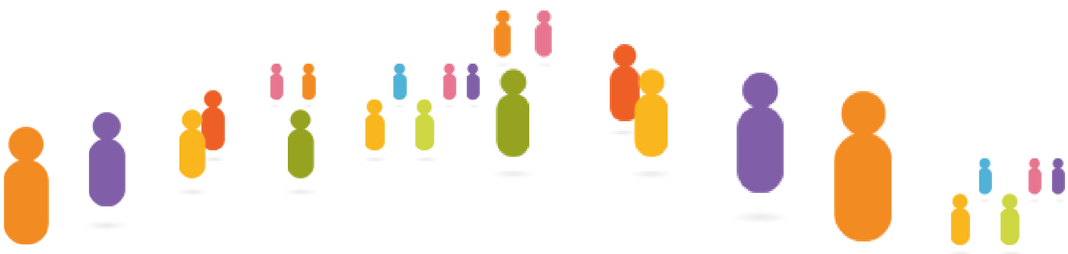
The Consumer Voice in Europe

A CONSUMER AGENDA FOR SUSTAINABLE RETAIL FINANCE & BANKING

Consumer priorities for the 2024-29 period



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Why it matters to consumers

An increasing number of consumers want to contribute to a more sustainable economy through the way they invest their savings or through purchasing more energy-efficient heating systems or cars or retro-fitting their homes. To do so, they need investment options that are genuinely sustainable and affordable financing for home or other big-ticket purchases. In recent years, laws have been put in place to facilitate this, especially in the sustainable investment area, but consumers are still too often effectively prevented from making the choices that conform to their values and preferences because of ineffective rules. The legislative cycle 2024-29 should be the time when the EU finishes what it started in 2019-24, by fortifying existing rules and closing regulatory gaps for sustainable investment and 'green' banking services for consumers.

Summary

Policy-makers often shy away from taking the necessary decisions and put too much responsibility for effecting the sustainable transition on consumers. Consumers stand ready to contribute to the transition, but they cannot do it alone because their financial decisions only have a limited impact on company behaviour. This paper elaborates on the conditions that need to be put in place to allow consumers to contribute effectively.

Sustainable investment services
Many consumers wish to invest their savings sustainably, and the EU has been trying to facilitate that, especially through the Sustainable Finance Disclosures Regulation, which improves the transparency around investment products that are sold as sustainable. However, despite these efforts, it is still exceedingly difficult for consumers to identify investment products that are suitable and truly sustainable and there is still too much scope for greenwashing. More regulatory action and, above all, a new approach to the regulation of sustainable investment products is necessary. Product transparency is still important, but insufficient, and needs to be supplemented by binding standards for sustainable products that take consumers' fundamental motives for investing sustainable as their point of departure.

- More or better transparency will not solve retail investors' problems. The EU should introduce a genuine product standard for sustainable investment products, complete with unambiguous and operational definitions, minimum requirements, intuitive product categories and labels.
- Three mutually exclusive investment product categories and labels should be established on the basis of investment strategies, similar to proposals from the Dutch Financial Markets Authority and the UK Financial Conduct Authority.
    - Products that do not fulfil the criteria of any of those three categories must not be sold as green or sustainable and carry a warning that they are likely to contain harmful exposures. However, they should also be subject to minimum disclosures about their negative sustainability impacts.
- If a (colour-coded) graded label for investment products is introduced instead of the three categories proposed above, it must be greenwashing-proof by clarifying and tightening the SFDR definition of sustainable investments and reduce discretion for asset managers.

- The share of a portfolio that does not contribute to the sustainable investment goal must still be subject to the 'do-no-significant-harm' principle, e.g. through exclusion lists.
- The minimum share of sustainable investments should increase over time to reflect the growth of available sustainable investment opportunities.

- Financial supervisors should require advisers to have sufficient sustainability competences and verify that they inform prospective clients correctly about the sustainability features of offered products. Prospective advisers should also have to undergo professional training.
- Financial advice must be independent and work for consumers, not the advisers. Therefore, a ban on sales commission must be introduced.

'Green' retail banking and financing tools
Apart from being retail investors, sustainability-conscious consumers may also want to contribute to a more sustainable world through the way they live and spend their money. However, large expenditure items like the purchase of an energy-efficient home, retrofitting an existing home or buying an electric vehicle often require specific financing tools like 'green' loans and mortgages. Such tools need to become widely available and affordable, while certain newer lending products, such as equity release schemes, need to be regulated. Consumers who are still unable to pay for green loans or mortgages need adequate public support.

- When the Mortgage Credit Directive comes up for review, it should be amended to require Member States to oblige mortgage lenders to offer green mortgages at a lower total cost of credit than conventional mortgages.
- A definition of green mortgages should be introduced that is consistent with the EU energy and climate goals and excludes items that are not aligned with the EU climate goals, such as gas boilers or renovation projects that do not lead to heat pump-readiness. A definition of green loans should also be inserted into the Consumer Credit Directive. The definitions of green loans and green mortgages should be finetuned so that green lending contributes to lower overall energy consumption (energy sufficiency).
- When transposing the Consumer Credit Directive, Member States should introduce lower cost caps for green loans than conventional loans.
- Lower-interest rate green lending should be made attractive for commercial banks through cheaper refinancing through central banks and/or through public guarantees for green loans and mortgages.
- Public financing or incentive schemes should be available for lower-income households, especially those who live in the least energy-efficient buildings.
- Banks should be required to train staff to sufficient levels and in sufficient number, to provide advice about green loans and mortgages.
- Energy consumption, including expected energy savings from energy retrofitting, should be factored into creditworthiness assessments.
- When transposing the Consumer Credit Directive, Member States should include long-term rental agreements for things like electric cars and renewable energy equipment in the scope of the Directive.
- The revision of the Mortgage Credit Directive should bring equity release schemes and similar products under its scope and protect consumers through cost regulations or product intervention powers for supervisory authorities.

Supervision and enforcement of sustainable retail financial services
The best laws for green loans and sustainable investment products are only as good as their practical implementation, and that requires vigorous monitoring and enforcement that is consistent across the EU.

- The European Supervisory Authorities should use supervisory convergence tools, especially the powers to coordinate mystery shopping and peer reviews, systematically to improve supervisory consistency and enforce minimum standards for business conduct across the EU.
- National supervisors should be given more far-reaching powers and collaborate systematically with consumer protection agencies and consumer associations.
- To make the ESAs more independent from national supervisors, they need a new governance framework with strong powers for independent executive boards and adequate financing.

Other important elements of the regulatory framework to improve sustainable financial services

Sustainable retail finance only works well if embedded into a wider system of sustainable finance. This system comprises aspects and regulations that are not directly related to consumers, but support, or are, indeed, indispensable for, sustainable retail financial services. This paper concludes with an overview of these non-consumer aspects of the sustainable finance system.

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This paper identifies the consumer priorities in the field of sustainable financial services for the next European legislative cycle that will start with the European Parliament elections in June 2024. A lot happened in the 2019-24 cycle. The Sustainable Finance Disclosures Regulation (SFDR), the EU Taxonomy Regulation (also known as the 'Regulation on the establishment of a framework to facilitate sustainable investment'), the Carbon Benchmarks Regulation and the EU Green Bond Standard have been passed into law and a regulation for ESG rating providers has been adopted. Sustainability concerns have been integrated into prudential rules for banks and insurers, and several Regulations or Directives that either encourage sustainable business conduct or require transparency about it have also been passed into law or are far advanced in the legislative process. This includes the Corporate Sustainability Reporting Directive, the Corporate Sustainability Due Diligence Directive and the Regulation on the European Single Access Point for information related to financial services, capital markets and sustainability.

Before this regulatory push, sustainable finance was a largely un- or self-regulated niche industry that catered to growing consumer demand for financial products for investing and saving without trashing the planet or harming its people. These days are over, but despite these improvements, sustainability-conscious consumers still cannot be confident that their money does not support unsustainable business activities and still struggle to find their way through the dense forest of confusing product descriptions, sustainable-sounding product names and marketing promises of questionable sincerity. Even crystal-clear communication about a sustainable financial product can hide much less sustainable product *content* because of weaknesses in the legal framework itself. Much remains to be done to make sure that sustainable finance works for consumers. The next legislative cycle offers the chance to complete the work on the edifice of sustainable finance in the EU, and to fix those parts that do not work as intended.

1. The bigger picture: putting sustainable finance into perspective

Sustainable finance, including sustainable retail investing, has become something that not only retail investors and the financial institutions that serve them are interested in. Political actors have begun seeing it as a tool for mobilising (a part of) the money needed to finance the transition to a sustainable economy. In its *Strategy for Financing the Transition to a Sustainable Economy* of July 2021, the European Commission[1] emphasised the role that sustainable retail investment can play in financing the transition. People want to invest sustainably and we welcome that financial regulators and supervisors have decided to facilitate this, but we have mixed feelings about the high hopes that are associated with sustainable investing. Yes, it can contribute to transition, but only if it is part of a much broader effort that focuses not just on financial flows, but also the regulation of, and incentives for, the financed economic activities.

The capacity of sustainable finance, especially retail finance, to change the world is restricted chiefly by two factors. The first concerns the limitations of sustainable investing by regular, as opposed to very wealthy, retail investors. Retail investing usually means buying and selling securities on secondary markets, which means that there are no immediate effects of those investment decisions on the capital expenditure decisions of investee companies. There can be indirect effects, (see Section 2.1.1), but they depend on propitious conditions and are fundamentally uncertain.

1 European Commission, 'Strategy for Financing the Transition to a Sustainable Economy', 2021, https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52021DC0390 (accessed 18 April 2024).

The second, more severe limitation, concerns the real economy. Finance can only finance sustainable business activity if there is enough sustainable business activity to finance. It cannot simply *wish* it into existence. 'The EC [European Commission] have targeted the financial sector as a proxy hoping to accelerate the transition in the real economy. But the real economy will have to be targeted itself. Financial institutions are acting on risks and opportunities shaped by regulatory measures in the real economy. Not so much the other way around.'[2] Sustainable investing can support, but not replace more robust forms of economic policy intervention. After all, businesses react more immediately to subsidies, tax incentives or emissions standards that affect the relative profitability of sustainable and unsustainable business activities or, as a last resort, simple bans, than to the signals coming from securities markets.

Policy makers must not shy away from taking the decisions that really change how business is done by shifting too much of the responsibility for the sustainable transition onto the shoulders of consumers. Sustainability-conscious retail investors want to contribute to the transition, but their contribution can only be a modest one, and policy makers have not yet put the conditions in place to enable it. The remainder of this paper is essentially about those conditions.

2. What do consumers expect from the next Parliament and Commission?

Sustainability-conscious consumers can use different types of financial services in accordance with their preferences. As savers, they may want to buy a sustainable investment product or put their money in a sustainable savings account with a bank. But, as homeowners for example, they may themselves require green or sustainable financing from banks. This chapter looks at the needs of sustainability-conscious consumers concerning investment and banking services.

2.1. Sustainable investment services[3]

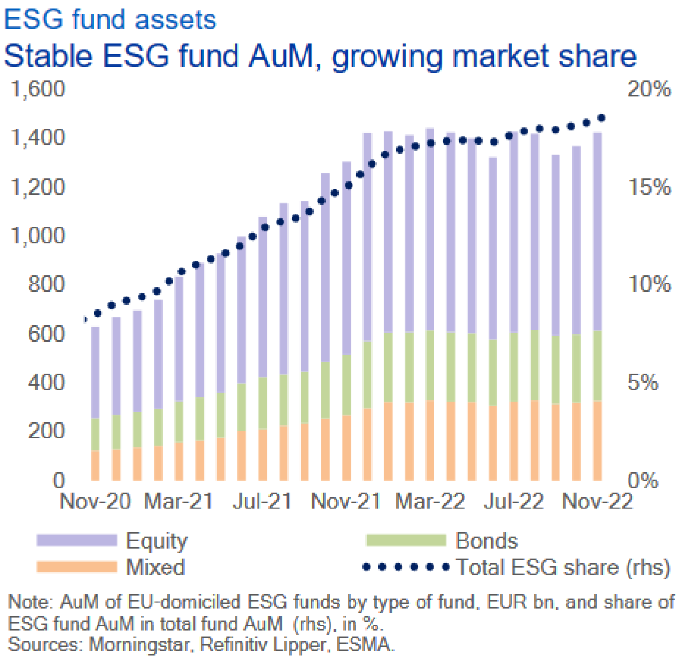
Investment products that are sold as 'sustainable', 'green' or 'ESG' are probably the most important type of sustainable financial products for consumers. They are also the ones that consumers complain about the most. The main problem is *greenwashing*, a mismatch between the content of the product and its name or marketing, but there are also complaints about the *complexity* of the products and the information materials that are supposed to help consumers choose. Despite these difficulties, there is no doubt about the strong demand for these products. According to a 2022 Eurobarometer survey,[4] over 60% of respondents find it 'important that their savings and investments do not fund economic activities that have a negative impact on the planet'. The amount of money that flows into sustainable investment funds in Europe is continuously increasing. Research by the European Central Bank shows that assets under the management (AuM) of investment funds and institutional investors with an explicit green/sustainable mandate have almost tripled between 2015 and 2021, rising to a total of over €1.4tn.[5] (See also Figure 1.) AuM of ESG funds are consistently growing as a share of the total fund AuM.

[2] Jakob König of Sveriges Konsumenter, private communication, September 2023.

[3] Many financial instruments and products through which you can invest are practically unavailable to retail investors on low to medium incomes, for example private equity, venture capital or investment funds that only accept wealthier and more sophisticated investors. Others are in principle available to regular retail investors, but are not commonly used by them. These include company shares and bonds or government bonds. The vast majority of normal people who have savings to invest use investment or pension funds that are open-ended and open to the general public. This paper assumes this as the default scenario for sustainable retail investment. In legal terms, we are talking about certain packaged retail and insurance-based investment products (PRIIPs), especially Undertakings for the Collective Investment in Transferable Securities (UCITS), insurance-based investment products (IBIP) and, to a lesser degree, Alternative Investment Funds (AIFs).

[4] Eurobarometer Retail Financial Services and Products, October 2022, https://europa.eu/eurobarometer/surveys/detail/2666, (accessed 18 April 2024).

Figure 1: Absolute assets under management of ESG funds and their share of total fund AuM[6]



The growth of ESG investment funds is likely to continue. Recent ESMA reports about the market for retail investment products have found that ESG investment funds attracted larger money inflows in 2021 and 2022 than non-ESG funds, almost tripling the amount of inflows compared to 2020.[7] ESMA's findings refer only to investment funds that fall under the Undertakings for Collective Investment in Transferable Securities Directive, or UCITS Directive, but this is by far the largest category of retail investment vehicles, especially for regular consumers. These inflows have taken the AuM of ESG UCITS funds to €1,058bn by the end of 2022, which corresponds to a little under 21% of the total AuM of EU equity, bond and mixed funds UCITS funds.

2.1.1. What do consumers want from sustainable investment products?

Sustainable investment can pursue different, even conflicting, goals and it can be done in different ways. As retail investors, consumers want a financial return, but they also want to avoid harming people and planet and/or contribute to making the world a better place. The oldest form of sustainable investing is about excluding from your investment portfolio businesses that contradict your values, whether those are religious or based on ethical convictions. In the past this meant excluding 'sin stocks' like gambling or alcohol, but today

5 European Central Bank, 'The performance and resilience of green finance instruments: ESG funds and green bonds', https://www.ecb.europa.eu/pub/financial-stability/fsr/focus/2020/html/ecb.fsrbox202011_07~12b8ddd530.en.html, November 2020, (accessed 18 April 2024); European Central Bank, 'Financial Stability Review, November 2021', https://www.ecb.europa.eu/pub/financial-stability/fsr/html/ecb.fsr202111~8b0aebc817.en.html (accessed 18 April 2018).

6 European Securities and Markets Authority, *ESMA Report on Trends, Risks and Vulnerabilities*, No. 1, 2023, p. 37, https://www.esma.europa.eu/sites/default/files/library/ESMA50-165-2438_trv_1-23_risk_monitor.pdf (accessed 18 April 2024).

7 European Securities and Markets Authority, *ESMA Market Report: Costs and Performance of EU Retail Investment Products 2023,* 18 December 2023, p. 24ff, https://www.esma.europa.eu/sites/default/files/2023-12/ESMA50-524821-3052_Market_Report_on_Costs_and_Performance_of_EU_Retail_Investment_Products.pdf; European Securities and Markets Authority, *ESMA Market Report: Costs and Performance of EU Retail Investment Products 2023*, 17 January 2023, p. 19, https://www.esma.europa.eu/sites/default/files/2023-01/esma50-165-2357-esma_statistical_report_on_costs_and_performance_of_eu_retail_investment_products.pdf (accessed 18 April 2024).

this means excluding stocks connected to harmful products, such as heavy greenhouse gas (GHG) emitters, producers of landmines or companies involved in severe human rights violations.

Another motive for investing sustainably is to make the world a better place with one's savings. This can mean supporting business activities that are already sustainable or promote a sustainable economy like renewable energy generation, also known as *impact* investing, or it can mean using share ownership to pressure currently unsustainable companies to improve their sustainability performance, e.g. through winding down or selling highly polluting factories. The latter approach is also called *transition* investing.
Financial motives can also play a role. Retail investors might assume that, for example, highly polluting companies are strongly exposed to financial risks that come from reputational damage and that it makes financial sense to avoid them.

The existence of these three motives that can be imputed to sustainability-conscious retail investors (value coherence/avoiding harm, improving the world, financial return) raises the question whether they can be pursued simultaneously or whether there are trade-offs. First, is it possible to avoid harm *and* have an impact on the world? In principle yes, but it depends on the type of impact sought and the range of activities excluded. It is perfectly possible for a sustainable portfolio to focus on investing in sustainable businesses in an attempt to support them while also excluding a wide range of unsustainable or ethically objectionable activities. However, combining a transition strategy with a strict exclusion or do-no-harm approach is more difficult. The point of transition investing is not to exclude bad businesses from one's portfolio, but to improve their sustainability performance through voting and shareholder engagement. It often focuses on high GHG emitters, that is, on companies that are actively harming the planet at the time of purchase. To influence them one must first buy their shares, whereas an exclusion-based approach would exclude them.

Second, can exclusion-based products that focus on avoiding harm also aim for real-world impact? In principle yes, and many retail investors who choose such products do not only want to have a clean conscience. They also want to be part of a divestment movement that makes it harder for very unsustainable businesses to fund their activities. However, selling or simply not buying a certain share has no immediate effect on what companies do, unless divestment pressure is large, and even then success is far from certain. (It is still an open question whether divestment can have real world effects. See Section 2.1.2 for a longer discussion.) For now, it therefore makes sense to treat the goals of impact and value coherence/harm avoidance as distinct, though not contradictory.

Third, are retail investors willing to accept a return that is, on average, lower than that of a conventional return-only investment if that is the price for pursuing sustainability goals? There are several reasons why a trade-off between return and sustainability performance may exist at product level. There is probably no perfect correlation between the financial performance of a stock or bond, i.e. their price movements and payouts in the form of dividends or coupons, and the sustainability performance of the companies or other entities that have emitted them. Maximising both types of performance for one investment portfolio is therefore also likely to involve trade-offs. Moreover, if a business activity or investment project is profitable it will normally be implemented by the business in question and receive financing from (conventional) lenders or investors regardless of its sustainability performance. Sustainable investors can invest in those, but if they wish to achieve impact they must also finance business activities that are relatively less profitable and yield lower financial returns.[8] On the other hand, there are empirical studies that suggest that sustainable assets, especially shares, perform equally well or better in terms of return than

[8] M. Wilkens and C. Klein, ‚Welche transformativen Wirkungen können nachhaltige Geldanlagen durch Verbraucherinnen und Verbraucher haben?' Verbraucherzentrale Bundesverband Germany, 2021, https://www.vzbv.de/sites/default/files/downloads/2021/02/11/gutachten_wilkens_und_klein_nachhaltige_geldanlagen.pdf (accessed 18 April 2024).

conventional ones.[9] Moreover, the above-mentioned ESMA market reports find that ESG UCITS funds tended to outperform non-ESG UCITS funds from 2019 to 2022, although they underperformed in 2022 due to the strong financial performance of the energy sector in that year, a sector that ESG funds tend to eschew. ESG funds also tend to be cheaper or at least not more expensive than non-ESG equivalents. The main exception are bond funds, where ESG ones perform worse than their non-ESG counterparts. Exchange-traded ESG equity funds (ETFs) are slightly more expensive than their non-ESG counterparts.[10]

In this paper we take no position on the question of whether sustainable investment products under- or outperform conventional ones. However, retail investors do not seem to mind very much. Studies and surveys suggest that they are willing to accept even considerably lower returns in exchange for better sustainability performance[11] although more research and consumer surveys are still necessary. Given that the evidence so far does not suggest relevant return drawbacks and that investors simply do not care even if such drawbacks existed, this question is irrelevant for our current purposes.

To conclude, there is no ideal-typical sustainable retail investor. There is a variety of motives, and any reform of the EU's sustainable investing regulatory framework should cater to this variety. However, what can be said for certain is that retail investors who shop for sustainable investment products do *not* expect to be sold **'best in class**' products or other investment approaches that pick companies whose sustainability performance is merely better, or less bad, compared to others in the same sector. No retail investor will see relative sustainability as genuine sustainability. Selling such products as 'sustainable', 'green' or 'ESG' is always greenwashing. The same applies to **'ESG integration**', if that means merely considering the effects that ESG factors may have on the product's financial performance because, as stated above, sustainability-conscious retail investors care about more than financial performance.[12]

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[9] G. Friede, T. Busch and A. Bassen, 'ESG and financial performance: aggregated evidence from more than 2000 empirical studies', *Journal of Sustainable Finance & Investment*, Vol. 5(4), 2015, p. 210-233, DOI: 10.1080/20430795.2015.1118917

[10] ETFs differ from the more traditional funds, so-called mutual funds, in that shares in them can be bought and sold on exchanges, like listed shares or bonds. They are typically passive investment vehicles, which means that they merely track a stock market or other kind of asset-related index, as opposed to active funds, where an asset manager picks the securities to be included in the fund portfolio. ETFs are popular among retail investors because they normally have lower fees than active funds.

[11] University of Cambridge Institute for Sustainability Leadership, 'Walking the talk: Understanding consumer demand for sustainable investing', 2019, https://www.cisl.cam.ac.uk/resources/sustainable-finance-publications/walking-the-talk-understanding-consumer-demand-for-sustainable-investing, (accessed 18 April 2024); R. Bauer, T. Ruof and P. Smeets, 'Get Real! Individuals Prefer More Sustainable Investments', *Review of Financial Studies*, Vol. 34(8), 2021, p. 3976–4043, https://doi.org/10.1093/rfs/hhab037; 2DII, 'A Large Majority of Retail Clients Want to Invest Sustainably', 2020, https://2degrees-investing.org/resource/retail-clients-sustainable-investment/ (accessed 18 April 2024).

[12] Cf. UNPRI, 'What is ESG integration?', 2018, https://www.unpri.org/investment-tools/what-is-esg-integration/3052.article (accessed 18 April 2024).

2.1.2. Real-world effectiveness of sustainable investing

There is no doubt that demand for **impact** products, i.e. those that promise to have an actual effect on the real world,[13] is strong and that it is met by a growing supply of often dubious products. But can sustainable investment really change the behaviour of companies and make a positive difference to people and planet?[14]

There are two types of impact that investors can aim to achieve: they can either try to help companies that have a positive impact on people or environment to grow, or they can try to convince or pressure harmful companies to improve. Theoretically, there are three main channels through which impact can be achieved: financial support for companies that have a positive sustainability impact, but struggle to get sufficient or sufficiently cheap financing; engagement to encourage or force improvement; influencing share prices and capital costs through exclusion/negative screening (intentionally or as a desirable side-effect of a value-alignment/do-no-harm strategy).

Helping positive impact-companies grow: One can help companies that have a positive net sustainability impact to grow by financing when conventional investors or lenders will not do so, but the financial instruments for this – private equity, private debt or venture capital – are typically not available to regular retail investors. Normally they only have access to publicly traded securities, usually through funds. It is, of course, possible for an investment fund that is available to the general public to focus on established listed companies that have positive impact, but these companies will normally already have access to sufficient finance from conventional investors and lenders. Therefore, the allocation decisions of that fund will not make a difference to the companies' growth and investment decisions. This is called the problem of '**additionality'**. It means that this kind of impact investing can only truly be said to have generated impact if the investee company takes action that it would not have taken in the absence of that investment.

Exclusion/negative screening has no immediate impact on the companies whose shares are sold or consciously not bought. Unlike directly supporting positive impact companies, no money flows, or is withheld, between investor and investee company. However, if a sufficiently large share of investors decides to sell a company's shares or bonds or communicates their decision not to buy them, there can be an effect on share or bond prices that can incentivise the company to change its behaviour. Unfortunately, it is hard to tell when that critical mass of investors has been reached, and empirical evidence that exclusion really affects companies is not strong. However, a recent statistical analysis of the 'effects of mutual fund decarbonisation on stock prices and carbon emissions'[15] has found 'cautious but consistent evidence' that share prices do indeed go down when selling pressure on a high-carbon stock is high and that the affected companies do reduce their carbon emissions. Still, retail investors who buy funds that use exclusion strategies must be aware that impact is highly uncertain and may be rather modest.

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[13] A 2022 survey of sustainable retail investors by the Dutch Financial Markets Authority AFM found that 49% wanted their investments to have impact, while 31% wished to align their investments with their values and another 21% want to invest sustainably because they believe that it will deliver better financial returns. (Autoriteit Financiële Markten, 'Duurzame beleggers in kaart. Onderzoek naar doelstellingen en verwachtingen van duurzame retailbeleggers', 2022, p. 10, https://www.afm.nl/~/profmedia/files/afm/trendzicht-2023/duurzame-beleggers.pdf?la=nl-NL (accessed 18 April 2024)). Research by the 2-Degrees-Investing-Initiative (2Dii) in six EU countries in 2022 confirms the importance of the impact motive for retail investors (2Dii, '6 National Country Reports', https://2degrees-investing.org/resource/the-6-national-country-report/, (accessed 18 April 2024)).

[14] The content of this section is largely based on the above-mentioned study by Wilkens & Klein as well as F. Heeb's and J. Kölbel's excellent and highly readable 'The Investor's Guide to Impact: Evidence-base advice for investors who want to change the world', 2020, https://www.csp.uzh.ch/dam/jcr:ab4d648c-92cd-4b6d-8fc8-5bc527b0c4d9/2020_CSP_Investors Guide to Impact_21_10_2020_spreads.pdf?_hsenc=p2ANqtz---eyny3UvF6oovZBfUJ6NB6RafCrGy6kMimVDF6QCAOwhX38RYpBDGU0PXPyoBDLCM00nk (accessed 18 April 2024).

[15] M. Rohleder, M. Wilkens and J. Zink, 'The effects of mutual fund decarbonization on stock prices and carbon emissions', *Journal of Banking & Finance*, Vol. 134, 2021, (https://doi.org/10.1016/j.jbankfin.2021.106352).

In the case of **engagement/stewardship**, the causality is simple: sustainability-minded shareholders use their rights to sway the management of an investee company to improve its sustainability through direct conversations with management or by tabling resolutions and voting at annual general meetings. The larger the shareholder or group of shareholders who demand those changes, and the more modest the demanded changes, the higher the chance of success. The problem with this strategy is that it requires a very well-defined plan about the precise goals that engagement is supposed to achieve, by when these goals are to be achieved and what is to be done when the investee company does not implement the necessary measures. Moreover, the strategy is best for achieving modest, incremental improvements, but no radical turnarounds.

Does successfully altering a company's behaviour or helping it to grow ultimately make a positive difference to people and planet? The truth is that we do not know. The chances of success are probably highest in the case of positive impact/growth investing, provided that the investee companies' net-positive impact can be determined with reasonable certainty. However, this investment approach is normally not available to regular retail investors. In the case of engagement/stewardship the uncertainty is higher, especially when an investee company's business model is inherently unsustainable as in the case of fossil fuel industries. For example, engaging in conversations with the management of an oil major to get it to reduce pollution risk in its operations, i.e. making sure that oil rigs, pipelines or oil tankers are safer from leakage, would not make its business model acceptable in the long term. If the same oil major reduces its scope-3 GHG emissions by selling some subsidiaries and transforming itself into a provider of renewable energy the sold-off assets will be operated by someone else, with zero effect for total GHG emissions. Uncertainty over the real-world effects of changes in corporate behaviour is the highest for exclusion/divestment strategies. As stated above, a recent study has found evidence that companies that are under strong selling pressure reduce their GHG emissions, but it is unclear how those reductions were achieved and whether they really reduce the total amount of GHGs that are emitted into the atmosphere.

The question of the real-world effectiveness of sustainable investing cannot be answered here, but it is clear that **impact depends on conditions that are not guaranteed and that success in the sense of changing something in the world is highly uncertain. This means that many investment products that claim to have impact are probably making false promises.** Given strong consumer demand we must be aware of the many question marks surrounding them and that no sustainable investment product can guarantee real-world impact.

2.1.3. Transparency and disclosure approach in sustainable finance has failed consumers

So far, the EU has relied mostly on an information and transparency approach to empower retail investors to make informed choices about sustainable investment options. The Markets in Financial Instruments Directive (MiFID II) and the Insurance Distribution Directive (IDD) require firms that sell investment products and investment advice to conduct a suitability assessment for each potential client. They must collect information about the client's knowledge and experience with investment products, their ability to bear losses and their investment objectives to be able to offer them a suitable product. This duty to collect information has recently been expanded to the potential client's sustainability preferences.[16] Firms must also inform clients about sustainability-related investment products and help them understand what they are about.

[16] European Securities and Markets Authority, 'ESMA publishes final guidelines on MiFID II suitability requirements', 2022, https://www.esma.europa.eu/press-news/esma-news/esma-publishes-final-guidelines-mifid-ii-suitability-requirements-0 (accessed 18 April 2024); European Insurance and Occupational Pensions Authority, 'EIOPA publishes guidance on integrating the customer's sustainability preferences in the suitability assessment under the IDD', 2022, https://www.eiopa.europa.eu/eiopa-publishes-guidance-integrating-customers-sustainability-preferences-suitability-assessment-2022-07-20_en (accessed 18 April 2024).

However, the Regulation on sustainability-related disclosures in the financial services sector (SFDR) is the most important EU law on transparency in sustainable financial services, especially investment products. It includes numerous disclosure and information obligations for financial market participants and their products, both before the conclusion of a contract and for ongoing information and reporting on websites and annual reports. Among other things, they must inform customers:

- How the product intends to achieve its sustainable features or objectives;
- Whether and how sustainability risks are taken into account by the financial firm in general and at the level of specific products;
- Whether a capital market index is used as a benchmark and how it fits the sustainability features or objectives;
- What the minimum proportion of sustainable investments in accordance with SFDR Article 2(17) in the fund portfolio is;
- What the proportion of environmentally sustainable investments in accordance with the EU Taxonomy Regulation in the fund portfolio is.

This is a lot of information to digest, and much of it is hard to understand or interpret correctly.[17] Apart from transparency, the SFDR does not impose any substantial requirements on financial firms. There are no minimum standards or rules for what can and what cannot be counted as a sustainable investment product. It does contain a definition of 'sustainable investments', but that definition applies to financial instruments like specific shares or bonds, not investment products that assemble a portfolio of these instruments. Moreover, the definition leaves too much discretion to fund managers.

Unfortunately, the SFDR has also become a weak *de facto* product standard because it introduced the categories of *financial products with environmental or social characteristics* – also called 'light green' or 'Article 8' products – and *financial products that have a sustainable investment objective* – 'dark green' or 'Article 9' products. This has contributed to greenwashing because retail investors do not understand that investment products sold as 'light- or dark-green' are based on weak sustainability criteria, especially in the case of Article 8 products. The European Commission and European financial supervisory authorities are aware of this and have published clarifications concerning SFDR[18] as well as regulatory proposals for certain minimum requirements for Article 8 and 9 products or for investment funds with sustainable-sounding names, such as a minimum content of sustainable investments in the fund portfolio.[19] We welcome this, but they are only small improvements because they have to stay within the conceptual confines of a weak law.

It is important to keep in mind the difference between financial professionals and retail investors. Thanks to the SFDR transparency requirements, experts may be able to assess an investment product in terms of its actual sustainability, but retail investors are generally unable to process and evaluate the information.

[17] Consumer studies on behalf of the European Supervisory Authorities in four EU countries in spring 2023 have confirmed this. European Securities and Markets Authority, 'Final Report on draft RTS on the review of PAI and financial product disclosures in the SFDR Delegated Regulation', 2023, https://www.esma.europa.eu/document/final-report-draft-rts-review-pai-and-financial-product-disclosures-sfdr-delegated (accessed 18 April 2024).

[18] Joint Committee of the European Supervisory Authorities, 'Consolidated questions and answers (Q&A) on the SFDR (Regulation (EU) 2019/2088) and the SFDR Delegated Regulation (Commission Delegated Regulation (EU) 2022/1288)', 2024, https://www.esma.europa.eu/sites/default/files/2023-05/JC_2023_18_-_Consolidated_JC_SFDR_QAs.pdf (accessed 18 April 2024).

[19] European Securities and Markets Authority, 'Update on the guidelines on funds' names using ESG or sustainability-related terms', 2023, https://www.esma.europa.eu/sites/default/files/2023-12/ESMA34-1592494965-554_Public_statement_on_Guidelines_on_funds__names.pdf (accessed 18 April 2024).

More or better transparency will not solve retail investors' problems because they have neither the time nor the expertise to make an informed choice between different products, let alone make a reasoned assessment of whether a product that is marketed as sustainable can live up to its promise. The EU must use the next legislative cycle to introduce a genuine product standard for sustainable investment products, complete with unambiguous and operational definitions, minimum requirements, intuitive product categories and labels.

2.1.4. Retail investors need real product standards and intuitive product labels

The Sustainable Finance Disclosure Regulation (SFDR) is the EU's main transparency law for sustainable retail investment products, but it was not designed with the information needs of consumers in mind. We need a law that defines what a sustainable investment product is, or what the different types of sustainable investment products are, and that sets minimum quality standards for them. Such a law must also define labels that tell retail investors what they are buying and that it is genuinely sustainable.

The investment industry uses a confusing variety of different terms and approaches for investment products that claim to be low- or zero-carbon, green or sustainable. This includes negative screening, positive screening, value-based investing, exclusion/divestment, transition, impact investing, best-in-class, stewardship/engagement etc. However, with the possible exception of the 'best in class' and 'ESG integration' approaches, which are 'sustainability-light' and not acceptable for sustainability-minded consumers, this variety boils down to **three principal strategies** (see also Sections 2.1.1 and 2.1.2:

- **Negative screening/exclusion**, i.e. the filtering out of assets that are associated with highly polluting or generally unsustainable business activities.
- **Transition or stewardship strategies**, i.e. positively selecting assets that are associated with businesses that are currently harmful but have the potential to 'clean up' thanks to fund managers' pressure.
- **Positive impact/growth**, i.e. positively selecting assets that are associated with business activities that contribute to some sustainability goal, such as emissions reduction, e.g. investing in renewable energy.

In 2022, the UK Financial Conduct Authority (FCA) proposed three product categories with accompanying labels that correspond roughly to these three strategies.[20]

Figure 2: FCA proposal for sustainable investment labels/categories[21]

[20] The final rules for 'Sustainability Disclosure Requirements (SDR) and investment labels' were published in November 2023 (https://www.fca.org.uk/publications/policy-statements/ps23-16-sustainability-disclosure-requirements-investment-labels (accessed 18 April 2024)). Sadly, instead of sticking to the three clearly defined product categories, the FCA has added a fourth, called 'Sustainability Mixed Goals', that muddies the waters again.

[21] Financial Conduct Authority, 'Sustainability Disclosure Requirements (SDR) and investment labels: Consultation Paper CP22/20', 2022, p. 30, https://www.fca.org.uk/publication/consultation/cp22-20.pdf (accessed 18 April 2024).

'Sustainable Focus' products 'aim to invest in assets that a reasonable investor would regard as being environmentally and/or socially sustainable'.[22] Apart from excluding assets associated with harmful companies or industries, the FCA proposal also requires 'positive screening', i.e. including assets from companies that make a positive contribution to a particular sustainability goal.

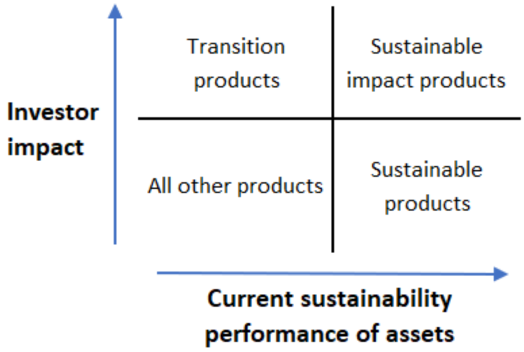
'Sustainable Improvers' products 'aim to invest in assets that, while not objectively environmentally or socially sustainable at present, have the potential to deliver measurable improvements in their environmental and/or social sustainability over time, including in response to the stewardship influence of the firm'.[23] This corresponds to the 'transition/stewardship' approach. These products would need criteria for selecting the companies to invest in to make sure they include only those that have a realistic chance of improving. They must also hold investee companies to well-defined improvement targets and define points that would trigger escalation or, ultimately, divestment if engagement is not successful in transforming the company.

'Sustainable impact' products 'aim to achieve a positive, measurable contribution to real world sustainability outcomes'.[24] They correspond broadly to the positive impact/growth strategy. They require additionality, i.e. the investment must make a real contribution to those positive sustainability outcomes. (In contrast to the Sustainable Focus products, that also invest in companies that contribute to a sustainability goal, but where the investment is not required to have an impact on investee companies' behaviour.)

In November 2023, the Dutch financial supervisory authority AFM made a similar proposal for a categorisation and labelling system that distinguishes between products with (i) a 'transition' label, (ii) a 'sustainable' label and (iii) a 'sustainable impact' label.[25] These categories 'differ on the one hand in terms of the current level of sustainability of the underlying assets and on the other hand in terms of the impact (additionality) of the investment itself'.[26]

[22] Financial Conduct Authority, 'Sustainability Disclosure Requirements (SDR) and investment labels', p. 32.
[23] Financial Conduct Authority, 'Sustainability Disclosure Requirements (SDR) and investment labels', p. 34.
[24] Financial Conduct Authority, 'Sustainability Disclosure Requirements (SDR) and investment labels', p. 36.
[25] Autoriteit Financiële Markten, 'AFM position paper on improving the SFDR', 2023, https://www.afm.nl/~/profmedia/files/rapporten/2023/afm-position-paper-on-improving-the-sfdr.pdf (accessed 18 April 2024).
[26] Autoriteit Financiële Markten, 'AFM position paper on improving the SFDR', p. 4.

Figure 3: AFM proposal for sustainable investment labels/categories



Products with a 'transition' label must aim to 'generate positive, measurable social or environmental impact alongside a financial return'. To that end, they must have an 'investor impact strategy,' which includes measurable impact targets, a shareholder engagement strategy and criteria and thresholds for divesting when the strategy fails. Investee companies must have credible transition plans, and the fund itself must have transition targets for decarbonisation and/or biodiversity. Products with the 'sustainable' label do not need to generate impact, but they must invest only in assets that are currently sustainable and do no harm. Apart from excluding shares or bonds connected to harmful activities, they should also invest a certain part of their portfolio in activities that contribute to a sustainability goal. Products in the 'sustainable impact' category must 'seek to make direct and measurable impact through investments, by financing underserved markets or companies that have a tangible positive impact on sustainability factors' in order to help these companies grow. They must also exclude harmful activities.[27]

This approach to product standardisation and labelling corresponds to different consumer motives for sustainable investing, which makes the categories more intuitive and should enable consumers to choose something that corresponds as far as currently possible to their wishes. Moreover, it can draw a crystal-clear distinction between sustainable investment products and investment products that are not sustainable and make no claim to it because any product that qualifies for one of the three labels is sustainable, albeit in different ways, while all others are not. There are no in-between products that are 'a little sustainable'.[28] This would provide much-needed clarity and simplicity to the market for investment products. Another advantage of this approach is that it is based on investment strategies that are already used in the fund industry. It codifies and standardises them through statutory requirements, making them more reliable and making different products comparable.

However, realising these potential benefits also requires certain **supporting rules**. First, the three categories must be mutually exclusive so that products remain clear and intuitive for retail investors. That does not mean that all products offered under one category have to be the same or that mixing different strategies should be banned, but a product can only have one label and mixing must not lead to violations of the requirements attached to that label. Second, investment products that are not sustainable because they do not meet any of the three sets of criteria must not be allowed to use product names or advertising of any kind that sounds or looks 'green' or sustainable, and they should also not be allowed to use terms that are similar to those used in the sustainability labels. Third,

[27] This product would be relatively risky and best suited for investors who can forego a certain amount of return in exchange for measurable impact. This would, therefore, not commonly be suitable for regular sustainability-conscious retail investors.

[28] The only possible justification for the existence of less sustainable products that we can think of would be the existence of a trade-off between financial performance and sustainability performance. However, as explained in section 2.1.1, there does not seem to be strong empirical evidence for such a trade-off. Why, then, should sustainability-conscious retail investors accept a lower sustainability performance if they are not rewarded with better returns?

investment products that make no claim to sustainability should also be subject to sustainability-related disclosure requirements, more precisely: disclosures about negative sustainability impact. The SFDR currently requires some, but not all, products to disclose sustainability-related information, including information about whether and how any negative sustainability impact of the product's investment portfolio is considered. Making them mandatory for all would solve the problem that sustainable products incur higher costs for monitoring sustainability performance and are therefore at a competitive disadvantage. Moreover, the public deserves to be informed about the actual and potential harm associated with a product. Fourth, products that do not fit into any of three categories should have to carry a clear and visible disclaimer that they are highly likely to contain a significant amount of harmful exposure. This is akin to health warnings on cigarettes that warn buyers about the consequences and raise general awareness about the harm of this product.

BEUC recommendations

- **Three mutually exclusive investment product categories and labels should be established on the basis of investment strategies, similar to proposals from the Dutch Financial Markets Authority and the UK Financial Conduct Authority.**
    - **Products that do not fulfil the criteria of any of the three categories must not be sold as green or sustainable and carry a warning that they are likely to contain harmful exposures. However, they should also be subject to minimum disclosures about their negative sustainability impact.**

2.1.5. The role of financial advice in sustainable finance

Regular retail investors will typically talk to a financial adviser at their bank or another financial institution before they buy a sustainable investment product. Advisers conduct a suitability assessment that must now also include a conversation about the prospective client's sustainability preferences. Unfortunately, the quality of advice and customer information is unsatisfactory. A mystery shopping exercise among large Spanish banks and fund managers by BEUC's Spanish member ASUFIN found that advisers often lack knowledge and do not seem to have the requisite training or qualifications.[29] Research by 2Dii in six EU countries in 2022/23 also found that the quality of sustainability-related financial advice left a lot to be desired.[30] Advisers often did not ask questions about the potential client's sustainability preferences, despite the legal obligation to do so. **Financial supervisors should require advisers to have sufficient sustainability competences** and make sure that they inform prospective clients correctly about the sustainability features and performance of the offered products. Generally speaking, **prospective advisers should have to undergo professional training**, e.g. a one-year university course or three years of vocational training, which they must finish with an examination before a higher education institution whose curriculum is officially accredited or another certified provider. The training itself should be certified by the national financial supervisor. Another problem of the sustainability-related financial advice process as laid down in MiFID and IDD is that it follows the definitions and concepts developed in the SFDR. It is reasonable to align the rules for financial advice with those of the main sustainable finance disclosure regulation, but, as we argued in Section 2.1.3, the latter is hard to understand for regular retail investors, so this problem is likely to affect the quality of advice, too. It

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29 ASUFIN, 'Mystery shopping: MiFID II Reform Compliance with retail investor sustainability preferences', 2022, https://www.asufin.com/wp-content/uploads/2024/04/221125_I_STUDY_MYSTERY_SHOPPING_MiFID_II_ENG.pdf (accessed 18 April 2024).

30 2DII, 'Moving the blockers of retail sustainable finance', https://2degrees-investing.org/resource/moving-the-blockers-of-retail-sustainable-finance/ (accessed 18 April 2024).

is possible to fine-tune advice to make it more consumer-friendly,[31] but it would be better to **define product categories and labels that are intuitive and correspond to retail investors' preferences and *then* adjust the rules for sustainability-related investment advice in IDD and MiFID accordingly**. In any case, the suitability assessment for sustainability preferences must be precise enough to prevent the mis-representation of the customer's preferences because this can lead to mis-selling in the form of recommending less sustainable products than what the customer actually wants.
Another problem is the **lack of independent advice**. Except for the Netherlands, advisers receive sales commission from product sellers and are therefore in a conflict between their self-interest to earn commission and the interest of the client who wants the most suitable product. The European Commission has acknowledged the problem in its Retail Investment Strategy, but unfortunately it stopped short of an outright ban of commission payments in relation to investment products. This affects the quality of financial advice in general, but also affects the sale of sustainable investment products. Wealthier consumers can try to avoid sub-optimal products by paying for independent advice, but those that need advice the most do not have this option.

BEUC recommendations

- **Financial supervisors should require advisers to have sufficient sustainability competences and verify that they inform prospective clients correctly about the sustainability features of offered products. Prospective advisers should also have to undergo professional training.**
- **Financial advice must be independent and work for consumers, not the advisers. Therefore, we demand a ban on sales commission.**

2.2. Sustainable retail banking and financing products

2.2.1. Sustainable/green savings and current accounts

What about consumers who wish to invest (some of) their savings sustainably, but through the safe, if old-fashioned, vehicle of savings accounts? So-called ethical banks attract client deposits by promising that they will not finance environmentally or socially destructive activities and/or focus their lending on businesses with a positive net sustainability impact. Conventional commercial banks have also started marketing 'green' current or savings accounts. The difference between an account with an ethical bank and a 'green' account with a conventional bank is that the former's own lending policies exclude financing harmful activities, while the latter claims that the client's savings will not be used for financing harmful activities, even though the bank continues to do so.[32]

How strong is consumer demand for green or ethical banks accounts? A recent study by our British member Which? found that of 'the 1,463 Which? members that were asked in January [2023], seven in ten (69%) picked opening an account with a sustainable bank as the least important way to tackle climate change, from a list of options that also included

[31] Finance Watch have made some suggestions for improvements: '*A guide to the next sustainable finance agenda Limitations of the current framework and recommendations for an effective transition*', 2024, p. 36, https://www.finance-watch.org/policy-portal/sustainable-finance/report-a-finance-watch-guide-to-the-next-sustainable-finance-agenda/ (accessed 18 April 2024).

[32] Basically, the ethical bank says to the client 'we do not finance bad stuff, so you can give us your money without worries', while the conventional bank that offers a green account says 'we do finance bad stuff, but your money will not be a part of it'.

flying less and recycling'.[33] Anecdotal evidence from other BEUC members confirms that consumer demand for 'green/sustainable' bank accounts is weak.

Can there even be such a thing as a 'green/sustainable' bank account in the case of conventional banks? Is it possible to separate the customer deposits paid into a 'green' account from the non-sustainable lending business of the bank? It is a common misconception that commercial banks take customer deposits with one hand and then pass them on to businesses as loans with the other. In reality, the connection between a bank's deposit taking and lending is much weaker. Banks do not pass money on when they lend, they *create* it.[34] Nonetheless, some banks claim that they can 'earmark' green deposits and trace specific loans back to specific deposits through *separate accounting* for conventional and 'green' deposits and loans.[35] An example for a different way of how this could work is provided by a small Italian coop bank that offers an account where depositors as well as the bank as lender voluntarily accept lower interest rates.[36] Since this seems to be coupled with a stringent list of criteria for what can and cannot be funded, there does appear to be an indirect connection between deposit and lending because the fact that depositors demand lower interests enables the bank to demand lower interest, too. However, this only works with banks that are not profit-maximising, so not for conventional banks.
We are not fully convinced that accounting separation and other mechanisms of tracing or attributing specific client deposits to parts of a bank's lending are fail-safe. Moreover, unless both clients and bank are willing to accept lower interest rates there is no guarantee that the 'green' deposits affect the bank's lending business or induce it to lend to businesses to which it would not have lent in the absence of those 'green' deposits (additionality problem). We do not rule out that sophisticated tracing and earmarking techniques can establish a meaningful connection between deposits and lending, but **consumers who wish to deposit their money sustainably should probably use ethical banks. If that is no option, they can open a 'green account' with a conventional bank and make inquiries about how that bank connects 'green' deposits and 'green' lending'.** Given these uncertainties, there is also a considerable greenwashing risk. There have been cases of where conventional banks sold 'green' accounts without any, or insufficient, substantiation of those green claims.[37]

Supervisors should make sure that conventional banks that sell 'green' or 'sustainable' accounts have very good tracking or earmarking systems in place to ensure an effective

[33] Which?, 'Which? puts major high-street banks in "red" warning category based on green credentials', 2023, https://press.which.co.uk/whichpressreleases/which-puts-major-high-street-banks-in-red-warning-category-based-on-green-credentials/ (accessed 18 April 2024).

[34] The Bank of England has published a highly readable explainer about the role of commercial banks in the modern monetary system: 'Money in the modern economy: an introduction' and 'Money creation in the modern economy', both in *Quarterly Bulletin 2014 Q1*, https://www.bankofengland.co.uk/-/media/boe/files/quarterly-bulletin/2014/money-in-the-modern-economy-an-introduction.pdf and https://www.bankofengland.co.uk/-/media/boe/files/quarterly-bulletin/2014/money-creation-in-the-modern-economy.pdf (accessed 18 April 2024).

[35] Accounting separation is the solution that was envisaged by the currently dormant EU Ecolabel for retail financial products. (See Joint Research Centre, 'Development of EU Ecolabel criteria for Retail Financial Products: Technical Report 4.0', p. 31) The same applies to the Austrian Ecolabel for retail financial products (Österreichisches Umweltzeichen, 'Austrian Ecolabel Guideline UZ 49: Sustainable Financial Products. Version 6.0', 2024, https://www.umweltzeichen.at/file/Guideline/UZ%2049/Long/UZ49_R6.0a_Sustainable%20Financial%20Products_2024_EN.pdf, (accessed 18 April 2024), and it is indeed the solution used by the Raiffeisenbank Gunskirchen, a small Austrian coop bank ('Umweltgarantie', https://www.umweltcenter.at/umweltgarantie (accessed 18 April 2024)).

[36] Raiffeisen Bozen, 'Unser Ethical Banking-Sparkonto', https://www.raiffeisen.it/de/bozen/wir-sind-genossenschaft/ethical-banking/ethical-banking-sparkonto.html (accessed 18 April 2024); Raiffeisen Bozen, 'Nachhaltig investieren. 20 Jahre Ethical Banking', *Magazin 02/2020*, 2020, https://magazin.raiffeisen.it/wp-content/uploads/2020/03/RV_Magazin_Ausgabe_02_20_200324_ONLINE_DE.pdf (accessed 18 April 2024).

[37] The regional German consumer organisation Verbraucherzentale Baden-Württemberg has launched successful complaints and lawsuits against banks and neobanks that have offered savings or current accounts with dubious promises of climate-neutrality or positive impact. More information here: 'Greenwashing bei der Geldanlage: Werbung mit Nachhaltigkeit', 2023, https://www.verbraucherzentrale-bawue.de/greenwashing (accessed 18 April 2024).

connection between deposits and lending. Banking supervisors should use the anti-greenwashing powers under the recently adopted [Directive for Empowering Consumers for the Green Transition] to verify whether accounts that are marketed as green comply with the new requirements. The [Green Claims Directive] is still (May 2024) being negotiated, but, once applicable, it should give supervisory authorities more far-reaching powers to move against unsubstantiated claims about 'green' accounts. Supervisors should also crack down on entity-level greenwashing by conventional banks that try to entice consumers to open accounts by portraying themselves as green or ethical, even if they do not make any claims about the accounts as such.

BEUC recommendations

- **No need for regulatory measures, but supervisors should ensure that conventional banks that sell 'green' or 'sustainable' accounts have very good tracking or earmarking in place to ensure an effective connection between deposits and lending.**

2.2.2. Green loans for product purchases and home ownership/renovation

In sustainable retail finance, consumers are usually in the position of having money that they want to put into a sustainable investment or savings product. However, many consumers also want to contribute to sustainability goals, especially climate change mitigation, through the way they spend their money. This includes renovating their homes, switching to more efficient household appliances, heat pumps and electric cars. When consumers borrow to buy energy-efficient homes or consumer products with sustainable credentials a completely different set of questions arises than in the sustainable investment area. Here we are not concerned with making sure that financial products hold what they promise, i.e. with product standards and the fight against greenwashing, but with the costs and conditions of accessing 'green' financial products, in this case loans or mortgages. High up-front costs often deter consumers from these purchases, therefore we need new borrowing instruments that are tailored to consumer needs and cheaper than conventional loans. This section looks at green consumer loans and mortgages and how they can be promoted. (The Energy Efficiency Directive and the Energy Performance of Buildings Directive address the availability of green loans and mortgages, but not consumer protection more generally, the cost of credit, or which type of lending product can be sold as 'green').

Green loans and mortgages from commercial banks are usually not affordable for lower-income households. They require public financial support in some form, either subsidies or very low to zero interest rate loans from publicly owned development banks. This section talks mainly about green borrowing instruments that can be marketed to consumers on a commercial basis, but also discusses how publicly-backed schemes can help lower-income households.

What are the financial incentives for taking out and providing green loans and mortgages?

Green loans and mortgages can be used by consumers to purchase an energy-efficient home, retro-fitting their current home or to purchase an energy-inefficient home with the condition that they will retrofit it. They are available in several EU Member States, but not always at an attractive interest rate. Mystery shopping by our Spanish member ASUFIN showed that conventional mortgages have on average lower interest rates than those marketed as green.[38] In Portugal, on the other hand, the central bank caps the costs of consumer loans and that cap is lower for green loans than for conventional consumer credit.[39] Green loans and mortgages must be cheaper than conventional ones if they are to contribute to the energy transition.

Why should commercial banks lend at lower interest rates? There are at least two tools for making such lending attractive to them. The European Central Bank (ECB) could grant favourable re-financing conditions to banks that meet specific green loan targets. The Targeted longer-term refinancing operations (TLTRO) programme[40] currently grants attractive conditions to commercial banks that focus their lending on the non-financial sector and households. The TLTRO does not take sustainability concerns into account but could be modified to incentivise green lending.[41] Another option for making comparatively cheap green loans attractive for commercial lenders is through public guarantees that reduce the default risk.

Lower-income households often live in the worst-performing buildings where the greatest energy savings could be made, but they are typically not able to borrow large sums from commercial banks. There should be public programmes (e.g. subsidies for renovating the worst-performing buildings) to ensure that the energy transition is affordable for them, too. The German state-owned development bank Kreditanstalt für Wiederaufbau (KfW), for example, offers subsidised loans where part of the principal does not have to repaid,[42] and the Dutch Warmtefonds provides interest-free loans for energy renovations up to a household income of €60,000.[43]

BEUC recommendations

- **When the Mortgage Credit Directive comes up for review, it should be amended to require Member States to oblige mortgage lenders to offer green mortgages at a lower total cost of credit than conventional mortgages.**
- **When transposing the Consumer Credit Directive, Member States should introduce lower cost caps for green loans than conventional loans.**
- **Lower-interest rate green lending should be made attractive for commercial banks through cheaper refinancing by central banks and/or public guarantees for green loans and mortgages.**
- **Public financing or incentive schemes should be available for lower-income households, especially those who live in the least energy-efficient buildings.**

Legally sound and forward-looking definitions of green loans and mortgages

[38] Asufin, 'IV Study on Green Finance in Spain, 2023, https://www.asufin.com/wp-content/uploads/2024/04/231121_IV_ESTUDIO_FINANZAS_VERDES_SEPTIEMBRE_2023_INGLES.pdf (accessed 19 April 2024).

[39] Banco de Portugal , ,Interest rates in consumer credit', https://clientebancario.bportugal.pt/en/interest-rates-consumer-credit (accessed 19 April 2024).

[40] European Central Bank, 'Targeted longer-term refinancing operations (TLTROs)', https://www.ecb.europa.eu/mopo/implement/omo/tltro/html/index.en.html (accessed 19 April 2024).

[41] This idea was floated by Positive Money Europe in 2021: 'Money looking for a home: How to make the European Central Bank's negative interest rates pay for building renovations', https://www.positivemoney.eu/wp-content/uploads/2021/02/2021_Building-Renovation-TLTROs.pdf (accessed 19 April 2024).

[42] Kreditanstalt für Wiederaufbau, 'Ihre Förderung für Haus und Wohnung', https://www.kfw.de/inlandsfoerderung/Privatpersonen/Bestandsimmobilien/ (accessed 19 April 2024).

[43] Nationaal Warmtefonds, https://www.warmtefonds.nl/ (accessed 19 April 2024).

Consumers invest money and time when renovating their homes or changing their heating appliance. The worst outcome is when they realise that they invested in the wrong way and the energy savings do not materialise. This includes buying a hydrogen-ready boiler and being exposed to high heating costs in the future,[44] undertaking a renovation that does not achieve the standard for a heat pump-ready home, or buying a hybrid car whose total ownership cost is higher than going fully electric.[45] Green loans and mortgages should be designed in a way that guides consumers to the right investment, both from a climate and economic perspective and avoid fossil lock-in effects.[46]

This requires consistency between EU laws. If the definition of green loans and mortgages were to be based on the EU Taxonomy Regulation the Taxonomy criteria would have to be aligned with the Fit for 55 package as soon as this package is fully adopted. For example, the Commission proposal for a new Energy Performance of Buildings Directive foresees that all new buildings must be zero-emission by 2030, whereas, according to the Taxonomy, all new buildings must only meet *near* zero-emission standards. Moreover, in line with the Fit for 55 package, green loans should not be available for fossil fuel technologies (e.g. gas boilers).

The definition of green loans and mortgages should also be fine-tuned so that purchases enabled by these loans and mortgages do not have the paradoxical effect of increasing, rather than reducing, overall energy and resource consumption. For example, mobility-related green loan programmes should help low- and middle-income households buy a reasonably-sized electric car or electric (cargo) bike rather than incentivising wealthy consumers to buy over-sized electric SUVs. On the consumer side, low-interest green loans and mortgages should be subject to the use of proceeds requirements to ensure that loaned money is used only to purchase green items.
Green loans should also be available for financing housing stock modifications that reduce energy consumption through other means than efficiency improvements, such as dividing one dwelling into two. This can be attractive for people whose children have moved out. The German public bank KfW already provides subsidised loans for such purposes.[47] Such schemes could, for example, be implemented when transposing the Energy Efficiency Directive, the Energy Performance of Buildings Directive and supported by funding from the Social Climate Fund.

BEUC recommendations

- **When the Mortgage Credit Directive comes up for review, a definition of green mortgages should be introduced that is consistent with the EU energy and climate goals and excludes items that are not aligned with those goals, such as gas boilers or renovation projects that do not lead to heat pump-readiness. A definition of green loans should also be inserted into the Consumer Credit Directive.**

- **The definitions of green loans and green mortgages should be fine-tuned so that green lending contributes to lower overall energy consumption (energy sufficiency).**

[44] BEUC, 'Goodbye gas: heat pumps will be the cheapest green heating option for consumers', 2021, https://www.beuc.eu/press-releases/goodbye-gas-heat-pumps-will-be-cheapest-green-heating-option-consumers (accessed 19 April 2024).
[45] BEUC, 'Electric cars: Calculating the total cost of ownership for consumers', 2021, https://www.beuc.eu/sites/default/files/publications/beuc-x-2021-039_electric_cars_calculating_the_total_cost_of_ownership_for_consumers.pdf (accessed 19 April 2024).
[46] Political support should be offered as a long-term measure to avoid spikes in demand for certified installers and raw materials or frustration when projects suddenly stop at an advanced stage of the planning process.
[47] Kreditanstalt für Wiederaufbau, ‚Altersgerecht Umbauen – Kredit', https://www.kfw.de/inlandsfoerderung/Unternehmen/Wohnwirtschaft/Finanzierungsangebote/Altersgerecht-umbauen-(159)/ (accessed 19 April 2024).

Barriers to access to green loans and mortgages

Consumers are not energy or financial experts. They need independent advice on which investment makes sense from a climate perspective and which financing instrument is suitable for them. Banks and installers have information about their respective products, but they will not help consumers find a certified installer or help them with the energy audit, loan and subsidy applications or budget planning. Consumers need one-stop shops that provide independent advice on all the necessary steps of the retrofitting project and suitable financing options. BEUC's Belgian member Testachats/Testaankoop has been raising awareness among consumers about the jungle of private and public funding options. There are 'classic renovation loans' and 'energy renovation loans,'[48] with the latter offering more attractive interest rates. Bank staff should be able to inform consumers about green loans and mortgages and be obliged to tell them about the closest one-stop shop for renovation and energy retrofit projects which will be set up when implementing the Energy Efficiency Directive and the Energy Performance of Buildings Directive. Banks and one-stop shops should cooperate to assess the viability and eligibility of the renovation project, factoring in all relevant technical and financial elements and exchange data. (If the exchanged data includes personal consumer data it must be subject to the consumer's consent). For example, the German KfW offers green loans together with technical advice by cooperating with a wide-spread network of qualified energy experts.

Creditworthiness can be another barrier, and the energy crisis has shown that energy bills are a significant chunk of household expenditure. Energy consumption should be factored into the creditworthiness assessment, but that must include the positive effect that lower consumption after a retrofit has on net household income, provided that it can be reliably determined. This can be tricky given low data quality, possible hidden follow-up costs or overly optimistic energy savings promises from appliance manufacturers. Lower-income households, however, may still not be eligible for a loan, even if energy savings are considered. For them there must be generous subsidies to help them renovate their homes.

BEUC recommendations

- **Banks should be required to train enough staff to provide advice about green loans and mortgages.**
- **Energy consumption, including expected energy savings from energy retrofitting, should be factored into creditworthiness assessments.**
- **Member States should set up independent advice structures (one-stop shops) when transposing the Energy Efficiency Directive and Energy Performance of Buildings Directive.**

Leasing and equity release: new, so far unregulated lending products

We have recently seen a surge of new types of lending products that are so far unregulated. Leasing agreements for heat pumps and electric cars that do not include an option or obligation to buy the leased item are not covered by the Consumer Credit Directive. In the case of mortgages, lenders offer so-called equity release schemes where some equity of the property is released to finance renovation. Many of these products do not make economic sense, but are advertised as attractive options for sustainable purchases. Many leasing agreements are far more expensive than paying directly or using a conventional consumer loan. BEUC has observed that providers factor in state subsidies to make the offer look more attractive, meaning the subsidy goes to the supplier rather than the

[48] Test-Achats/Test-Aankoop, 'Batibouw: voici les meilleurs prêts à la rénovation', 2023, https://www.test-achats.be/argent/prets-renovations/news/pret-renovation; Test-Achats/Test-Aankoop, 'Batibouw: vergelijk de beste renovatieleningen', 2023, https://www.test-aankoop.be/geld/renovatieleningen/nieuws/renovatieleningen?int_campaign=service-hub&int_source=hubv2&int_medium=hub-about&int_content=news&int_term=latest-highlights (accessed 19 April 2024).

consumer. Moreover, the (financial) conditions for purchasing the heat pump at the end of a contract are often unclear, with additional undisclosed sums to be paid. If consumers cannot pay, they will continue to depend on renewed leasing agreements for their heating. If the leasing agreement takes the form of a long-term rental agreement, the Consumer Credit Directive does not apply. This means that the provider does not have to do a creditworthiness assessment, can bypass cost caps that apply to consumer credit and is not required to offer forbearance measures in case consumers encounter financial difficulties.[49]

The Energy Efficiency Directive promotes on-bill schemes as an innovative way of financing. When such schemes are introduced, consumers should be protected by the Consumer Credit Directive and given transparent information about the pricing of these products. As reported by BEUC's Portuguese member DECO, on-bill schemes are offered allegedly as a zero-interest loan, but the overall price of the appliance (e.g. solar panels) can be higher when using an on-bill scheme than with traditional consumer credit.

Equity release schemes are schemes where consumers sell part of their home in exchange for a larger lump-sum or monthly payments while continuing to live in their homes. These schemes are offered as a way of financing renovation projects, but they are harmful for consumers who lose a lot of money and in some cases even the status as owner of their house (sell and lease schemes).[50] Our member Which? found that some equity release schemes capture more than 70% of the home's value for just a 20% advance.[51] Meanwhile, ASUFIN calculated how much of the value of their property a consumer would receive if using an equity release scheme. They found that a consumer who reaches 83.3 years (the average life expectancy in Spain) would only get 18.4% of their initial property value. That share rarely surpasses 30-35% of the property value even for people who live longer than that.[52] The German Financial Supervisor calculated different scenarios and showed that it is very rare for consumers *not* to lose money in equity release schemes and warns consumers that they risk losing their home if they cannot pay the monthly 'user fee'.[53]

BEUC recommendations

- **When transposing the Consumer Credit Directive, Member States should include long-term rental agreements and on-bill schemes for financing the purchase of items like electric cars and renewable energy equipment in the scope of the Directive.**
- **The revision of the Mortgage Credit Directive should bring equity release schemes and similar products, such as sale-and-lease schemes, under its scope and introduce adequate protections, like cost regulations or product intervention powers for supervisory authorities.**

49 BEUC, 'From boilers to heat pumps', 2023, https://www.beuc.eu/sites/default/files/publications/BEUC-X-2023-102_From_Boilers_to_Heat_Pumps.pdf (accessed 19 April 2024).
50 For example, sale and lease schemes in Portugal: DECO, '"Crédito fácil": DECO alerta para as promessas de dinheiro em troca da garantia da sua casa!', https://deco.pt/servicos-financeiros/credito-facil-promessas-de-dinheiro-garantia-casa/ (accessed 19 April 2024).
51 Which?, 'What is equity release? Lifetime mortgages, costs and fees explained, 2024, https://www.which.co.uk/money/pensions-and-retirement/youre-retired-working-on-benefits-equity-release/equity-release/what-is-equity-release-a5jqy4d36xlv (accessed 19 April 2024).
52 INMO NEWS, 'Análisis de la hipoteca inversa por Asufin', 2021, https://www.inmonews.es/analisis-de-la-hipoteca-inversa-por-asufin/ (accessed 19 April 2024).
53 Bundesanstalt für Finanzdienstleistungsaufsicht, ‚Teilverkauf Ihrer Immobilie – wo stecken die Risiken?', https://www.bafin.de/DE/Verbraucher/KrediteImmobilien/Immobilienfinanzierung/Immobilienteilverkauf/Immobilienteilverkauf_node.html (accessed 19 April 2024).

3. Supervision and enforcement[54]

The best laws for green loans and sustainable investment products are only as good as their practical implementation, and that requires vigorous monitoring and enforcement. The laws for sustainable retail finance and banking services may be made at EU level, but day-to-day supervision and enforcement is largely left to national financial supervisors in the Member States. Unfortunately, many of them do not have a clear legal mandate to protect consumers or do not have sufficient powers and resources. Apart from reducing the effectiveness of financial supervision, it also means that its quality is patchy across the EU. Quality and consistency of financial supervision in the EU must be improved, with the final goal being supervisory convergence to ensure the development, implementation and monitoring of minimum standards of business conduct supervision at national level. This should ultimately lead to a *single rulebook for business conduct*.

The European Financial Supervisory Authorities (ESAs) should focus on enforcing the rules for market conduct as much as they focus on financial stability or prudential concerns. They should use the convergence tools at their disposal systematically to identify dysfunctions in the markets for retail financial services and to promote best practices for enforcing proper conduct by financial firms. The power to coordinate mystery shopping by national supervisors can serve to identify such shortcomings, while the power to conduct peer reviews of the activities of national supervisors can help to remedy them. Making these interventions more effective requires giving more powers to national supervisors and creating formal collaboration channels with other authorities, especially consumer protection agencies, as well as consumer associations. This will be particularly important once the recently adopted Empowering Consumers for the Green Transition Directive becomes applicable.
The ESAs' governance structure should also be improved. Currently, each ESA has a board of supervisors that comprises the 27 heads of the EU Member States' national supervisory authorities, which reduces the effectiveness of the European rules. In 2022, the Commission concluded 'that the governance system of the ESAs, with decisions being taken by the 27 national supervisors, may still give too much prominence to national interests and occasionally produce sub-optimal results'.[55] The ESAs should become more independent from national supervisors. We therefore support earlier proposals from the European Commission to establish a new governance framework with strong powers for independent executive boards. The ESAs should also be equipped with appropriate financial resources.

[54] This section repeats many demands from our response to the consultation on supervisory convergence and the single rulebook: 'Targeted Consultation on the Supervisory Convergence and the Single Rulebook', 2021, https://www.beuc.eu/sites/default/files/publications/beuc-x-2021-054_supervisory_convergence_and_single_rulebook.pdf (accessed 19 April 2024). It also draws on the BEUC report 'Strengthening the Coordinated Enforcement of Consumer Protection Rules: The revision of the Consumer Protection Coordination (CPC) Regulation', 2022, https://www.beuc.eu/position-papers/strengthening-coordinated-enforcement-consumer-protection-rules (accessed 19 April 2024). BEUC will publish a more in-depth position paper on supervision and enforcement in financial services in due time.

[55] European Commission, 'Report from the Commission to the European Parliament and the Council on the operation of the European Supervisory Authorities', 2022, p. 10, https://finance.ec.europa.eu/system/files/2022-05/220523-esas-operations-report_en.pdf (accessed 19 April 2024).

BEUC recommendations

- **ESAs should use supervisory convergence tools, especially the powers to coordinate mystery shopping and peer reviews, systematically to improve supervisory consistency and enforce minimum standards for business conduct across the EU.**
- **National supervisors should be given more far-reaching powers and collaborate systematically with consumer protection agencies and consumer associations.**
- **To make the ESAs more independent from national supervisors, they need a new governance framework with strong powers for independent executive boards and adequate financing.**

4. Other important elements of the regulatory framework to improve sustainable financial services

Sustainable retail finance only works well if embedded into a wider system of sustainable finance. This system comprises aspects and regulations that are not directly related to consumers, but support, or are, indeed, indispensable for, sustainable retail financial services. This section gives an overview of these non-consumer aspects of the sustainable finance system.

4.1. Corporate Sustainability reporting and ESG ratings: the data infrastructure for sustainable financial services

If sustainable finance can be likened to a building one might say that the EU built the roof before the foundations. Those who offer sustainable financial products must first gather and analyse sustainability-related information about the businesses in the real economy or governments that request a loan or whose securities are being considered for inclusion in an investment portfolio or capital markets benchmark. There are several laws that have either been adopted recently or are currently making their way through the legislative process that would have laid the informational and data foundations on which the other floors of the house should have been built.

4.1.1. Corporate Sustainability Reporting

At the very bottom of the sustainable finance edifice is the sustainability-related information provided by businesses in the non-financial sector. If that information is incomplete, unreliable or incomparable, it will be hard to put together in an accurate manner a portfolio for an ESG investment fund, an ESG capital markets index or to develop a reliable ESG rating for these companies. The Corporate Sustainability Reporting Directive (CSRD) and the European Sustainability Reporting Standards (ESRS), which are based on the CSRD, want to change that. These standards cover the entire range of sustainability topics, from climate change and biodiversity to workers' rights. Sustainability reports must now also be audited independently. This should give actors in the financial system the information they need to provide genuinely sustainable financial products to consumers.

However, the ESRS that were adopted in December 2023 are a watered-down version of the original proposals because they leave too much discretion to the reporting companies and have reduced the number of reporting items. This reduces the comprehensiveness, reliability and comparability of sustainability information and does a disservice to consumers. We call on the European Commission and the EU legislators to correct these mistakes in a future review of the CSRD/ESRS. Until then, some of the damage could be undone by swiftly adopting robust sector-specific ESRS. The ESRS adopted in December 2023 apply to companies in any economic sector, but the CSRD also mandates the

Commission to adopt specific sustainability reporting standards for each sector. Unfortunately, the adoption deadline has been extended by two years to June 2026, but the Commission is called upon to 'endeavour' to adopt the standards for up to eight high-impact sectors before that deadline.[56] **We call on the Commission not to delay the sector standards any further and to prioritise them above all other ESRS-related work.**[57]

4.1.2. ESG ratings

ESG rating agencies assess how companies perform regarding environmental, social and governance-related sustainability aspects. Many asset managers rely on them for putting together sustainable investment portfolios. Unfortunately, ESG ratings are currently unreliable and not comparable, which leads to serious quality problems further down the line, i.e. in the investment products offered to retail investors. For example, ratings for the same company from different agencies can differ wildly because they do not measure the same things when they talk about ESG performance, or because different agencies employ different rating methods and draw on different data sources.

In February 2024, the European Parliament and Council agreed on a regulation for ESG rating agencies[58] that sets out rules for their authorisation by competent supervisors, their governance, the avoidance of conflicts of interests as well as transparency requirements concerning rating methods. This law is a step forward, but a missed opportunity for solving the problems that afflict ESG ratings because it only regulates the behaviour of ESG rating agencies, but does not set rules and minimum quality standards for the ratings themselves, which would have made them more reliable and comparable. There is not much that can be done for now, but we hope that product level regulations will be introduced at the next possible opportunity.

4.2. Green bond standard

The European Green Bond Standard Regulation becomes applicable in December 2024. It introduces minimum product and disclosure requirements for green bonds that intend to use the official 'European Green Bond' label. These bonds must allocate no less than 85% of the proceeds from the bond's emission to assets or activities that comply with the EU Taxonomy criteria for environmentally sustainable economic activities. The Regulation also introduces a template for mandatory disclosures about the bond's characteristics. These requirements are good, but unfortunately voluntary because they can be avoided by simply not using the official EU Green Bond designation for a bond that is sold as 'green' or 'sustainable'. Minimum product criteria and transparency requirements should have been mandatory for all green bond issuances to deter greenwashing. Considering that the Regulation was only adopted in 2023 there will not be a review any time soon, which makes this another missed opportunity for putting in place watertight rules for a green financial product.

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[56] European Parliament, 'Deal on delayed reporting standards for some companies', 2024, https://www.europarl.europa.eu/news/en/press-room/20240205IPR17414/deal-on-delayed-reporting-standards-for-some-companies (accessed 19 April 2024).

[57] BEUC has critically supported the project of ESRS development since 2022: 'Factsheet: How to improve corporate reporting', 2022, https://www.beuc.eu/sites/default/files/publications/BEUC-X-2022-127_How_to_improve_corporate_sustainability_reporting%20.pdf; 'Letter to Commissioner McGuinness: Consumers support the draft Sustainability Reporting Standards (ESRS)' 2023; https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/14012-European-sustainability-reporting-standards-ESRS-postponement-of-deadlines-under-the-Accounting-Directive/F3447162_en, 2023; (all accessed 19 April 2024).

[58] Council of the EU, 'Environmental, social and governance (ESG) ratings: Council and Parliament reach agreement', 2024, https://www.consilium.europa.eu/en/press/press-releases/2024/02/05/environmental-social-and-governance-esg-ratings-council-and-parliament-reach-agreement/ (accessed 19 April 2024).

4.3. ESG benchmarks

Capital market benchmarks, or indices, are hugely important for retail investors who put their money into so-called passive funds. These funds do not select the securities to include in their portfolios, they simply replicate the composition of an index, which is why they are also called 'index trackers'. Nowadays, there are ESG indices that are tracked by a growing number of passive ESG investment funds.[59] If an ESG index is bad because the shares or bonds included in it are not very sustainable the corresponding ESG index tracking products are also bad and will mislead retail investors.

In November 2019, the EU legislators ordered the European Commission to present a report on the feasibility of an EU ESG benchmark label to the European Parliament and Council by December 2022 and to consider the option of a draft law that regulates ESG benchmarks (Article 54(5) EU Benchmarks Regulation). However, the Commission never submitted the requested report to the EU institutions, even though the European Securities and Markets Authority (ESMA), strongly supported the introduction of an EU ESG benchmark label that would harmonise the methods of benchmark construction.[60] This is another missed chance to improve the quality of sustainable investment products for retail investors. We need minimum quality and transparency standards for anything that is called an ESG benchmark to avoid greenwashing. **The Commission should comply with its legal duties under the Benchmark Regulation and produce a report that seriously evaluates the option of an ESG benchmark regulation.**

4.4. The role of insurers and banks in fighting climate change

Sustainable retail finance can contribute to the transition to a more sustainable economy, but banks and insurers can contribute directly and more effectively to the transition by modifying the costs of doing (unsustainable) business in the non-financial sector.
The insurance sector in particular plays a gatekeeper role in any modern capitalist economy because nothing moves that is not insured. Insurance fees are among the costs of doing business that it can influence. Insurers should add sustainability performance to their criteria for determining insurance fees so that more harmful businesses pay more. If doing this for all sustainability matters is too difficult at the moment, they should at least do it for climate change because we will soon have good company-level information about greenhouse gas emissions and climate transition plans. Businesses that harm the climate also cause massive risks to the economy, as well as insurers and consumers, so they can be expected to pay higher fees.[61] One of the limiting factors on retail sustainable finance is the scarcity of genuinely sustainable investments in the real economy. If insurers adjusted their fees to take negative sustainability effects into account they would contribute to a shift in the real economy that would enlarge the supply of genuinely sustainable investment opportunities, which, in turn, would allow the financial industry to offer more genuinely sustainable retail products. Insurers are also major investors in companies, and as such they can turn to sustainable investing by either excluding particularly harmful industries or businesses from their investment portfolios or by using their position as shareholders to pressure company managers to become more sustainable.

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59 European Securities and Markets Authority, 'ESMA Market Report: Costs and Performance of EU Retail Investment Products 2023, 2023, https://www.esma.europa.eu/sites/default/files/2023-01/esma50-165-2357-esma_statistical_report_on_costs_and_performance_of_eu_retail_investment_products.pdf (accessed 19 April 2024). Passive ESG funds are a rapidly growing segment of the retail investment market (p. 19).

60 European Securities and Markets Authority, 'ESMA's response to the Commission's consultation on the BMR review', 2022, p. 12f., https://www.esma.europa.eu/sites/default/files/library/esma81-393-502_esma_response_to_the_ec_consultation_on_the_bmr_review_2022.pdf (accessed 19 April 2024).

61 The 'Insure Our Future' campaign tries to draw attention to this. ESG considerations are starting to be integrated into insurance policies and fees, but it is too early to tell whether this is genuinely significant (see e.g. Marsh, 'A snapshot of ESG thinking in the development of the underwriting process', 2022, https://info.marsh.com/l/395202/2022-08-31/cfh9rv/395202/1661955692WiqoJI8y/Insurer_approach_to_ESG.pdf (accessed 19 April 2024)).

Capital requirements for banks should reflect more accurately the financial risks that lending to high-emission businesses entails. Higher capital requirements would make this kind of lending less profitable for banks, unless they charge the borrower a higher rate of interest. Either way, it drives up the cost of climate-harming business and would also improve overall financial stability.

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