, for instance due to the exclusion of selected assets from their investable universe (e.g. tobacco, some energy companies or investees that disregard governance aspects such as salaries, hygiene, work hours, etc.).

Concerning consultancy costs, many respondents did not specify this expense category further or provide any quantification. Some mentioned possible costs of benchmarks or ESG data analysis, including environmental and social impact assessment, ESG due diligence on investees, and assessment of ESG performance of funds. Others mentioned consultancy costs related to improving their sustainability assessment methodologies or to implementing sustainability criteria in the investment decision-making process for companies that have not previously considered sustainability.

Concerning legal counsel costs, a few respondents mentioned that there will be costs when external legal advice is sought. Examples include costs related to Know Your Customer requirements and active voting practices.

Concerning compliance costs, several respondents stated that costs would be limited, with some mentioning that these costs would be outweighed by benefits, such as enhanced returns in the long term. Several respondents expected additional costs in their control framework and others mentioned costs related to i) defining new investment policies, ii) taking measures to improve ESG performance of investee companies or iii) membership in relevant bodies (such as UNPRI or GRESB).

In terms of other costs, respondents mentioned the costs of human resources, data gathering and analysis, and communication, while also pointing to the net benefits to clients and society as a whole from the integration of sustainability factors into investment decisions. One respondent from the industry mentioned an overall annual cost of EUR 130 000 related to ESG services.

Question 2 – What would be the level of costs associated with the integration of sustainability factors in investment decision making in the different areas? Please tick the relevant box. (Costs as % of the AUM).
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There were relatively few answers to this question, which offered the choice between several ranges. The lowest range available was "lower than 0.5% of AUM". Out of those that responded, all respondents indicated that costs would be below 0.5% of the assets under management (AUM) in the areas of investment policy, valuation and disclosure. In the areas of governance and risk management, only one respondent indicated higher costs

than 0.5% of AUM, estimating them to be in the range of 1 to 3% of AUM or 0.5 to 1% of AUM, respectively. For the overall costs, all but one respondent indicated that the costs would be lower than 0.5% of AUM.

Question 3 – Please explain whether integration of sustainability factors in any of the above mentioned areas would lead to particularly significant (or potentially disproportionate) impacts in terms of costs or benefits incurred by stakeholders.

The overwhelming majority of respondents mentioned that costs would be small or that benefits would outweigh the costs. One investor stated that these factors can lead to new risk management processes being put in place (for example, data controls/certifications/guidelines).

Most respondents mentioned that costs are low. As an illustration, one respondent stated that they spend less than 3% of their overall costs on ESG analysis and data which corresponds to a minuscule percentage of their AUM.

A few respondents mentioned that increased integration of sustainability factors will lead to higher costs, potentially resulting in reduced returns for their customers. These respondents found it difficult to estimate the precise level of this impact. One stakeholder gave the following example: in case costs increase by 0.5% of AUM, this could impact net returns to investors by 5 % if these costs are fully passed on to these investors.

Question 4 – Do you engage with your clients/beneficiaries as regards their sustainability preference?

If so, could you estimate the average costs associated to that engagement in proportion to the assets under management?

There were only a limited number of answers to this question. Out of those that responded, a large majority stated that they engage with their clients/beneficiaries on their sustainability preferences. Among those that engage with their clients/beneficiaries, several respondents did not provide any opinion, while all the remaining respondents estimated their costs below 0.5% of AUM, the lowest range indicated in the answer as possible choice.

Question 5 – What could be the benefits associated with the integration of sustainability factors? Please specify and quantify where possible and relevant.

The majority of respondents mentioned that consideration of sustainability factors as part of an active and integrated approach to investment improves the long-term risk-return profile of investors. Respondents also pointed to benefits in the area of risk management such as avoiding the risk of investing in stranded assets. Other respondents mentioned that sustainability considerations have a positive effect on their reputation and contribute to attracting talented, mainly young employees. When referring to quantification, respondents mentioned that such quantification is difficult and cannot be provided at this point in time.