FI Supervision

Sustainable advice is a challenge for firms

No. 29

28 March 2024

Ref. 23-17298

Contents

Summary 3

The in-depth analysis 5
Applicable provisions 6

How have companies integrated sustainability into their suitability assessments? 7
Barely half of the customers received an updated suitability assessment.... 7

Difficult for the customer to express their preferences 9
Barely one-third of customers have sustainability preferences 9
Terms are difficult to understand 9

Deficient processes to match sustainability preferences with suitable savings product 10
Unclear definitions increase risk of greenwashing 11

Advisor's process affects customers' sustainability preferences 12

What FI will do now 14

Appendix 15
Firms in this in-depth analysis 15

FI Supervision

Finansinspektionen publishes regular supervision reports in a numbered series. The supervision reports describe investigations and other supervision carried out by FI. Through these reports, we present our observations, assessments and expectations in various matters. The reports, which are a part of our communicative supervision, are intended to support firms in their operations.

Finansinspektionen
Box 7821, 103 97 Stockholm
Street address Brunnsgatan 3
Telephone +46 8 408 980 00
finansinspektionen@fi.se
www.fi.se

Summary

Finansinspektionen (FI) has conducted an in-depth analysis of how banks, investment firms and insurance intermediaries have considered customers' sustainability preferences when giving advice about savings. The analysis shows firms have begun to implement the regulations, but there is still work to be done. It also shows that the firms vary considerably in how far they have come in their implementation.

One of the challenges the firms highlight is that sustainability concepts, which contain many technical terms, are difficult to explain and help customers understand. Many of the firms experience that this challenge leads to customers choosing not to state any sustainability preferences. FI views this to be highly problematic since the aim of the regulations is for customers to be able to make well-grounded decisions based on sustainability. Firms need to become better at providing customers with information in an effective manner – in other words, pedagogically and without technical terminology.

Almost all of the firms state that they ask the required questions to understand customers' sustainability preferences. However, a review of their advice templates shows that questions about sustainability preferences that are based on EU definitions are often missing. This raises questions about how the templates are actually used in practice.

The background to this analysis is the new rules set out in a delegated regulation for MiFID II and a delegated regulation for IDD[1] on customers' sustainability preferences during investment advice and portfolio management. The new rules aim to make things easier for customers who want to save sustainably and help customers understand that savings products can have varying degrees of sustainability. The rules will also reduce the risk for greenwashing. One of FI's prioritised areas in 2023 was also to review and promote the prevention of greenwashing[2].

According to the regulations, the firm must establish a process for being able to consider customers' sustainability preferences and then match these preferences with a suitable savings product. We have noted that this process is missing in some

[1] The new regulations were introduced through (EU) 2021/1253 of 21 April 2021 amending Delegated Regulation (EU) 2017/565 (delegated regulation for MiFID II) and (EU) 2021/1257 of 21 April 2021 amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 (the delegated regulations for IDD).
[2] Greenwashing, for example, is when a financial advisor does not provide fair, non-misleading or suitable advice about a product's sustainability features when recommending a sustainable product that matches the customer's sustainability preferences.

cases, and in other cases the process includes completely different sustainability preferences than what is required by the regulations.

Despite the lack of data and other challenges associated with the new regulation, which industry representatives have highlighted in different contexts, the majority of the firms say that they often have products that correspond to the customers' sustainability preferences. We see a potential risk that the firms' processes are designed in such a manner as to lead customer to provide preferences that can be matched to the firms' own products. FI encourages the firms to maintain a neutral and impartial approach which is also highlighted by the European Securities and Markets Authority's (ESMA) guidelines.

Our review shows that there is still work to be done for the firms to meet the requirements set out in the regulations. The delegated regulations' requirements on gathering and considering customers' sustainability preferences are new, but the regulations have been in force for more than a year. The rules are embedded in a central customer protection process – the suitability assessment – which FI considers to underline the importance that has been assigned to the rules. Given this background, FI had expected the firms to have progressed further in their work and thus would like to encourage the firms to continue to prioritize implementation of the rules. We will follow up on the firms' compliance with the rules and promote implementation of necessary improvements. When it comes to this analysis, we expect that firms will read the conclusions and consider them in their continued work. FI also encourages the firms to consider the current guidance from ESMA.

The in-depth analysis

The background to Finansinspektionen's (FI) in-depth analysis is that, as of 2 August 2022, firms must apply new rules requiring the identification and consideration of customers' sustainability preferences in conjunction with the suitability assessment pursuant to Commission Delegated Regulation (EU) 2021/1253 and Commission Delegated Regulation (EU) 2021/1257.[3] The regulations aim to facilitate for consumers who want to invest sustainably by integrating sustainability into the suitability assessment. Firms are obligated to conduct such an assessment as part of their investment advice and portfolio management procedures and ensure that the information obtained is of a good quality while maintaining a high degree of consumer protection. The financial instruments that have been developed to date have varying levels of ambition when it comes to sustainability. The new regulation aims to make it easier for customers to understand the varying degree of sustainability in financial instruments and thus allow customers the right opportunities for making well-grounded investment decisions related to sustainability. The delegated regulations are new regulations and are supplemented by guidelines from ESMA and the European Insurance and Occupational Pensions Authority (EIOPA). The guidelines from EIOPA became applicable in 2022, and ESMA's final guidelines became applicable in 2023.[4] The objective of this in-depth analysis has been to follow up on whether firms are taking into account customers' sustainability preferences during investment advice and portfolio management and, if they are, how they are doing so.

Our analysis includes 22 firms; see the appendix. We based our analysis on the survey responses the firms submitted regarding information about their customers' sustainability preferences in relation to the three categories of financial products: taxonomy-aligned activities, sustainable investments pursuant to the Sustainable Finance Disclosure Regulation (SFDR), and principal adverse impacts.[5] We also requested that the firms submit the template they use when providing advice to provide FI with additional information about their advisory services.

[3] MiFID II (EU) 2021/1253 of 21 April 2021 amending Delegated Regulation (EU) 2017/565 (delegated regulation for MiFID II) and IDD (EU) 2021/1257 of 21 April 2021 amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 (delegated regulation for IDD).
[4] Point 4 of ESMA's Guidelines on certain aspects of the MiFID II suitability requirements (ESMA35-43-3172) and page 3 of EIOPA's Guidance on the integration of sustainability preferences in the suitability assessment under the Insurance Distribution Directive (EIOPA-BOS-22-391).
[5] Article 1 of the delegated regulation for MiFID II and Article 2 of the delegated regulation for IDD:

In addition to applicable provisions and accounts of our observations, which are presented for groups of firms, the report also includes several boxes where we present both good and bad examples of specific occurrences.

Applicable provisions

The delegated regulations specify for investment firms and insurance intermediaries that, for investment advice and portfolio management activities, as an additional step in the suitability assessment, they must also assess whether the financial instrument fulfils a customer's sustainability preferences, if such are available.

The delegated regulations define sustainability preferences as a customer's choice of whether any of the following financial products should be integrated into the customer's investment strategy:

a) A financial instrument or an insurance-based investment product for which the customer or potential customer determines that a minimum proportion shall be invested in **environmentally sustainable investments** according to the definition set out in Article 2(1) of the Taxonomy Regulation.

b) A financial instrument or an insurance-based investment product for which the customer or potential customer determines that a minimum proportion shall be invested in **sustainable investments** according to the definition set out in Article 2(17) of the SFDR.[6]

c) A financial instrument or insurance-based investment product that takes into account **principal adverse impacts for sustainability factors** for which the customer or potential customer determines which qualitative or quantitative features indicate that such are occurring.

[6] Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (SFDR).

How have companies integrated sustainability into their suitability assessments?

FI notes that all firms in the analysis state in their survey responses that they have integrated sustainability into their respective suitability assessments. However, we note that there is broad variation in the extent to which they have integrated the new regulatory framework. Almost all of the firms state that they ask the required questions to understand customers' sustainability preferences. In some cases, the firms do not ask their customers if they want to have environmentally sustainable investments or sustainable investments according to the SFDR. In other cases, they do not ask the customers about the minimum proportion that should be invested in the selected sustainability preference. FI also noted in its review of the advice templates that there was a large discrepancy between what the firms responded in the survey about their questions and the actual questions included in the advice template. This demonstrates that there is a potential risk that the firms' survey responses do not align with their actual actions.

The regulatory framework requires that the companies must collect information from the customer during a suitability assessment in order to determine whether the recommended transaction meets the customer´s sustainability preferences. This is a prerequisite for customers to be able to make conscious decisions regarding sustainability and thus ensure that the consumer has access to savings products that are sustainable.

Barely half of the customers received an updated suitability assessment

The survey responses show that, since the regulatory framework went into effect in August 2022, an average of 43 percent of customers have received an updated suitability assessment that includes sustainability preferences.[7] However, this figure is unevenly distributed between the firms. For example, one firm has updated its suitability assessments for all of its customers, while another firm has only updated the assessments for 4 per cent of its customers. A low updating frequency is not necessarily incorrect. However, according to the delegated regulations for MiFID II and IDD; the suitability assessment should be updated with sustainability preferences no later than at the next regular update of customer information.[8] In reality, this should mean that a higher share of customers at the

[7] This is an average of all firms in the analysis and does not consider how many customers each firm has.
[8] See Recital 4 in the delegated regulation for MiFID II and Recital 10 in the delegated regulation for IDD.

firms in general should have had their suitability assessments updated. An updated suitability assessment is a prerequisite for the firm to be able to take into account their customers' sustainability preferences.

Difficult for the customer to express their preferences

Barely one-third of customers have sustainability preferences

The analysis shows that on average 29 percent of the firms' customers have stated that they have sustainability preferences. [9] This figure is low compared to a survey conducted by FI that shows that 6 out of 10 want to save sustainably.[10] However, FI notes that the distribution between firms in the survey is large (1–100 percent). The analysis shows that the way the advisor discloses and asks about sustainability preferences has a large impact on whether the customers state that they have sustainability preferences. FI thus sees a risk that customers' sustainability preferences are not taken into account in several cases.

Terms are difficult to understand

Most of the firms state that their customers find the new requirements difficult to understand. The firms state in the survey questions that their customers had the most difficulty understanding the meaning of the term *environmentally sustainable investments* according to the taxonomy regulation and *sustainable investments* according to the SFDR. Several firms also state that their customers had difficulty understanding the difference between products that take into account sustainability preferences and products that do not take such preferences into account. FI notes that there is a risk that terms that are difficult to understand make it difficult for the customers to understand sustainability and, ultimately, their possibilities for expressing their sustainability preferences. FI therefore encourages the firms to keep consumers' challenges with sustainability terminology top of mind when designing and providing information about products' sustainability features.

Good practices 1: Simplifications and practical examples

One firm has tried to simplify for the customer by highlighting several principal adverse impacts. The principal adverse impacts that the firm has chosen are those that have better access to data that describes the financial product's impact on sustainability factors. The firm describes what the terms entail in practice by giving

[9] This is an average of all firms in the analysis and does not consider how many customers each firm has.
[10] https://www.fi.se/sv/publicerat/nyheter/2023/hallbarhet-allt-viktigare-for-fondsparare/

concrete examples. The customer then answers whether the investment should take into account these principal adverse impacts for sustainability factors.

In FI's opinion, the simplifications and practical examples make it easier for the customer to express their preferences. According to ESMA's guidelines, the customer should be able to express their preferences without being steered only to the preferences that match the firm's available products.

Example 1: Too detailed and difficult questions

One firm uses 17 detailed questions to determine the manner in which the customer would like to take into account principal adverse impacts for sustainability factors. The questions are multiple choice and have 10 answers each. The questions contain difficult technical terms for which the customer needs to be knowledgeable about sustainability to be able to answer.

In FI's opinion, the technical terms, difficult concepts and many detailed questions make it difficult for the customer to express their sustainability preferences. ESMA´s guidelines state that companies should explain sustainability-related concepts in a clear way without technical language to help customers understand.

Deficient processes to match sustainability preferences with suitable savings product

FI notes that, for a large number of firms, the process of ensuring that the products correspond to the customers' sustainability preferences is poorly described. At some firms we also see that there are no procedures for taking the customers' preferences and matching them with a suitable product. FI therefore sees a potential large risk that these firms' customers will not receive the product that corresponds to their sustainability preferences.

In order for advisors to be able to match customers' sustainability preferences with a suitable product, detailed information about the funds must be available. The pre-purchase information contains both quantitative and qualitative data and is also the only place where there is information describing how a manager defines a sustainable investment or the engagement process. According to the survey responses, the information that the firms use to match a suitable product with customers' preferences differs between companies. EU's standardised template (European ESG template, EET) is the one most firms use. The EET template only uses quantitative information about the funds. It is also voluntary for fund management companies to use the EET template. It is surprising that only a few firms instead use the pre-purchase information. In FI's opinion, it is important that the firms use this information so they can take into account the customer's sustainability preferences.

Good practices 2: Process for grouping funds

One firm says that it has developed a process for grouping funds based on the sustainability preference(s) the funds meet.

In FI's opinion, the firm thus makes it easier for the advisor to match the customer's preferences with suitable products.

Example 2: Does not take into account the customer's sustainability preferences

When a customer says that they have sustainability preferences, one firm asks if the customer has preferences related to environmental, social or governance-related matters. The firm also asks if the customer wants to exclude firms that have an adverse impact on various sustainability areas. The customer then is given a suggestion of suitable products that are the same for all customers, regardless of their specified sustainability preferences.

In FI's opinion, the customers' preferences have no impact on the products recommended to the customer. The customers also are given a false impression that their sustainability preferences have an impact on the advice they are given. The firm thus does not ask the fundamental questions required by the regulations. According to the regulations customers are to be given the opportunity to express their preferences based on the three categories of sustainability preferences. A product recommendation must then be based on the customer's specific sustainability preferences.

Unclear definitions increase risk of greenwashing

The survey shows that many firms are finding that there are challenges associated with how the phrase *sustainable investment according to the SFDR* should be defined. The regulation leaves a lot of room for managers of financial products to define themselves what is considered a sustainable investment, which leads to large variation.[11] The firms' different definitions of a sustainable investment place

[11] In this report, the term *managers* refers to managers of UCITS and special funds.

demands on advisors' level of knowledge and resources in order for them to understand how a sustainable investment differs between products.

The analysis shows that barely half of the firms take into account that managers define a sustainable investment differently. Given the large differences in the assessment of what is a sustainable investment, FI takes the position that it should be important for the firms to define these differences for customers. Customers otherwise risk receiving sustainable investments that do not correspond to their expectations.

Example 3: Does not consider different definitions of sustainable investment

Several firms state that they do not consider the different definitions of sustainable investments because of the current uncertainty about how a sustainable investment should be defined.

FI takes the position that it is important to explain the difference for customers for this very reason. Otherwise, there is a risk that customers will receive a product that does not meet their expectations.

Advisor's process affects customers' sustainability preferences

We see a general relationship between the manner in which an advisor provides information about sustainability, the questions the advisor asks during the session, and the extent to which customers say that they have sustainability preferences. Several firms have said that their customers are more willing to express sustainability preferences if they avoid describing sustainability in technical terms. During our review of the advisory templates, we noted that the firms that describe sustainability in a simple, brief and pedagogical way also reported that a larger share of customers have sustainability preferences. Several firms highlight that it is difficult for customers to independently express their preferences and to a large extent need help with alternative explanations of what kind of practical impact a sustainability preference has.

The majority of the firms state that they often have products corresponding to customers' sustainability preferences. The fact that such a large share of firms has appropriate products is unexpected given the newness of the regulatory framework, the challenges identified in this analysis, and the lack of data noted in the survey responses. Therefore, FI sees in this context a potential risk that the process that many firms have designed to consider customers' sustainability preferences has been designed in such a way that can lead customers to state preferences that can be matched to the firms' own sustainable products. One firm has said that very few (1 per cent) of its customers state preferences that refer to the principal adverse impacts for sustainability factors at the same time as the firm does not have any products at all that are considered to match a customer with such preferences. There is an obvious risk in such a situation of a conflict of interest, where the advisor can influence customers to state preferences that then can be matched to the products the advisor has to offer.

FI expects firms to adopt a neutral and impartial approach during the advisory process so as not to influence customers' answers, which is also evident from ESMA's guidelines.

What FI will do now

Based on the observations from the survey, we note that in general there is room for the firms to develop and improve their procedures and processes when offering investment advice. Given that the regulation is part of the suitability assessment, FI would have expected the firms to have come farther in their work in applying the rules. Therefore, FI encourages the firms to continue to dedicate a special focus to this area and prioritise the application of these rules.

FI sees that there is a risk of greenwashing and improper sales of sustainable products and expects the firms to consider the observations and conclusions in this in-depth analysis. ESMA’s Guidelines on certain aspects of the MiFID II suitability requirements (ESMA35-43-3172) entered into force in October 2023. FI therefore expects the firms to consider these guidelines in future work. FI will continue to advocate that the firms make necessary improvements. In cases where we have identified a need for extensive improvement work, FI will conduct additional follow up with affected firms.

FI will continue to focus on this area in 2024 and will conduct another survey as part of a joint supervision activity within the EU/EEA on ESMA’s initiative.

Appendix

Firms in this in-depth analysis

Firm	CIN
Investment firms	
Alpcot AB	556963-4180
B & P Fund Services Aktiebolag	556605-5298
Coeli Wealth Management AB	559008-1716
East Capital Financial Services AB	556988-2086
Indecap AB	556622-4480
JRS Asset Management AB	556734-9070
Mangold Fondkommission AB	556585-1267
Max Matthiessen Värdepapper AB	556523-8606
Optise AB	556989-9932
Pareto Securities AB	556206-8956
SIP Nordic Fondkommission AB	556708-6649
Svensk Värdepappersservice i Stockholm AB	556324-5447
Säkra Spar AB	556547-9309
Söderberg & Partners Wealth Management AB	556674-7456
Banks	
Nordea Bank Abp, filial i Sverige	516411-1683
Skandinaviska Enskilda Banken AB	502032-9081
Svenska Handelsbanken AB	502007-7862
Swedbank AB	502017-7753
Insurance intermediaries	
Dise & Järås Inväst AB	556660-6876
Olsen Fond & Försäkring	556851-1652
Proxina Pension & Försäkring	556470-1505
S.P. DLRAE Väst AB	559089-3359