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SUSTAINABLE FINANCIAL PRODUCTS

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1 Summary

1.1 Objectives and Methods

This study about sustainable financial products was conducted from May 2021 to January 2022.

The goal of the study is to describe the status quo with sustainable financial products. In this context, the following aspects are analyzed:

- Legal framework, laws
- Factors on the supply side (banks, investment companies, rating agencies)
- Factors on the demand side (consumers)

The methodology in this study is based on **surveys** among experts (at banks, investment companies, rating agencies, other sustainability experts) and analyses from already existing studies (**desktop analysis**). In addition, all **websites** of the financial institutions were examined with respect to the transparency of the sustainability information.

The analysis of the supply side covered banks and investment companies that create and market sustainable investment funds as well as sustainable products involving current accounts, savings accounts, and loans. Sustainable investment funds play the biggest role among these sustainable financial products. In this study, the major factors for sustainability were evaluated, namely credibility (authenticity) and the transparency activities of these financial services companies. To this end, numerous interviews were conducted with experts from different specialty areas (banks, fund management at investment companies, customer advisors at banks, ESG research and rating agencies, asset management firms). Many interviews and surveys were conducted:

- 39 interviews with fund managers, customer advisors, and scientists
- Contacts or information exchanges with 72 contact people at banking institutions, NGOs, and universities
- Evaluation of six questionnaires averaging about 20 questions apiece, which were sent to 17 investment companies and 28 banking institutions
- Anonymized online survey with 42 questions, which were answered by 239 investment advisors
- Mystery shopping at 16 banks
- Analysis of six sustainability rating platforms

On the demand side (ie, from the standpoint of consumers), the main thrust was to evaluate existing studies dealing with consumer expectations of and attitudes toward sustainable financial products. This study contains service information and tips for consumers. A special focus of this work is to illuminate the perspective of consumers.

The point of this study is **not** to provide a detailed evaluation of individual investment funds touted as sustainable (“Is this fund really sustainable?”) or of other sustainability products (eg, sustainable savings deposits). Instead, the object is to cast a **critical look** at the status quo in the implementation of the EU Action Plan on Sustainable Finance. The phenomenon of sustainability labels is also discussed.

1.2 EU Action Plan on Sustainable Finance

In 2018 the European Commission enacted an Action Plan on Sustainable Growth (also sometimes referred to as the Action Plan on Financing Sustainable Growth). The plan follows the 2016 Paris Climate Agreement and the United Nations 2030 Agenda for Sustainable Development. The aim of the European Commission is to create a legal framework that puts environmental, social, and governance (ESG) aspects at the center of the financial system to ensure an economic and societal transition to a climate-friendly future. The objectives are addressed to business enterprises and to all financial market participants (eg, banks, insurers, investment companies, securities firms, asset managers, distributors, etc).

Central legislative proposals in this context:

Taxonomy Regulation

The EU Taxonomy Regulation sets down criteria about when an economic activity is ecologically sustainable. An investment is deemed sustainable if it makes a substantial contribution to achieving one or more of the **six environmental objectives**:

- Climate change mitigation
- Climate change adaptation
- The sustainable use and protection of water and marine resources
- The transition to a circular economy
- Pollution prevention and control
- The protection and restoration of biodiversity and ecosystems

Economic activity must not be allowed to impair any other environmental goal. In addition, international minimum social and labor law standards must be complied with.

Disclosure Regulation

It lays down the disclosure requirements in the financial services sector (Regulation amending Directive (EU) 2016/2341), which address how to include environmental, social and governance (ESG) factors in the investment decisions of financial institutions. Furthermore, institutional investors must provide evidence that their investments correspond to the ESG objectives and disclose how they meet these requirements.

New rules on the provision of advice on investments and insurance

In the future, investment and insurance intermediaries are to be required by law to take ESG factors into consideration in their investment advice.

Sustainability reporting by companies

The main point of the EU sustainability provisions is to increase accountability and disclosure requirements for companies with respect to environmental, social and governance aspects. In the EU, large companies oriented to the capital market as well as credit institutions and insurance companies have been obliged since 2017 to file non-financial reporting based on the **EU Non-Financial Reporting Directive** or **NFRD** for short.

The NFRD has major shortcomings, as evidenced by numerous evaluations of previous reporting practices, the results of the EU Commission's "fitness check" and the impact assessment presented with the proposal for a directive. The main points of criticism pertain to the small group of users, the heterogeneous implementation of the reporting requirements, information gaps, a lack of comparability and reliability as well as the absence of internal and external quality control. Moreover, great degrees of freedom and the "voluntary commitment" principle in the selection of report standards and topics relevant to the reports have led to a definite failure in meeting a key goal, namely making companies genuinely accountable for their sustainability performance.[1]

In its proposal for a **Corporate Sustainability Reporting Directive (CSRD) of April 2021, the EU Commission therefore provides for a major expansion of the current valid reporting obligation in terms of application and scope and for the anchoring of this obligation in corporate governance.** The legislative proposal contains an extension of the area of application and more precisely formulated requirements for sustainability reporting. In addition, there is a plan to apply common European reporting standards, which are to be developed by the European Financial Reporting Advisory Group (EFRAG). It is to be mandatory from 2023 to anchor the new reporting obligations on environmental, social and governance aspects in the situation report. In addition, this proposal for a directive increases the requirements and responsibilities of company management boards and supervisory bodies with respect to sustainable management.

1.3 Results of the Study

1.3.1 Test on the quality of bank advice regarding sustainable investment funds

It is not easy for consumers to find a sustainable investment product. This became clear during the **mystery shopping conducted at 16 banks in Vienna, Lower Austria, and Carinthia as part of this study.** In total, the mystery shoppers visited 18 branch banks to find out how banks proceeded in their consultations with customers about sustainable investment funds. The mystery shoppers were instructed to say they were interested in a sustainable investment and had EUR 10,000 available to invest (all at once in a single payment). Other specifications: Time horizon: 5 to 10 years. Return: 3 % to 5 % a year. Purpose of the investment: apartment/car/saving for retirement). Another stipulation was "**willingness to take a moderate risk**." The results of these test purchases:

- The mystery shoppers were told to say they wanted a sustainable investment and were "willing to take a moderate risk." This preference was often not covered. In many cases the advisors recommended that the mystery shoppers purchase equity funds (50 % of the available products), which exceeded the indicated risk tolerance. So, **customers were classified upward as having a "high risk tolerance"** – often without this being explicitly stated. One in two investment funds being offered was an equity fund with purchase fees averaging 5 % (front-end load).

- Time and again, the advisors recommended that the mystery shopper buy only conventional investment funds without sustainability features. In doing so, the advisors **ignored the mystery shopper's investment specifications**.

[1] Niklas, Wieser (2022): "Corporate Sustainability Reporting – Nachhaltiges Wirtschaften braucht Mitbestimmung," (German only) at https://www.akeuropa.eu/sites/default/files/2022-01/Corporate%20Sustainability%20Reporting_DE_1.pdf

- A total of **42 investment products** were offered during the 18 consultations: 21 equity funds, 13 mixed funds, 4 bond funds, 2 real estate funds and 2 certificates. This means that half of the products offered were equity funds (50 %) and about one third were mixed funds (31 %).

- The sustainable investment funds being offered had **no fee advantages** over the conventional investment funds: The **front-end load/purchase fees** being charged ranged from 4 % to 5.25 % for the equity funds, from 0 % to 5 % for the mixed funds, from 0 % to 3.5 % for the bond funds and 3 % for the real estate funds (purchase fees for the certificates: 1.28 %).

- The **ongoing expenses charged (management fee per year)**, which are charged to the fund assets, diverge substantially: they amounted to between 0.56 % and 2.68 % per year. For bond funds, these fees ranged from 0.56 % to 1.19 % pa; for mixed funds, from 1.08 % to 1.7 % pa. **The management fees were highest for the equity funds: between 0.95 % and 2.68 % pa.**

- Given the high fees for the sustainable investment funds being offered, one can conclude that the **banks do not consider it important to make sustainable funds more attractive to customers**. In fact, between private customers interested in investing a relatively small amount (eg, EUR 10,000) and private customers with a much higher investment volume, the latter is much more likely to be granted a reduction of the front-end load (purchase fees) than “average” private customers.

- It was amazing that the already existing **quality labels** – of special note here are the Austrian Ecolabel for investment funds and the FNG label (featuring a 3-star rating system) from Germany – **played no role at all** in the consultations. The bank advisors did not actively bring up these quality labels nor did they mention the labels as quality features or aids for selecting sustainable investment funds. The planned EU Ecolabel is still stuck in the planning phase. It seems highly unlikely at present that quality labels will play a major role soon, because advisors are obviously unaware of them, and they are – presumably – hardly known to consumers either.

1.3.2 How do the sustainable financial products in Austria measure up?

What does the range of products look like for sustainable financial products? There are sustainable current-account and savings-account deposits, green bonds, and green loans as well as sustainable investment products, such as sustainable investment funds.

- **Sustainable current-account and savings-account deposits are financial products which ensure that the application of funds, the consumers’ deposits, comply with the ecological and social criteria.** This approach ensures that the deposits from savings products are used for granting green loans, for example, in renewable energy or sustainable real estate. It is important that the financial institution manage these deposits in a clearly defined system of accounts so it can verify at any time whether they are used to fund projects that are sustainable.

- Sustainable products involving savings accounts, current accounts and loans are relatively new. That may explain why **only five Austrian banks** (out of the 24 banks surveyed) currently offer sustainable products involving savings accounts or current accounts. The institutions that also have their financial products certified using the Austrian ecolabel known as UZ 49 deserve special mention, as the UZ 49 ensures a minimum level of compliance with the sustainability criteria. The bottom line: **Sustainable financial products involving savings accounts, current accounts and loans are virtually absent from the market.**

- There are only a small handful of banks with highly transparent websites and with information about sustainability activities and sustainable financial products that is comprehensive, understandable, and easy to find.

- **Sustainable investment funds** are among the most important financial products. The investment funds bearing the UZ 49 ecolabel have attained considerable importance. Despite this success story, one should add on a critical note that **sustainable funds do not differ significantly from conventional funds in their selection of securities. This can be explained by the fact that many large, well-known companies (eg, manufacturers of branded products) are also classified as sustainably run companies** – and these companies can be found in sustainability funds as well as conventional funds.

- If there is an insufficient number of companies in which sustainable funds can invest, it is inevitable that the same securities will be found in conventional fund products as in sustainable fund products. Another point of criticism is that several stocks in the major equity indexes have achieved an above-average level of market capitalization and their percentage share gives them decisive sway over the index. **The consequence of this is that fund managers cannot do without these stocks, because these equity indexes are usually given as internal benchmarks for their funds.**[2]

- Alongside sustainable investment funds, there are also **green bonds** [3] **and green loans**. Both product segments are slowly gaining in importance in the product portfolios of banks. Green bonds – they can be issued by governments, companies, or banks – have seen substantial growth in recent years. In August 2021, the Austrian Ministry of Finance announced that the Austrian Federal Government would be issuing its first-ever green bond in 2022.[4]

- **Green loans** are characterized by the fact that their purpose is linked to aspects of environmental protection. The range of products is negligible overall. One can conclude from this that the banks should be encouraged to offer a larger range of green loans attractive to consumers by setting conditions for them that are more favorable (interest, fees) than for conventional loans. In sum, it can be noted that **the financial sector is not yet really geared toward green lending**. Another indication of this fact is that the new FMA minimum standards for lending leave out the subject of green loans altogether.

- There is obviously a wide gap between the banks that have already made considerable progress about sustainable financial products and those that are just starting out. On a bright note, the major banks ERSTE Österreich and UniCredit Bank Austria and the regional banks BKS, Oberbank, Raiffeisenbank Gunskirchen and Steiermärkische Bank and Sparkassen, each of which consistently apply ESG criteria in lending, **have defined minimum criteria for the sustainable products pertaining to loans, savings accounts, and current accounts, and report their sustainable activities transparently on their websites.**

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[2] For example, FANGMAN stocks (Facebook, Amazon, Netflix, Apple, Microsoft, Google, Amazon) and Tesla make up more than 25 % of the S&P500. Their market capitalization is also much higher than the GDP of Japan, Germany, or India.

[3] The EU Commission has proposed a Green Bond Standard: European green bond standard | European Commission (europa.eu), accessed 28 April 2022 https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/european-green-bond-standard_en

[4] Austria intends to issue green bonds in 2022 for the first time (bmf.gv.at), text in German only, accessed on 22 March 2022 https://www.bmf.gv.at/presse/pressemeldungen/2021/August/greenbonds.html

1.3.3 Regarding sustainable investment funds issued by investment companies

Sustainable investment funds are among the main products in the financial services sector. Nonetheless, several problematic aspects were also ascertained for sustainable funds during this study:

- As most of the investment companies draw on the data of the same sustainability rating agencies when designing their sustainable investment fund products, the investment universe of these investment companies is almost identical. **Just two sustainability rating agencies –** namely MSCI ESG and ISS ESG – **cover most of the domestic fund companies.** This, in turn, results in the fact that many sustainable investment funds do not differ substantially in the composition of the equities they include – in other words, there is limited diversity among them. This situation culminates in a cluster risk, which manifests itself in, for example, a massive drop in the price of securities in the sustainability universe (which is often identical with others that are used) leading to an identical or similar drop in prices in many sustainability funds.

- **Regarding rating agencies and data quality**: The quality of the data indicating whether companies successfully implement their sustainability activities will be a decisive issue for financial institutions in the years to come. **The level of data quality for the sustainability funds is not generally expected to rise substantially until the final implementation of the EU Action Plan on Sustainable Finance, ie, the final implementation of the sustainability information requirements set forth in the EU Directive on Corporate Sustainability Reporting.**

- **Research and rating agencies** provide the data on companies or securities and assess the state of sustainability at the examined company. The principle is this: the better the data quality is, the better and more credible will be the design of a sustainable fund. This analysis work is very expensive, which means that **larger companies with greater financial resources tend to be able to set up more fund products and fund products that are more authentic in the sense of credibility**. Experience shows that smaller investment companies and banks have less money available to them for investing in research activities. This, in turn, means that smaller market participants are at a competitive disadvantage. It is therefore worth considering the creation of a data pool that would be equally available to all financial institutions at fair conditions. The advantage of this approach is that all investment companies would have the same conditions in terms of cost and competition when it came to designing their products. This data pool could serve as the basis for offering and marketing a larger number of sustainable, sufficiently diversified financial and investment product.

1.3.4 How should people feel about quality labels for sustainable financial products?

To date, the European Commission has not yet managed to create an EU Ecolabel with strict standards that could serve as a model for the various national labels in the EU Member States or that could have a homogenizing effect. **The planned EU Ecolabel for financial products – according to the majority of bank experts surveyed in this study – will not harmonize the label landscape in the EU.** In fact, one can assume that, at best, the EU Ecolabel will coexist with the respective national labels in the EU. There are **nine different quality labels** in Europe right now.

In Austria, the Austrian Ecolabel leads the way. This ecolabel has existed since 2004, ie, it stands out as a long-recognized standard also in the financial services sector. The FNG quality label is also significant. Ecolabel Directive 49 (UZ49) refers to sustainable financial products. As of February 2022, there were 224 financial products bearing this ecolabel; there are not yet any ecolabel-certified loans.[5]

1.3.5 How do rating agencies and online rating platforms measure up?

This study clearly shows that the **research and rating agencies** tasked by financial institutions arrive at different sustainability ratings on one and the same investment fund. The reason for this is that the sustainability classifications are also based on **different assessment procedures**. In detail, there are, for example, different assumptions made with respect to the tolerance limits for exclusion criteria; one rating agency applies a threshold of at most 10 % of sales for a company with sales in the armaments industry whereas another agency sets the threshold value at a maximum of 5 %.

Consumers can examine ratings at various **online rating platforms (Cleanvest, Mountain-View, Stiftung Warentest, Fondsweb, yourSRI)**. The same can be said of the platforms as of research and rating agencies: each platform has **its own approach and key figures** for assessing sustainable investment funds. For consumers, it is therefore important not to rely on a fund name but instead – whenever possible – to find the given fund on at least two different platforms and to read through the assessments they have of the fund. It is also necessary to determine the different assessment approaches **on their merits** to answer the fundamental question: What factor or factors account for the basic rating differences? When selecting a sustainable investment fund, consumers should therefore draw on at least two rating sources.

1.3.6 How credible (authentic) are the investment companies?

Authenticity is used here in the sense of **the credibility** of an investment company (or bank) with regard to sustainability. As part of this study, the following criteria were examined to assess the authenticity of the product issuers of investment funds, ie, the investment companies:

- Are minimum criteria set for sustainable funds?
- Are voluntary commitments upheld?
- How does the data quality for sustainability measure up and how many data providers are involved?

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[5] Nachhaltige Finanzprodukte unter der Lupe ← Produkte ← Anlegen-mit grünem Gewissen! ← Umweltzeichen.at (Sustainable financial products under the microscope ← Products ← Invest with a green conscience! ← Ecolabel.at), in German only, accessed on 28 April 2022. https://www.umweltzeichen.at/de/produkte/finanzprodukte/nachhaltige-finanzprodukte-unter-der-lupe

- Is there ongoing monitoring of whether the companies contained in the fund abide by the sustainability criteria? Does any kind of organizational responsibility exist, eg, in the form of an ESG committee or an ethical advisory board?
- Are employees given training courses?

The results of this examination were as follows:

- **One in every two domestic fund companies is authentic (credible) with regard to the sustainable investment funds it offers.** Of the 17 investment companies examined, **50 % had high to good authenticity (credibility) standards**. However, there is a vast difference between the top investment companies and those who showed themselves to be engaged in very little or no activities involving the examined characteristics.

- Highly authentic (credible) Investment companies emphasize **internal process controls, a high level of transparency on their websites or a broad range of data sources** for evaluating sustainable companies. These measures give consumers much greater certainty that “greenwashing” is being avoided.

- Authenticity (credibility) can be examined based on internal processes. However, it should be noted in this context that the companies must make this authenticity (credibility) more comprehensible to consumers through **external transparency** (eg, on websites and in annual reports and accountability reports). If this (outward) informational transparency about these internal processes is missing, consumers are justified in having substantial doubt about the company’s authenticity (credibility). **The authenticity of a financial institution can be discerned from the extent and quality of information about sustainability found on its website**.

- Outward transparency raises another set of issues: **No authority or other certifying entity currently exists for verifying this information**. Theoretically, banks and other providers of financial services could assert anything they wanted without having to furnish evidence of the veracity or plausibility of their sustainability reports. One phenomenon observable today is that high-end private banks in particular provide only a minimum of information on their website. This warrants criticism even though customer advisors at private banks presumably provide their wealthy clients with more extensive advice about sustainability aspects of an investment.

1.3.7 Regarding the legal framework of sustainable financial products

1.3.7.1 The EU Action Plan on Sustainable Finance

This action plan, **released by the EU Commission on 8 March 2019**, is aimed at reorienting capital flows toward more sustainable investments in order to achieve sustainable and integrative growth in Europe. Another aim is to manage financial risks stemming from climate change, resource depletion, environmental degradation and social issues. Transparency is an important vehicle for fostering sustainability. This study uncovered the following inaccuracies in the action plan:

- **The statutory sustainability requirements currently stipulated by the EU are still too vaguely defined and imprecise, which could enable greenwashing to take place (Disclosure Regulation, Taxonomy Regulation).**

- One big initial step toward sustainability occurs when the financial institution presents itself authentically (credibly) and also transparently depicts its sustainable activities on its website. **However, this study has clearly shown that many financial institutions (eg, banks, investment companies, asset managers, etc) have a lot of catching up to do when it comes to authenticity and transparency**.
- **“Quarter-by-quarter thinking” takes and will continue to take primacy over all else, especially in the financial sector, at least for now.** That means that fund managers gear themselves toward what the quarterly performance of business activities is (eg, fund management, etc). So, return is presumably given preference over sustainability in this context, too.
- The fund manager survey during this study yielded an assessment that the EU Action Plan on Sustainable Finance would be deemed a success if it also brought about a “quick win” for the financial sector as well. As mentioned above, this quick win is primarily measurable at quarterly intervals. So, it turns out that a major problem is that quarter-by-quarter thinking (still) prevails at financial institutions but also at major companies.

1.3.7.2 Regarding problematic aspects of the Disclosure Regulation

Regulation (EU) 2019/2088 of the European Parliament and the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector governs the **disclosure requirements of financial services companies as regards the consideration they give to sustainability issues** in their strategies, processes and products. Two central points are product classification according to article 8 (product promotes social and/or environmental objectives) and article 9 (product pursues a clear sustainability objective).

This categorization is done independently by the market participants themselves, which has turned out to be a problem. It has led to different classifications because there are no clear definitions of what is to be deemed sustainable in the meaning of article 8 or article 9.

As an initial step, the financial institutions themselves determine in an unsupervised procedure which funds are to be deemed sustainable in the meaning of the Disclosure Regulation.

There are currently no minimum standards about what should be deemed sustainable in the meaning of the Disclosure Regulation. That is because **the** EU Commission does not **currently** require any minimum standards either. For this reason, it can happen that financial products are classified in article 8 or article 9 in which, for example, only 1 % of the fund volume is considered sustainable according to the taxonomy. If an investment fund is declared sustainable, ecological or social although the fund managers invest only an infinitesimally small amount in sustainable companies, the fund would be violating the law against unfair competition rather than this Disclosure Regulation. [6] The status quo in Austria is that the Austrian Financial Market Authority (FMA) plays, at best, an observer role with respect to the Taxonomy Regulation and the Disclosure Regulation. Unlike Germany[7], Austria has no threshold values specifying the point above which an investment fund is to be classified light green (article 8) or dark green (article 9 of the Disclosure Regulation).

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[6] (Dolezal, Wie nachhaltig sind grüne Finanzprodukte, 2021) (how sustainable are green financial products), German only

[7] BaFin - Aktuelles - Übersicht über nachhaltigkeitsbezogene Offenlegungspflichten für … (BaFin Federal Financial Supervisory Authority -- Current -- Overview of Sustainability-Related Disclosures (link does not work) https://www.bafin.de/SharedDocs/Downloads/DE/Anlage/dl_Uebersicht_Offenlegungspflichten_BJ2102_Sustainable_Finance.html;jsessionid=9FD0759956B4A3320C4C019D399B1D9F.1_cid503?nn=9021442

The financial institutions examined during this study did not stand out in terms of transparency. This was exhibited by the fact that top quality information about the company's own sustainability measures were in short supply on the websites of the financial institutions. In a positive example of reporting, Erste Bank KAG (an investment company) provided information on its website about the investment funds categorized as light green and dark green (under articles 8 and 9 of the Disclosure Regulation). In general, it can be assumed that the financial institutions engage in cherry picking. They put good news on their homepage while not even mentioning bad news, ie, news indicating a lack of sustainability thinking within their organization. To be specific, just five of the 17 banks[8] had good menu navigation to the Disclosure Regulation and enable customers to search for the sustainability funds falling under article 8 or article 9.

1.3.7.3 Regarding shortcomings in the Taxonomy Regulation

The EU Commission's Taxonomy Regulation created a sustainability classification system that determines whether an economic activity is climate friendly. To this end, the regulation legally defines six environmental objectives, which are ultimately designed to serve as the basic principles to apply to investments in projects and economic activities. Beyond that, companies and financial market participants have statutory disclosure requirements. **Two environmental objectives, namely climate change mitigation and climate change adaptation, went into effect on 1 January 2022.**

The Taxonomy Regulation is an important step toward establishing sustainability in business life and in the financial sector. But it does have several shortcomings:

- **Companies must report on their sustainability agendas. That is because** fund managers who decide on the composition of a fund also must solicit company data for international funds to comply with legal disclosure requirements (eg, the Disclosure Regulation, etc). **However, the data quality required to meet the taxonomy requirements in the sustainable investment funds depends heavily on companies outside the EU and less on the EU market participants themselves.** About 70 % of the companies on the MSCI World index are from the United States[9]; only about 20 % of the securities are based out of the EU. Whether the data quality required in the EU Action Plan on Sustainable Finance can be achieved will be up to the goodwill of companies headquartered outside the EU. One major problem is therefore that the data quality in sustainability reporting is not guaranteed.

- **Criteria in the Taxonomy Regulation are (still) not sufficiently fined tuned. Delegated acts** that more specifically define the technical screening criteria for sustainability objectives **are required** to provide a more precise definition for the basis established in the Taxonomy Regulation. The German federal ministries responsible for climate change mitigation and the environment determined that an initial delegated act covered the economic activities of about 40 % of the listed companies in sectors that account for nearly 80 % of the direct greenhouse gas emissions in Europe.[10]

[8] Allianz Invest KAG, Ampega Investment, Amundi Austria, ERSTE Asset Management and Kepler Fonds KAG.

[9] (Finanztipp, 2021)

[10] BMWK - Habeck und Lemke reaffirm criticism of taxonomy rules on nuclear energy (bmwi.de): Accessed on 29 April 2022, press release dated 22 January 2022. https://www.bmwk.de/Redaktion/EN/Pressemitteilungen/2022/20220122-habeck-and-lemke-reaffirm-criticism-of-taxonomy-rules-on-nuclear-energy.html

- There are very **questionable criteria for energy sources that were determined to be sustainable**. The second delegated act addressed the inclusion of nuclear power and natural gas as sustainable energy sources in the taxonomy system. The Federal Republic of Germany expressed its disapproval together with the Republic of Austria.

- **There are no criteria for social taxonomy.** Until now, there are just the six defined environmental objectives; a social taxonomy that fully articulates the social standards (eg, human rights, rights of workers, etc) has not yet been established. This shortcoming detracts from legal certainty, especially for banks and investment companies that design sustainable financial products.

1.3.8 Findings regarding greenwashing

Greenwashing is the process of providing misleading information on the ecological benefits of a product, a service, or an organization **to present a company as more environmentally friendly than it is**.

The following criteria can be applied to determine whether greenwashing is occurring:

- **Impact**: Do sustainable financial products achieve an **impact** that makes the world better ecologically or socially? What influence does the financial industry have on climate change and a “green” future?[11]
- **Quality**: How is **quality** defined with respect to a sustainable financial product or when is a product sustainable?
- **Process**: Which **process** (including associated control mechanisms) was set up at the financial institution to create a sustainable financial product?
- **Transparency**: How **transparent** is the financial institution in its external communication when describing the activities, it conducts in connection with the financial products?

Essential **findings** on greenwashing from this study:

- Financial products can be assumed to be greenwashed if, for example, the impact of a fund is extensively promoted **but the reports that are supposed to prove that impact are not published on the website**. A financial institution can be assumed to be engaging in greenwashing if it offers green finance but does not explain on its website which projects it is financing or which ones it is excluding.

Regarding greenwashing in the case of investment funds: Sustainability funds contain large international corporations that consumers do not directly associate with sustainability (eg, Microsoft, Amazon, Apple). This can be explained from the standpoint of the fund management as follows: its objective is to ensure liquidity by integrating highly liquid securities in the fund and to achieve specified performance benchmarks. These companies do meet the sustainability criteria; otherwise, they would not be listed in the sustainability investment universe for the fund management. However, consumers have difficulty understanding why these companies are listed as sustainable funds. The bottom line: Greater transparency is needed as to why the listed companies are classified as sustainable.

- As the mystery shopping survey in this study revealed, **investment advisors at banks exhibit major shortcomings and knowledge deficits** during their consultations with customers.

[11] Prof. Dr. Johannes Jäger delves into this issue in the 2020 Vienna Chamber of Labor Study (AK-Wien Studie) (Jäger, 2020)

- The scope ranges from consumer expectations that funds invest exclusively in green companies to the self-promotion by banks that suggest that a bank is green or sustainable on the whole. In each case, consumers should be given objective explanations and information on what sustainable financial products **can** deliver. **Sound, high-quality advice** is therefore also vitally important.
- **Better training of bank-affiliated and other investment advisors** would lead to more realistic expectations on the part of consumers.
- The **great latitude for interpretation and action under law** (Taxonomy Regulation, Disclosure Regulation) in connection with the designing of sustainable financial products gives rise in many cases to a suspicion of **greenwashing**. For this reason, the legal framework should be expanded to include ESG rating criteria that are as concrete and strict as possible.
- In actual practice, greenwashing is not easy to prove, as the DWS affair proved. A whistle blower had publicly accused this German financial institution of greenwashing. However, the investigations of the German and US authorities came to nothing.
- The most effective measure against greenwashing is to analyze in detail all corporate securities in a sustainability fund and to rate them **on the basis of strict exclusion criteria** to nip greenwashing in the bud. That is difficult in actual practice because this analysis work is a cost issue. In addition, overly strict exclusion criteria would end up excluding most companies and substantially reduce the investment universe.
- One alternative would be to create generally recognized **blacklists of companies** or lists of companies that are not put into an "investment bucket." For example, the Norwegian pension fund makes use of blacklists.
- An effective instrument in practice is to apply **minimum criteria to all set-up funds** of an **investment company** and in this way, apply sustainability to the entire fund product portfolio. This principle can also be applied to **banks**, namely ESG minimum criteria could be applied to **all** loan, current-account, and savings-account products of the bank.
- This study showed once again that a successful, authentic sustainability strategy begins at the management level in banks, insurance companies, investment companies, pension funds, etc If the **company's top management is committed to sustainability**, this attitude radiates to all levels of a financial institution.

1.3.9 What expectations do consumers have?

When is a financial product sustainable in the eyes of consumers?

- Sustainability aspects can be explained with the three letters E, S, G (Environmental, Social, Governance). The investment advisors at banks who were surveyed as part of this study indicated that **consumers interested in sustainable investments ask most about topics related to the environment or climate change mitigation**. Only one in ten consumers asks about the social component (human rights, provisions regarding labor law, etc) at the start of a consultation. Governance goes almost totally "undetected" by consumers (corruption, tax evasion, etc).[12] This matches findings from another study, which reported that consumers are interested first in environmental aspects, then in social criteria and only then, in governance factors. [13]
- Many consumers have a certain expectation of the companies being invested in. Consumers expect to have truly "green" companies in their portfolio. **They also believe that sustainable funds invest solely in these green companies.** As most consumers have no connection to major listed companies, they have images of model companies in their heads (for instance, listed companies such as Verbund or Andritz, or also companies from their immediate area with which they have built up a relationship, such as Druckerei Gugler, Waldviertler Werkstätten, Sonnentor, etc).
- **In most cases, consumer expectations about the companies in which sustainable funds should invest is the exact opposite of what sustainable funds offer.**
- When asked to make a choice, **most consumers always opt for return and risk but only a small number for sustainability**.[14] This raises the question of whether any change would occur if sustainable investment products were more transparent, understandable, and verifiably sustainable. **Return is more important than sustainability as a decision-making criterion in the selection of financial products.**
- In summary, different studies show that **consumers** may be interested in sustainable financial products but when it comes to purchasing investment funds, they apparently follow the motto: **performance before sustainability.** This makes a feedback effect on the product supplier (ie, the investment companies) plausible, ie, the fund managers will also continue in future to gear their thinking toward the performance of funds rather than toward the creation of sustainable investment products. This leads to a conclusion: **Sustainable investment funds must show a return equal to that of conventional funds** – otherwise sustainable investment funds run the risk of not even appearing in greater numbers in the product range and – if they have a lower return than the benchmark – they even run the risk of not being selected or purchased at all.

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[12] Survey among bank advisors as part of the Vienna Chamber of Labor Study (AK Wien Studie)

[13] (Altersvorsorge, Wie halten es die Anleger mit der Nachhaltigkeit?, 2020), 36

[14] (BaFIn, 2019), 25–30