

Opinion of the European Economic and Social Committee on 'Socially responsible financial products' (own-initiative opinion)

(2011/C 21/06)

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On 1 October 2009, the European Economic and Social Committee decided to draw up an own-initiative opinion, under Rule 29(2) of its Rules of Procedure, on

Socially responsible financial products.

The Section for Economic and Monetary Union and Economic and Social Cohesion, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 4 May 2010.

At its 463rd plenary session, held on 26 and 27 May 2010 (meeting of 26 May), the European Economic and Social Committee adopted the following opinion by 129 votes to three with two abstentions.

1. Conclusions and recommendations

1.1 The term 'Socially responsible financial products' could be interpreted to mean all the products and services available from the banking, insurance and investment management sectors. However this opinion, for the most part, deals with socially responsible investment (SRI) provided by collective investment funds available to both institutional investors and the general public. By definition, collective investment funds make investments. For the fund to qualify as socially responsible, it must carefully select its investments against appropriate criteria. Most funds invest in the shares of companies. The central issue for most funds is their ability to identify companies which meet the necessary ESG (Ethical, Social, Governance) criteria. In mature SRI environments there are a wide range of organisations which determine the extent to which individual companies meet ESG criteria.

1.2 Many advisory bodies exist, providing technical assistance to SRI. International stock indices such as the Dow Jones Sustainability DJSI Index or the FTSE4Good provide relevant information for SRI funds to be established and operated, on either a general or selective basis. For example, some funds may concentrate on well established companies meeting excellent ethical and governance standards. Others might have a green or ecological agenda. All of these variations are provided for.

1.3 In the post crisis environment, it is necessary to channel investment towards companies with social and ethical values in order to win back the public's confidence in the financial markets. We can definitely say that it will not be 'business as usual' after this crisis.

1.4 With the benefit of hindsight we can see that the performance of many financial institutions in recent years has fallen far short of the social and governance standards expected of such leading businesses. The EESC therefore calls for the

responsibility programmes of financial institutions to address Europe's social and governance expectations in the 21st century.

1.5 The results of Socially Responsible Investment (SRI) point to the positive link between the social and financial ratings of institutions offering socially responsible investment funds. Moreover, profitability is no lower with SRI than with traditional investment, nor is the risk any greater.

1.6 Collective investment undertakings and institutions for occupational retirement provision are an important channel for steering savings into productive investment. Nevertheless, more attention will have to be given to advice on investments, improving management methods and the human relations and social responsibility component that is apparent in communication.

1.7 The contribution of professionals working for financial institutions to Socially Responsible Investment must take account of the following aspects: long-term vision, consideration of the general interest, reliability and analytical rigour.

1.8 The EESC calls on the Commission and the Member States to encourage the development of SRI in order to facilitate the 'standardisation' and consolidation of the current management systems for these products promoting transparent information, comparability in the analysis of investors, technical training and the exchange of best practices. There is some evidence that financial markets react positively to the introduction of standardisation systems and the awarding of certification by official bodies.

1.9 One positive effect of SRI filtering, whether by regulation or by professional advisors, is the possibility of certain securities being excluded from investment portfolios, which will prompt companies to improve their ESG performance.

1.10 The EESC advocates launching specific finance-related promotional and educational initiatives: publications, training or setting up specialised websites and teaching financial subjects in schools and colleges.

1.11 One of the aims of financial education programmes is to encourage households to be responsible, prudent and long-term investors, in line with their risk profile, their assets and their personal objectives.

1.12 Socio-demographic developments call for changes in cultural and business approaches to long-term investment. The EESC feels that public bodies should put their weight behind moves to encourage investments in socially responsible funds through the creation of appropriate tax and financial regulations as well as public procurement itself.

1.13 Public administrations actually play an important role in encouraging both responsible investment demand (individual or institutional investors) and supply (management and marketing companies). Public administrations themselves can stimulate the market by managing investments by sovereign wealth or reserve funds. As well as serving as an example, their own behaviour is a major catalyst with a powerful influence in leading the way.

1.14 Issuers and companies, for their part, can mobilise the investment community by persuading them that their sustainability policies are indicative of their management quality when it comes to transparency and the inclusion of these criteria in their investment strategy.

2. The social responsibility of financial institutions

2.1 The so-called 'socially responsible company' in the management context creates opportunities for financial institutions that can respond to what society expects of them.

2.2 With the publication of the European Commission's Green Paper on Promoting a European Framework for Corporate Social Responsibility⁽¹⁾ and subsequently the OECD document on Corporate Social Responsibility⁽²⁾ the socio-economic model of a company assuming responsibility vis-à-vis the stakeholders has taken hold⁽³⁾.

2.3 In the realm of financial institutions, the founding principles of the savings banks⁽⁴⁾ confirm these bodies, along with credit cooperatives and social welfare mutual organisations, as

the forerunners of today's corporate social responsibility (CSR). Their social dimension as an identifying feature⁽⁵⁾ gives them specific objectives closely related to the philosophy of the Social Economy, a social and economic force gaining pace throughout the world⁽⁶⁾, one reflection of this commitment being the inclusion of the disabled.

2.4 The current financial crisis originated in the banking industry where the excessive risks taken by the bankers were compounded by the failure of banking supervision. From this there emerged financial products (secured loans for housing and consumer credit, derivatives and structured products) and moral hazards in the banks' marketing process. In this respect, the role played by credit rating agencies – marked by clear conflicts of interest – was crucial in intensifying the depth of the crisis, together with the recognised supervisory shortcomings.

2.5 The financial institutions' main responsibility is now to prudently and rigorously manage their business while granting funds for financing projects in the productive economy and household consumption.

2.6 In the current financial crisis, the banks must not break with their commitment to society. Moreover, the crisis itself has demonstrated a measure of corporate irresponsibility and has highlighted the need for more and better CSR. CSR is a question of identity, commitment and corporate strategy.

2.7 For all these reasons, the EESC is committed to defining strategic lines of action in the financial sector to drive the growth of SRI, promote appropriate fiscal measures, introduce systems for standardising products, enhance protection for investors, introduce good banking practices and strengthen the European market with responsible and relevant financial services.

3. Socially responsible financial products

3.1 Definition and scope of the opinion

3.1.1 This covers **savings products** (current accounts, high interest accounts, savings deposits, structured deposits), **investment products** (collective investment undertakings: mutual funds and unit trusts; pensions and insurance, pension funds and plans; retirement plans, financial or unit linked life assurance, thematic funds), **credit finance instruments and financial support mechanisms** (micro-credits, revolving funds, mutual guarantee funds and risk capital), which include built-in **environmental, social and good governance criteria** without, under any circumstances, overlooking the necessary goals of risk and financial profitability.

⁽¹⁾ COM(2001) 366 final. See also the Commission Communication on *Implementing the partnership for growth and jobs: Making Europe a pole of excellence on corporate social responsibility*, COM(2006) 136 final.

⁽²⁾ *Corporate Social Responsibility: Partners for Progress*, OECD, Paris 2001.

⁽³⁾ See the EESC Opinion on the *Ethical and social dimension of the European financial institutions*, OJ C 100, 30.4.2009, p. 84.

⁽⁴⁾ Included in document 143/90 of the European Savings Bank Group.

⁽⁵⁾ E. Castelló (2005): *El liderazgo social de las Cajas de Ahorro* (The social leadership of the Savings Banks), FUNCAS Ediciones.

⁽⁶⁾ García, J. L. (2009): *Las cuentas de la economía social: magnitudes y financiación del tercer sector en España, 2005* ('Accounts in the social economy: scale and financing of the tertiary sector in Spain, 2005'), Civitas Ediciones.

See the European Parliament Resolution of 19.2.2009 on the social economy, drawn up by the rapporteur, Patricia Toia.

3.1.2 This opinion focuses on **investment products**, either via the retail market or the institutional market. Broadly speaking, it involves investing in those organisations that behave better and encourage sustainable development. They therefore claim to be an effective instrument for helping with society's global development, encouraging companies to behave in a manner appropriate to investors' interests.

3.1.3 However, there should be no confusion between ethical investment funds and mutual investment funds. The latter simply give a percentage of their profits to social entities, but are not obliged to meet ethical criteria when selecting their investments. Nevertheless, mutual investment and ISR can be included in the same fund.

3.2 Background and developments

3.2.1 The origins of socially responsible investment (SRI) are linked to moral principles. This phenomenon has been gathering pace since the 1980s, driven on by globalisation, greater ecological and social awareness and the development of new information and communication technologies.

3.2.2 SRI emerged in the Anglo-Saxon world⁽⁷⁾. In Europe⁽⁸⁾, some markets display large volumes of growth such as the United Kingdom, the Netherlands, Norway, France, Sweden and Belgium and, to a lesser extent, Italy, Spain and Germany.

3.3 Conceptual details

3.3.1 SRI funds invest in companies. Traditional ethical investment had an essentially moral, ideological or social basis, whilst it now tries to include economic, environmental, social and governance aspects of company performance, in an integrated manner and with a long-term view.

3.3.2 Social responsibility criteria (filters) are applied to investments by excluding specific investments and choosing those that behave better. In this respect, the challenge for SRI is to influence future corporate strategy and match investors' values with those of the investment target.

3.3.3 Advisors use as many as sixty criteria. Some of the most frequently used criteria are listed in the following table⁽⁹⁾.

⁽⁷⁾ Eurosif (2008). The volume of assets in the United States stood at EUR 1 917 billion in 2007.

⁽⁸⁾ Eurosif (2008). SRI assets in Europe totalled EUR 2 665 billion in 2007.

⁽⁹⁾ Muñoz *et al* (2004): *The social responsibility performance of ethical and solidarity funds: An approach to the case of Spain*. Business Ethics. A European Review. Vol 13, number 2/3 April, July.

Negative criteria	Positive criteria
Armaments	Equal opportunities
Experiments on animals	Recycling
Third World exploitation	Saving energy and natural resources
Pollution	Data transparency
Genetic manipulation	Support for training and education
Pornography, tobacco and alcohol	Commitment of solidarity with society
Damage to the environment	Regulation and standardisation of products

3.3.3.1 This list does not assume that the companies having negative attributes are actually irresponsible in their management. On the contrary, they may have the highest ethical standards in the way they do business, even though some investors may find a particular sector, e.g. armaments, morally reprehensible.

3.3.4 The sustainability criteria used in SRI must be understood in a dynamic sense, enabling new and important CSR aspects to be taken on board. In connection with equal opportunities, for example, value-based criteria concerning disabled people should be included, such as indicators on employment integration or the accessibility of workplaces, commercial premises, products and services.

3.3.5 In order to draw up comparative data on how SRI has developed throughout the world, the market segmentation strategy creates a distinction between the institutional market (essentially institutions for occupational retirement provision) and the retail market (which is still limited to investment funds).

3.4 New institutions

3.4.1 The institutions operating on the financial market have created mechanisms to include sustainability in their management practices. Both the so-called traditional banks and the ethical banking sector⁽¹⁰⁾ talk with their stakeholders and this can be carried out in meetings or via exchanges on electronic platforms.

⁽¹⁰⁾ The term 'ethical' is a generally accepted name which does not exclude others such as 'civic', 'alternative' or 'social'. See INVERCO (Ethics Committee) (1999).

3.4.2 The development of SRI has led to the creation of new institutions or the adaptation of traditional institutions involved in drawing up and distributing international stock indices (for example, the Dow Jones Sustainability DJSI Index or the FTSE4Good), creating and marketing data bases, sustainability analysis and SRI advice agencies, etc.

3.4.3 Various factors have helped promote the development of the UN's 'Principles for Responsible Investment' (PRI) including the European Commission's active role, the setting up of the Social Investment Forum (SIF) in the United States, or the European Social Investment Forum (Eurosif) in Europe contribute to the dialogue with stakeholders⁽¹¹⁾.

3.5 Portfolio management

3.5.1 Socio-economic modelling combines social profitability measures with conventional financial models, replacing the profitability-risk combination. Thus socially responsible investment uses social, environmental and good governance criteria in addition to the strictly financial as a basis for its objectives when selecting investments.

3.5.2 In the last few years the need to build an ethical framework into the financial sector, resulting in the so-called sustainable or social finance, has been recognised. This trend ties in with developments in behavioural finance theory and broadens analysis of the economic and psychological behaviour of the players to include social and environmental attitudes⁽¹²⁾.

3.5.3 'Sustainability analysis agencies'⁽¹³⁾ have done the most to develop methods for assessing and rating companies on their socially responsible behaviour using a range of appraisal methods. In practice, the results from various studies in this area have shown that socially responsible investments do not mean investors lose out from an economic profitability point of view in the medium and long-term.

3.6 Regulation and standardisation of products

3.6.1 Introducing and establishing socially responsible products (for investment, savings or credit purposes) calls for a prior and absolutely clear definition of the requirements they need to fulfil, guaranteeing that the principles of social responsibility together with the rules governing monitoring, continual assessment and transparency can be applied.

3.6.2 The Spanish Association for Standardisation and Certification (AENOR)⁽¹⁴⁾ is revising a standard for socially responsible financial products (UNE 165001: 2002 EX, Ethical financial instruments), in order to set out the general requirements for guiding institutions wishing to create or market such products and to provide maximum transparency and information on these ethical criteria for users.

3.6.3 In recent years, self-regulation criteria⁽¹⁵⁾ have been developed for this sector in many EU countries, often at the instigation of government supervisory bodies, to allow registration of the increasing number of new investment funds classified as ethical. Auditors and professional advisors provide a further check and balance.

3.6.4 Attention is also drawn to the initiative to encourage transparency in the use of self-regulation criteria, which is being promoted by Eurosif and various SIFs of the Member States. This gives the consumer information on the criteria used and their application, without prejudging the merits or social responsibility of the products.

3.6.5 The initiative to promote comparability of SRI reports drawn up by financial institutions is intended to create a kind of standardised document model which meets the information needs of investors in different EU countries.

4. Consumer protection

4.1 The financial crisis has caused consumers to lose confidence in financial service providers. Because the sector's morality has been called into question, financial institutions have the opportunity to encourage measures for the establishment and consolidation of ethical financial products.

4.2 Improving customer information

4.2.1 One of the effects of the financial crisis has been the growing concern on the part of regulating bodies for savers and investors. This attitude has been strengthened through arbitration committees, information leaflets and manuals, surveillance of advertising⁽¹⁶⁾ (which has to be clear, impartial and not misleading) for all financial products; the introduction of 'complaints services' or of a customer watchdog (Ombudsman).

⁽¹⁴⁾ AENOR (2008): *Ética. Sistema de gestión de la responsabilidad social de las empresas* (Ethics. Corporate social responsibility management system).

⁽¹⁵⁾ The committees supervising institutions for occupational retirement provision explain whether or not they are using social responsibility criteria in their investment decisions.

⁽¹⁶⁾ See EESC opinion on the Proposal for a Directive of the European Parliament and of the Council amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, COM(2009) 491 final, CESE 257/2010.

⁽¹¹⁾ See EESC opinion, on the *Impact of investment funds on industrial change*, OJ C 128, 18.5.2010, p.56).

⁽¹²⁾ The pioneering work of Amartya Sen is relevant in this respect (1970): *Collective choice and social welfare*, Holden-Day.

⁽¹³⁾ They offer investors a consultation option and act as a supervisory body.

4.2.2 In practice, however, banks do not always provide customers with sufficient information according to their needs. A recent European Commission study⁽¹⁷⁾ has criticised European banks in many countries for irregularities, such as a lack of transparency and high rates of bank account fees and the difficulty customers have in comparing bank offers and thus in choosing the most advantageous.

4.2.3 Transparency vis-à-vis clients calls for clear, precise, understandable and comparable information. In practical terms, socially responsible financial products must at least include the definition of the SRI applied, the practical criteria used (SRI filter), the membership of the SRI Committee⁽¹⁸⁾, the management and deposit fees etc, as well as the periodical publication of independent reports on compliance with the social responsibility philosophy of the product.

4.2.4 Securing information through the customer care service helps with the ongoing improvement (a key factor in the quality of service) and responsible provision of the 'after-sales services' covering the product's life-cycle, or until the customer severs his links with the product.

4.3 Promoting financial education

4.3.1 Financial education is one of the responsibilities that should be addressed by cooperation between the public and private sectors to meet the challenge that an ever more complicated financial environment presents. Nevertheless, this education should be undertaken free from the marketing interests of specific financial products.

4.3.2 A range of initiatives from the supervisory authorities and banks entitled 'Financial education plans' have been put forward to broaden people's knowledge of finance and specifically to prevent household over-indebtedness and help them to choose products appropriate to their risk profile and financial situation. The financial education policies undertaken are helping to create confidence in the financial system.

4.3.3 Its importance was recognised by the European Union in both the Commission Communication on Financial Education⁽¹⁹⁾ and the financial conclusions of the ECOFIN Council held on 14 May 2008⁽²⁰⁾.

⁽¹⁷⁾ Data collection for prices of current accounts provided to consumers, European Commission, 2009, http://ec.europa.eu/consumers/strategy/docs/prices_current_accounts_report_en.pdf

⁽¹⁸⁾ Collegiate body of experts that helps the financial or management entity or the supervisory body for the product to ensure that the ethical filter is properly applied and to check the information to be provided. Each financial product should have its own Committee, although this is not always the case.

⁽¹⁹⁾ COM(2007) 808 final.

⁽²⁰⁾ Council Press Release 8850/08 (presse 113), p. 14.

4.3.4 Encouraging SRI research and training market operators allows financial institutions to adopt 'best practices' in their sustainability policies. Educational material and codes of conduct are good tools for developing training.

4.4 Advice from the financial services

4.4.1 The European MIFI Directive⁽²¹⁾ requires financial institutions to step up investor protection and offer their customers products suited to their various investment profiles. Moreover, it calls for a clear demarcation between advice and marketing and for financial intermediaries to have a detailed knowledge of the products they are selling. Thus as part of the suitability assessment, the customer should be asked whether they agree with SRI policies when offering or allocating them (portfolio management) the most suitable SRI products.

4.4.2 In particular, socially responsible financial products must include internal supervisory mechanisms that identify investment risks and check for conflicts of interest, reporting as appropriate to the SRI Committee (which must be made up of a majority of external experts to guarantee the objectivity of their observations).

5. Prospects for socially responsible investments

5.1 Responsible investment can emerge strengthened from a crisis such as we are experiencing if investors can distinguish between companies opting for corporate social responsibility in the long term and those using it merely as a marketing tool.

5.2 Institutions for occupational retirement provision promise to offer the greatest scope for growth in responsible investment. According to Jáuregui⁽²²⁾, in Spain, the possible launching on the market of 10 % of the Social Security Reserve Fund with sustainable criteria⁽²³⁾ would encourage the development of a social responsibility culture.

5.3 An example of good practice to mobilise the business community and public authorities that is worth mentioning is the *Medal of Social Solidarity* organised by one of the largest Polish businessmen's organisations – the Business Centre Club. This is a special award honouring individuals and CEOs for promoting, inter alia, the idea of corporate social responsibility.

⁽²¹⁾ Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments.

⁽²²⁾ Member of the European Parliament and member of the Alternativa Responsable ('Responsible Alternative') movement.

⁽²³⁾ A number of countries of the European Union have this fund.

Medals are awarded in the presence of hundreds of CEOs, ministers, members of the diplomatic corps, the Prime Minister and even the President of Poland, the President of the European Commission or the EESC President.

5.4 For socially responsible investment to reach maturity, the EESC urges the public institutions to give their backing in order to facilitate the creation of the appropriate legal frameworks, promote investment with sustainability criteria, help to highlight good practices and encourage investments in these kinds of financial products, for example, through suitable tax policies⁽²⁴⁾. One very effective way of stimulating the market is for public bodies to apply sustainability criteria in their own investments, whether yields are fixed or variable, through social security reserve funds or sovereign wealth funds, as happens in

France. In the field of regulation and from the transparency viewpoint, it is important to highlight the impact of introducing rules that encourage investment fund management companies or institutions for occupational retirement pensions to state whether or not they include social and environmental criteria in their choice of investments, as happens in the United Kingdom.

5.5 The EESC underlines the importance of companies' commitment and active management on the part of financial market intermediaries. Managers of institutions for occupational retirement provision, the SRI product committees, supervisory commissions and trade unions are all driving forces in the market for socially responsible funds.

Brussels, 26 May 2010.

The President
of the European Economic and Social Committee
Mario SEPI

⁽²⁴⁾ Economistas sin Fronteras (Economists without Borders) (2007) *Cómo fomentar la inversión socialmente responsable en España* ('How to encourage socially responsible investment in Spain'), UNED.