Please note that this document contains only sections and questions of relevance to FERMA. For the full consultation document please visit the website of the European Commission.

FERMA's response to the European Commission public consultation on its renewed sustainable finance strategy.

15 July 2020

1.1 Company reporting and transparency

Question 14: In your opinion, should the EU take action to support the development of a common, publicly accessible, free-of-cost environmental data space for companies' ESG information, including data reported under the NFRD and other relevant ESG data?

- Yes/No/Do not know.
- If yes, please explain how it should be structured and what type of ESG information should feature therein. [BOX, 2000 characters]

FERMA supports the digitalisation of non-financial information in a centralised European repository to facilitate its availability and comparability. To be actionable, this data should be delivered in an accessible and interactive format. The database should therefore be arranged by industry with the possibility to sort companies on different dimensions, such as by country or other indicators.

Data should be collected, reported and classified in three main ESG sections (corresponding to the three topic areas, namely Environmental, Social and Governance). An additional section titled "Other" will give companies the opportunity to provide any further non-financial information they consider relevant.

Each section should be structured following the requirements of the Non-Financial Reporting Directive (NFRD). Companies should indicate the applicability of each requirement based on the "comply or explain" principle. This principle permits companies to either comply with the NFRD provisions or explain why they have not complied, that is, why they have deviated from the provisions of the directive. Applicability should be determined through a risk and opportunity materiality assessment, following the process described by FERMA in its response to the recent public consultation on the review of the NFRD (see link below). This process involves the construction of a risk and opportunity-based Materiality Matrix, focused on a few clear priorities that may distinguish information that is important and necessary to disclose from that which could be considered secondary and optional. This Matrix uses Enterprise Risk Management (ERM) to assess the relevance of each risk and opportunity in order to select key sustainability topics. It will increase the quality of non-financial information for both companies and stakeholders, while ensuring the scope remains limited to only the most relevant aspects. For more information about this process, and to read FERMA's overall position on the NFRD, please visit https://www.ferma.eu/advocacy/ferma-calls-for-a-clarified-and-targeted-non-financial-reporting-standard-based-on-erm/.

1.3. Sustainability research and ratings

Question 17: Do you have concerns on the level of concentration in the market for ESG ratings and data?

- Please express your view by using a scale of 1 (not concerned at all) to 5 (very concerned). 4
- If necessary, please explain the reasons for your answer. [BOX, 2000 characters] Although there are many ESG assessment tools available to help gauge a company's sustainability level, few of them are well-recognised internationally. This leads to a concentration in the market for those few that are well-recognised, namely the Dow Jones Sustainability Index, Carbon Disclosure Project (CDP) and Ecovadis (particularly for the automotive industry). Companies are subsequently more interested in obtaining a high score/rating from one of the above than from other providers. Therefore, in addition to the Commission study that will explore possible measures to manage conflicts of interest and enhance transparency in the market for sustainability tools, there may be a further need to define the minimum requirements (i.e. standards) with which any tool should comply to ensure comparability of information independently of the tool used. Such criteria will help to avoid the market concentration described above and the unfair focus on a few well-recognised providers to the detriment of others.

Question 18: How would you rate the comparability, quality and reliability of ESG **data** from sustainability providers currently available in the market?

- Please express your view by using a scale of 1 (very poor) to 5 (very good). 4
- If necessary, please explain the reasons for your answer. [BOX, 2000 characters] Sustainability providers request that respondents complete a standard questionnaire, with the option to provide supporting documentation if desired. This standardisation greatly improves the quality and reliability of ESG data as it makes it possible to compare results across the EU.

Question 20: How would you assess the quality and relevance of ESG **ratings** for your investment decisions, both ratings of individual Environmental, Social or Governance factors and aggregated ones?

- Individual: Please express your view by using a scale of 1 (very poor quality and relevance) to 5 (very good). 4
- Aggregated: Please express your view by using a scale of 1 (very poor quality and relevance) to 5 (very good). 3
- If necessary, please explain the reasons for your answer. [BOX, 2000 characters] – The individual rating is particularly well-suited to address concrete investment decisions on each ESG factor as it is designed to indicate best performance. The aggregated rating is slightly less relevant as it is, by nature, less targeted. However, since the aggregated rating is used to compare ESG factors across companies, it is more strategic for a company to obtain a high aggregated than individual rating as it will have more effect on a company's image and reputation.

Question 21: In your opinion, should the EU take action in this area?

- Yes/No/Do not know.
- If yes, please explain why and what kind of action you consider would address the identified problems. In particular, do you think the EU should consider regulatory intervention? [BOX, 2000 characters]

  In order to incentivise companies' investment decisions in ESG factors, the European Commission should define the acceptable rate/thresholds for ESG, similar to an EU-level Sustainability Risk Appetite. This means that for each ESG factor, the Commission should define the minimum acceptable rating that companies need to achieve (based on one or a combination of ratings provided in the market, for example). Any result that is below the acceptable rating, meaning that the company risks non-alignment with the EU's sustainability strategies (such as carbon neutrality), will incentivise a company to define clear action plans to achieve the target.

  Although no penalties or fines should be levied, it is important that each judgment is well justified by the European Commission, taking into account particular interdependencies within certain industries that may mean compliance with one ESG factor necessitates non-compliance with another.

1.6. Corporate governance, long-termism and investor engagement

Question 40: In your view, should there be a mandatory share of variable remuneration linked to non-financial performance for corporates and financial institutions?

- Yes/No/Do not know.
- If yes, please indicate what share. [box 2000 characters] – A mandatory share should ensure that non-financial performance is included in directors' variable

remuneration. It is important that the European Commission defines clear guidelines or instructions to help companies select the specific non-financial performance to be taken into account. To be compliant with the Shareholder Rights Directive (SRD II), it is most important that these targets are easily monitored and verified. With regard to the following question, FERMA believes that a defined set of EU companies should be required to include carbon emission reductions in their lists of ESG factors affecting directors' variable remuneration providing that a carbon emission strategy is clearly defined at company level, implying a commitment to specific investments and actions. Thorough non-financial performance reporting can be achieved only if there is commitment from the company on each specific topic.

Question 41: Do you think that a defined set of EU companies should be required to include carbon emission reductions, where applicable, in their lists of ESG factors affecting directors' variable remuneration?

- Yes/No/Do not know.

3.1. Identifying exposures to harmful activities and assets and disincentivising environmentally harmful investments

Question 82: In particular, do you think that existing actions need to be complemented by the development of a taxonomy for economic activities that are most exposed to the transition due to their current negative environmental impacts (the so-called "brown taxonomy") at EU level, in line with the review clause of the political agreement on the Taxonomy Regulation?

- Yes/No/Do not know.
- If no, please explain why you disagree [BOX max. 2000 characters]
- If yes, what would be the purpose of such a brown taxonomy? (select all that apply)
  - Help supervisors to identify and manage climate and environmental risks.
  - Create new prudential tools, such as for exposures to carbon-intensive industries.
  - Make it easier for investors and financial institutions to voluntarily lower their exposure to these activities.
  - Identify and stop environmentally harmful subsidies.
  - Other, please specify. [box max. 2000 characters]

Question 83: Beyond a sustainable and a brown taxonomy, do you see the need for a taxonomy which would cover all other economic activities that lie in between the two ends of the spectrum, and which may have a more limited negative or positive impact, in line with the review clause of the political agreement on the Taxonomy Regulation?

- Yes/No/Do not know.
- If yes, what should be the purpose of such a taxonomy? Please specify. [BOX max. 2000 characters]

Question 87: Beyond prudential regulation, do you consider that the EU should take further action to mobilise insurance companies to finance the transition and manage climate and environmental risks?

- Yes/No/Do not know.
- If yes, please specify which actions would be relevant. [BOX max. 2000 characters] – The EU should help the insurance market clarify, by industry, the perimeter of climate and environmental risks, and their related effects; the current scope is too broad for the insurance market to manage without additional support. Additionally, the EU should consider new cooperative partnerships with insurance companies and other industry representatives in order to incentivise the accumulation of reserves needed to response effectively to a range of systemic risks, including climate change and environmental degradation. To that end, FERMA is currently working to develop a Resilience Framework for Catastrophic Risks (RFCR) that will create a multi-layered and graduated public-private partnership to encourage the prudential assessment and identification of risks needed to access public funds, while enhancing coordination across the EU. Should the Commission wish to learn more about this initiative, please refer to the position paper included with this consultation, or contact FERMA CEO, Typhaine Beaupérin, directly at typhaine.beauperin@ferma.eu.

3.5. Improving resilience to adverse climate and environmental impacts

Question 99: In your opinion, should the European Commission take action to enhance the availability, usability and comparability of climate-related loss and physical risk data across the EU?

- Yes/No/Do not know.
- If yes, please select all that apply:
  - Loss data, please explain why [BOX max. 2000 characters]
  - Physical risk data, please explain why [BOX max. 2000 characters]

    More reliable and accessible risk data will place public and private decision makers in a better position to apply risk management practices that will help them make more informed decisions. If applied correctly, these practices should increase the resilience of public infrastructures, services and commerce, and reduce the financial impact of climate-related risks on the economy at large.

Ensuring wider access to climate-related data also reduces the risk of asymmetric information between insureds and insurers, in which there is a significant risk of adverse selection. This creates, in turn, a solid foundation for fairer dialogue between corporate insurance buyers and the insurance market.

Ultimately, enhancing the availability, usability and comparability of climate-related loss and physical risk data across the EU would support economic growth, as it would reduce the financial impact of climate-related risks on businesses in terms of physical damage and business interruption, while keeping insurance costs at a sustainable level.

To be actionable, data from both public and private sources should be delivered in an accessible and interactive format. This is already the case in some countries, such as France (French Géorisques portal), Slovenia (Geoportal ARSO), the United Kingdom (UK Flood map), as well as in the Global Wind Atlas (used for the energy sector) and the European Climate Database (ECAD). To allow all economic actors to develop adaptation strategies, climate-related risk data should ideally be aggregated on joint platforms and kept up to date by their operators.

Private organisations and Member States should also be encouraged to share data publicly at EU level for all types of climate-related risks (storms, floods, droughts, wildfires, etc.). Risk Managers and Insurers should be closely involved and incentivised by public authorities to actively provide and update EU-wide weather-related risk data.

Question 100: Is there a role for the EU to promote more equal access to climate-related financial risk management mechanisms for businesses and citizens across the EU?

- Yes/No/Do not know.
- If yes, please indicate the degree to which you believe the following actions could be helpful, using a scale of 1 (not helpful at all) to 5 (very helpful) and substantiate your reasoning:
  - Financial support to the development of more accurate climate physical risk models. [BOX max. 2000 characters] 4 – to facilitate the estimate of financial impacts expected from climate physical risks
  - Raise awareness about climate physical risk. [BOX max. 2000 characters]. 5 – the potential effects of climate physical risk are not yet well understood and known by companies who focus more on near-term profits than strategic fundamentals. Following the recommendations of the High-Level Expert Group (HLEG) on sustainable finance, greater awareness of long-term systemic threats, including ESG risks, would be very helpful to discourage short-termism.
  - Promote ex-ante “build back better” requirements to improve future resilience of the affected regions and or/sectors after a natural catastrophe. [BOX max. 2000

characters].

- Facilitate public-private partnerships to expand affordable and comprehensive insurance coverage. [BOX max. 2000 characters]. 5 – In some cases, it is beyond the capital of the private insurance market to provide material capacity for the transfer of systemic risks, such as climate change, due to their large-scale effects. Public-private partnerships, such as the RFCR described in response to question 87, may help to address this issue, leading to a favourable common insurance approach while also helping to incentivise the accumulation of reserves needed to respond effectively to a range of systemic risks that are currently addressed on an ad hoc basis.
- Reform EU post-disaster financial support. [BOX max. 2000 characters].
- Support the development of alternative financial products (e.g. catastrophe bonds) offering protection/hedging against financial losses stemming from climate- or environment-related events. [BOX max. 2000 characters] 4 – Such financial products could help substitute or compensate existing insurance coverage
- Advise Member States on their national natural disaster insurance and post disaster compensation and reconstruction frameworks. [BOX max. 2000 characters].
- Regulate by setting minimum performance features for national climate-related disaster financial management schemes. [BOX max. 2000 characters].
- Create a European climate-related disaster risk transfer mechanism. [BOX max. 2000 characters]. 5 – As mentioned previously, FERMA is currently working to develop the RFCR with the aim to help governments and Member States respond better to systemic risks and their associated market failures. Specifically, FERMA envisages a multi-layered approach that starts with the identification of risks through enterprise-level risk management (ERM). These risks are then transferred to the private insurance and reinsurance markets, supported by national Member State pool guarantees, and coordinated by the European Union. The promotion of this mechanism at EU level will facilitate its adoption across Member States, increasing the capacity of European insurance markets and enhancing the resilience of EU businesses overall.
- Other, please specify. [BOX max. 2000 characters].

Question 101: Specifically with regards to the insurability of climate-related risks, do you see a role for the EU in this area?

- Yes/No/Do not know.
- If yes, which actions you would consider to be useful? In particular, is there scope for EU action to improve the offer of products and services for climate-related disaster risk reduction, enhance insurers’ potential to promote increased resilience of their

policyholders beyond a mere compensatory role?[1]

- Yes/No/Do not know.
- If yes, please explain which actions and the expected impact (high, medium, low). [BOX max. 2000 characters] The EU should be part of a risk transfer solution for systemic risks, including inter alia climate-related disaster risk, because the currently existing national insurance pools are:
  - Only available in a minority of Member States
  - Even if available, triggers, coverage and funding are not consistent.
  - As they are national, these pools do not cover pan-European losses. Given the interdependency of European economies, this makes national pools an insufficient solution, particularly for losses caused by Business Interruption.

  The uneven landscape across Member States with regards to the current availability of insurance pools points to a weakness in insurance markets that must be addressed if the EU is to increase the resilience of the Internal Market. Therefore, any EU action in this area will likely result in a high expected impact.

  If no, please explain. [BOX max. 2000 characters]

Question 102: In your view, should investors and / or credit institutions, when they provide financing, be required to carry out an assessment of the potential long-term environmental and climate risks on the project, economic activity, or other assets?

- Yes / No / Do not know.
- If yes, what action should the EU take? Please list a maximum of three actions. [BOX max. 2000 characters] – As mentioned in the previous sections, the EU should help companies clarify the perimeter of climate and environmental risks and related impacts on business, facilitating the internal assessment and consequent dialogue with investors and credit institutions.

[1] For instance, EIOPA in its opinion on sustainability on Solvency II talks about "impact underwriting which includes the development of new insurance products, adjustments in the design and pricing of the products and the engagement with public authorities without disregard for actuarial risk-based principles of risk selection and pricing".

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