

IRSG

INSURANCE AND REINSURANCE STAKEHOLDER GROUP

Advice on product disclosure templates under
the Sustainable Finance Disclosure Regulation

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IRSG Response

Executive summary

The IRSG unanimously strongly supports the EU sustainability objectives and welcome the ESAs work on disclosures for sustainability-related products as a step towards increased transparency in sustainable investing. It is key that this work reflects market reality, is workable across product types and delivers clear and understandable sustainability-related information to customers.

While we fully understand the need for standardisation and comparability to contribute to the environmental transition, some members would encourage the ESAs to consider a more flexible approach to enable a smooth phasing in, allowing for more innovation at this initial phase. Less prescriptive templates and optional use of them could help make the implementation of the Sustainable Finance Disclosure Regulation (SFDR) easier.

*In our opinion, the example provided (together with the draft RTS) **gives insufficient prominence to the role of stewardship** in promoting environmental characteristics and in mitigating sustainability risks and impacts, as well as engaging companies to commit to sustainable practices and the transition to a low-carbon economy. This is important since a key element beyond purely ‘deep green’ investments per se is how investors encourage and engage with companies to follow a ‘pathway to transition’. The template highlights that the **prescriptive definitions being proposed are likely to confuse, and risk misleading, end consumers** of products promoting sustainable characteristics (and so undermining one of the key objectives of the Regulation, which is transparency on sustainability).*

Whilst we acknowledge that some of these definitions are unfortunately set in the Regulation, it would be very difficult for a retail customer, for example, to understand “This financial product promotes environmental or social characteristics, but does not have as its objective a sustainable investment. It might invest partially in assets that have a sustainable objective, for instance, qualified as sustainable according to the EU classification.” A customer is likely to think that they do want to make sustainable investments (in the sense of investments that contribute to a sustainable planet and society, rather than as defined by the Regulation) so may be concerned that they are being told that the product does not have an objective of sustainable investment. The statement then goes on to say that the product may, nonetheless, invest in some sustainable investments, and goes on to show a graph of the percentage of the product that does make those investments.

Generally, we would propose an approach allowing in the limited period room and a possibility for improvements, encourage ESAs allowing for more innovation at this initial phase to work out the final template.

While all IRSG members support easy to understand simplified descriptions and explanations for consumers, the IRSG consumer representatives believe that the current ESAs proposals achieve this objective – and they would select very useful as an answer, while other representatives believe that the ESAs proposals need improvements to avoid being useless. Therefore, the IRSG answered 'neither useful nor useless'.

Survey - introduction

The illustrative mockups relate to disclosure documents for a fictitious exchange traded fund (ETF). Most ETFs are index funds. This means that they usually replicate the index by holding the same securities in the same proportions as a certain stock market index. This product replicates a fictitious index, called TRXI World Fossil Fuel Free Index, which replicates the total market index TRXI World Index, but excludes from it companies that own solid fossil fuel reserves.

The two documents that you will see are mockups of ESG information from the following underlying documents:

- a) **Prospectus of the ETF** – which provides information before buying the product*
- b) **Annual report of the ETF** – which provides information on the product for the last 12 months*

Questions

Q1 How useful is the highly standardised presentation of the information in this format?

- 1. Useless
- 2. Fairly useless
- 3. Neither useless nor useful
- 4. Fairly useful
- 5. Very useful

Please explain:

There are various opinions on the usefulness of the information in the proposed format. Generally standardisation is perceived as useful, but there are some doubts about the templates being able to deliver this outcome.

There was an opinion that, to be comparable, the information disclosed must reach the highest degree of standardisation at cross-sectoral levels and that standardisation concerns not only the

type of information to be included, but also the orderflow and format, or in other words, it must exhibit the same structure. That is why the template is a step in the right direction, yet it can be improved as there are many fairly complex sections (it requires strong attention and can be difficult for less experienced retail investors) and contains repetitions. Once consumers can understand and compare better sustainable products, they will know what to look for. While some IRSG members felt the explanatory notes are very informative and easy to understand, others are strongly opposed to the inclusion of such prescriptive text elements and the complexity of the language used.

At the same time, there are some reservations regarding the usefulness of this template in facilitating comparison across types of products, and even across the same type of products, meaning that intended objective of standardisation and comparability is not achieved.

Furthermore, from an operational viewpoint, some members perceived the format as unnecessarily prescriptive and hard to work with for insurers, who have the need to adequately describe the characteristics of different products, including more complex products such as hybrid products. In this respect, some members presented an opinion that a flexible approach is needed to allow companies to disclose comprehensible information to the average consumers, without overloading them with overly complex sustainability-related information and new documents. Such disclosures need to be balanced with respect to financial information, which is also crucial for investment decision-making.

Finally, the detail requested, and the choice of language is not appropriate to the different sectorial formats where these disclosures need to be implemented (e.g. PEPP-KID and Solvency II disclosures), even less if the ESAs insist on mandatory wording which has already led to significant problems in a cross-sectoral context. In some cases, the templates also duplicate information already provided in other documents, either required by other legislative texts at the EU or national level. A proper mapping can help avoid such duplication.

Some members suggest the ESAs focus on the type of information which is truly needed by customers for informed decision making. Ideally, this information should be driven by materiality thresholds. Also, the approach for the presentation of the disclosures should be contained in sub-notes: more flexible and consumer-centric, fully reflecting consumers' needs to easily access to the information on digital tools rather than being overwhelmed with excessive or overly-complex documents.

A high standardized level of disclosure could be helpful in ensuring consistency and comparability. On the other side, one template applying to all cases could not be feasible, considering products and investment strategy vary significantly as assets, structure and investment outlook. This could result in the disclosure of irrelevant information that will not help consumers, even mislead them.

Q2 More specifically, how useful is the presentation of the information with the use of **icons** as visual aids?

1. Useless
2. Fairly useless
3. Neither useless nor useful
4. Fairly useful
5. Very useful

Please explain:

Icons and visual aids can guide and help the investor to understand complex contents. In addition, the icons and visual images can make the text “lighter” and more intuitive for the investors. They make it easier to understand complex topics or to look up information.

However, some members of the IRSG pointed out that while the use of icons in consumer-facing documents is to be encouraged, the icons in this template are not helpful at all. They take space in already long templates, they complicate their implementation and do not help in navigating within them. As such, there should be no mandatory requirement for the use of such icons.

There was also a welcoming remark on the possibility for providers to adapt the font and colours to match the sectoral consumer information. Such flexibility should be extended to other elements, including the colours and font size of both icons. Other members believed that this should, however, be within set limits to ensure minimum levels of ‘readability’.

Q3 More specifically, how useful is the presentation of the information with the use of **graphs** as visual aids?

1. Useless
2. Fairly useless
3. Neither useless nor useful
4. Fairly useful
5. Very useful

Please explain:

We believe that the graphical representation could help individual investors to easily understand the sustainable features of the product as long as the same format of graphical representation (for example pie or bar chart) is used for the same product category. This would enhance comparability across sustainable products facilitating individual investors to understand the characteristics of the product. Research and extensive testing by the AFM (Dutch supervisor) on infographics for key information documents have confirmed their effectiveness.

Graphs seem to be useful, and with the combination of icons, colour, and text should make it easier on the consumer to understand the document. Some people like to see graphs as a quick explanation, especially in combination of suggestive color (blue – for water, yellow for production solar energy) because some combination could be confusing (black – for water supply for instance). On the one hand, in the sample template we consider them as useful, especially for better recognition of the difference between #1A and #1B. On the other hand, graphical representations duplicate information already provided in the narratives (to avoid information overloading, information in graphs should not be duplicated in tables.), and they risk misleading customers by giving them a false sense of comparability across products that make use of different strategies, methodologies and definitions. Another source of misleading or confusing is when the graph is not plotted to scale – this make difficult to compare different products using the graphs. The differentiation between environmental and social characteristics also does not appear to add value for customers and oversimplifies the classification of activities with both environmental and social characteristics. Since no consumer tests have been conducted on large sample of population, it is difficult to say how consumers will respond to the pre-contractual disclosures with graphs of different types.

Generally, it must be ensured at all times that graphics neither lead to a misleading simplification of the underlying information nor restrict comprehensibility due to excessive complexity.

Q4 More specifically, how useful is the presentation of the information with the use of **explanatory notes**, in the column at the right side of the document, which are presented on a grey background)?

1. Useless
2. Fairly useless
3. Neither useless nor useful

4. Fairly useful
5. Very useful

Please explain:

Explanatory notes are very useful for the individual investors but need to be adapted and remove doubt even for seasoned investors. In their current formulation, they appear to be too complex for an average customer. Therefore, they should be adapted to the type of information to be disclosed in such a way to avoid contributing to the complexity of the templates. Digital access via drawdown menus is also welcomed.

In addition, explanatory notes should remain adaptable to the specific product type. In case the exact wording to be used becomes mandatory, and not just general, they would lose their purpose. This prescriptiveness might lead to unintended rigidities and inaccuracies.

Q5 Are there any presentational aspects that might make it hard to understand the sustainability-aspects of products? For example, with regards the distinction between the sub-categories of investments, this is the difference between #1A and #1B?

- Yes
- No
- Other

Please explain:

Unfortunately, the distinction could not be understood well in a few words. At the same time, the ESA should reconsider the information requirements for the templates to avoid that excessive information will discourage consumers from reading it. This is key in consideration of the fact that:

- These disclosures will add to the already extensive product disclosures under the Solvency II Directive, the IDD, the PRIIPs Regulation and existing national legislation.
- For more sophisticated products, the disclosures will need to be way too extensive (the mockups of the simple index fund alone have six and four pages for the pre-contractual and periodic information respectively)

Following the same rationale, it should be explicitly possible to make use of links to websites with the relevant information as much as possible, including those to the webpage of external service

providers, such as asset managers. It is recommended that a link to the investment provider website be made or reference to KIID/brochure. In this way, you do not overload this document with too much text. The structure of the investment should be backed with graphs. There is a need to improve the way in which the features of the product (ESG objective vs ESG characteristics) and the key information are presented.

Other elements of the template that harm consumer understanding should also be reviewed:

- In the periodic disclosures, the long list with the top 25 investments and their sectorial split should be shortened as it is currently not valuable to customers.
- The coherence of information within the templates should be sought, e.g. between the product type at the beginning (article 8) and subsequent disclosures dedicated to a sustainable objective (associated with article 9 products instead).

One member presents an opinion that the separation between sections on “a description of the environmental or social characteristics promoted” and on “investment strategy” should be eliminated to avoid complicating the template. The separate section on derivatives is also overly-complex. However, there was also an opinion that it should be not eliminated. There is a need to clarify the definitions which at the moment are unclear and misleading for individual investors.

As mentioned in the previous consultation, there is not a clear distinction between “sustainable investment products” in Article 9 and “products that promote environmental, social criteria” in Article 8 of the Disclosure regulation. The information presented in the sub-category does not help the investor to understand the non-financial characteristic of the product. A simplified representation is needed in this regard.

The terminology should be accessible to the average consumer, acronyms should be avoid as much as possible.

Q6 Do you have any other suggestions or comments to improve the presentation of these disclosure documents?

Please explain:

We suggest to closely monitor and continuously improve the sample templates. However, there is a need for a single ESG ratio for a clear presentation of the product's features and comparativeness purpose, to avoid the problem in presenting the EU Taxonomy ratios, as they are not understandable. Eco-labels can also be an efficient instrument to communicate to retail customers the sustainability of financial products, ideally based on disclosed ESG information.

The templates need to avoid information overload and should be clear (in the MiFID sense; i.e. intelligible for the average reader), simple, short and concise, avoiding jargon and comparable. To be clear, simple, short and concise, it must focus only on key elements that can and should guide the financial and non-financial decision making of the average investor. At the moment the templates proposed are too long with information overload for individual investors. However, we agree with the use of graphs and icons to make the document "lighter" and more understandable.

Therefore, we suggest shortening the templates avoiding information overload, including complex and misleading information regarding the sub-categories of investments #1A and #1B.

Some members pointed out the ESAs should allow a more flexible approach and optional use of the template as the SFDR does not dictate the mandatory use of templates. On the contrary, optionality would allow financial market participants to adapt the disclosures to different product types and sectoral legislation. This approach is also consistent with the challenging implementation timeline that financial market participants are facing with the application of the SFDR in March 2021 and not yet finalised Level 2 measures or related templates. Challenges in the implementation of the templates should not impede the sale and promotion of products currently considered having sustainable characteristics or objectives.

There was also an expectation of testing proposed templates with a more complex product than a single fund product (as it is done in the mockups), as significant challenges may arise when applying the draft templates to insurance products involving the insurer's collective pool or with switching mechanisms between fund investment compartments and capital guarantee components. In general, these disclosures should be kept as much as possible need-based. It must be ensured at all times that the average customer can understand the information provided. For example, terms like "ESG rating above 'BBB' and RTT ESG Controversies score great than 4" should be avoided and translated into easy to understand wording.

Cross-referencing with external data sources, the use of links could enhance data reliability. On the other hand, layering could imply risks for consumer protection, augmented by digitalization if, in background, on the screen appear other information that facilitates the marketing of highly speculative products or the greenwashing.

Q7 When the templates are presented via digital media, can you foresee any particular challenges? Can you suggest how these particular challenges could be overcome while retaining the core aspects of the standardised template format?

Please explain:

The use of digital media can be a good opportunity to streamline on-line KIIDs or KIDs. It would be useful to have different layers disclosing different levels of details. In this way, the investor will have a more intuitive and shorter document (at first glance) with easier access to information.

We do not think there should be a difference in text between digital or e-mail etc. This can only confuse the consumer. A consumer should access this information both on-line and also by request on e-mail. The accessibility of the templates via digital tools is suboptimal due to their length, the use of tables with multiple columns and icons. The structure of the templates needs to be changed to ensure that consumers easily access most relevant information regardless of the device or operating system or technology they are using to access the document. For MOPs qualifying under article 8 or article 9 of the SFDR hundreds of pages would need to be presented to clients, this needs to be streamlined as consumers cannot be expected to synthesise so much information.

Finally, we believe more flexibility is needed in terms of means of delivery to customers, e. g.—regular mail, e-mail, website, etc.

BACKGROUND

The European Supervisory Authorities (ESAs) welcome comments on this survey setting out **the details of the presentation** of the information to be disclosed pursuant to Article 8(3), Article 9(5) and Article 11(4) of the Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services (SFDR). This information concerns pre-contractual and periodic disclosures to be included in existing disclosures provided for under EU sectoral legislation and provided by, for example, AIFMs, UCITS management companies, insurance undertakings, IORPs or PEPP providers. The ESAs propose to standardise the disclosures by requiring the use of specific templates, recognising the need for standardisation of

disclosures to promote comparability of different financial products in different Member States with respect to ESG information, in line with Recital 9 of the SFDR.

The colour of the font and of the template's background, as well as type of font to be used are not prescribed in the templates. These should be adapted by the financial market participants to fit the formatting of the underlying document to which the templates are integrated (prospectus, annual report, pre-enrolment disclosure for prospective pension scheme members, etc).

The final content of the templates is subject to the outcome of concurrent consumer testing exercise and the final report of the ESAs on the draft RTS under SFDR.

The consultation package includes:

- Preliminary, **illustrative mockups** of pre-contractual and periodic disclosure templates of products promoting Environmental and/or Social (E/S) characteristics (under Article 8 and Article 11 of the SFDR). The templates for the disclosure of products with a sustainable investment objective (Article 9) are very similar to those for the products promoting E/S characteristics and have not been included in the on-line survey. N.B. These mockups are purely illustrative for the purposes of gathering feedback on the presentation of information.
- An on-line survey