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## Consultation Response

### FCA DP 23/1: Finance for positive sustainable change: governance, incentives and competence in regulated firms

10 May 2023

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The Association for Financial Markets Europe (“**AFME**”) welcomes the opportunity to respond to the FCA’s discussion paper (DP 23/1) on finance for positive sustainable change: governance, incentives and competence in regulated firms (the “**Discussion Paper**”).

AFME welcomes and is eager to engage in industry-wide dialogue on firms’ sustainability-related governance, incentives and competences. AFME members are supportive of the aims that the FCA is looking to achieve in the paper but wish to raise a number of concerns common to each of the questions we are responding to:

1. For certain matters considered in the Discussion Paper, there already exists comprehensive legislative and regulatory frameworks that can be / are already being applied in a sustainability-context by firms. Where that is the case, there would not be additional benefit to be gained by introducing a sustainability-specific framework.
2. A prescribed “one-size-fits-all” approach to addressing sustainability-related concerns would not be appropriate for firms with a diverse range of regulatory profiles, business models and geographical footprints. Tom Gosling notes in Article 2 of the Discussion Paper that firms should focus on the “strategically material” ESG issues that require a step-change in their organisations. Across the diverse range of regulatory profiles that would be in-scope, there will be a diverse range of “strategically material” ESG issues. Building on this idea, if the sustainability-related considerations that are considered “strategically material” vary from firm-to-firm, a set of prescriptive sustainability-related expectations would not be appropriate and may be counterproductive. Instead, it would be more appropriate for firms to apply the existing legislative and regulatory frameworks noted above in a sustainability-context, taking the approach most suitable for their most strategically material sustainability-related considerations.
3. AFME members are particularly concerned with mandating a prescribed approach for UK subsidiaries or branches of third-country firms, in light of the following considerations:
  - a. Such firms’ sustainability policies/strategies are likely to be set at HQ-level, which may be in a jurisdiction that has a different regulatory landscape or approach/political appetite to sustainability-related considerations. Such firms would therefore be faced with a fragmented regulatory landscape with misaligned (and possibly conflicting) requirements. Therefore, the need for deference to the requirements of a firm’s home jurisdiction should be a key consideration when formulating the future approach in this area, allowing such firms the latitude to develop UK-specific approaches to sustainability where relevant, which takes into account their approach to sustainability-related considerations.
  - b. In addition to issues of fragmentation, third country firms may also be faced with the additional cost of preparing UK-specific policies and documentation, when group-wide policies/documentation are already prepared at HQ-level. The additional costs may not generate any real additional sustainability benefits and the additional process may prove to be inefficient. This will be a particular issue for third country firms with a small, limited UK presence. Therefore, the need to permit reference to policies/documentation produced

according to home jurisdiction requirements should also be considered when formulating the future approach.

- c. Where the issues raised at points (a) and (b) above arise, mandating a UK-specific prescribed approach may in fact create a barrier to UK international competitiveness and deter international firms from building out their presence in the UK.
4. Similarly, if a UK-specific approach is mandated, the concerns relating to anti-competitiveness will also apply in respect of UK firms operating internationally, as this may present a barrier to such firms building out their presence outside of the UK. Instead, we wish to highlight the importance of international coordination in relation to supervisory approaches to sustainability and encourage the FCA to coordinate through IOSCO and with counterparts in other jurisdictions, including the EU, to avoid fragmentation and misalignment.
5. If sustainability-specific expectations are set, this would necessitate a process of carefully crafting a set of considerations that are considered “sustainability-related considerations”. AFME members note that this will not be a straight-forward task, taking into consideration the evolving nature of this area, the resulting complexity and the difficulties previously encountered with crafting a definition of “sustainability” with sufficient specificity. Further, AFME members note that expert knowledge and understanding on sustainability-related topics are developing at a fast rate. In light of this, it may be too early to formulate a prescribed set of sustainability-related considerations or expectations.

For these reasons AFME members welcome the FCA’s focus on proportionality and differentiation between firms in determining the direction of future regulatory approach. If there are specific areas of risk or concern that the FCA are looking to address with its proposals, AFME members welcome the opportunity to discuss these specific areas with the FCA. However, AFME members have not identified any specific areas of risk or concern and therefore AFME members take the view that in the areas considered below, the proportionate response generally would not be to introduce sustainability-specific expectations, as the existing frameworks already in place can be, and are already being, applied by regulated firms in a sustainability-specific context.<sup>1</sup> It would not be proportionate to introduce new frameworks, when existing frameworks are already functioning effectively where there are no specific areas of concern that would require a new framework in order to be addressed. The existing frameworks allow firms the much-needed flexibility to formulate their approach to sustainability in the context of their own materially strategic sustainability-related concerns and in the context of their geographical footprint (including the relative size of their UK presence). The introduction of prescriptive sustainability-related expectations would be counterproductive in an area that inherently requires flexibility for firms to develop their own approaches and in an area that is still fast-evolving.

On this basis, AFME members take the view that it would be helpful for the FCA to introduce guidance to explain to firms the existing frameworks the FCA considers relevant in the context of the sustainability related considerations identified in this paper. This could take the form of a single document of non-Handbook guidance to direct firms to the frameworks and useful materials that already exist in this context. It could also

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<sup>1</sup> However, as an exception to this general position, in our response to question 7, AFME members take the view that it may be helpful to introduce non-exhaustive, high-level guidance on applying the existing product governance framework in a sustainability-specific context. We also note in our response to question 3 that it may be helpful to have guidance on how the upcoming sustainability-specific updates to the FRC Corporate Governance Code should be applied by regulated firms once these changes have been implemented and their impacts understood. In our response to question 8, we note that guidance would only be workable in so far as it is limited to a high-level general principle.

take the form of new guidance provisions in existing Handbook rules to remind firms where such existing rules also apply in a sustainability-context.

### **Consultation questions**

**We provide responses to individual questions from the consultation below.**

- 1. Should all financial services firms be expected to embed sustainability-related considerations in their business objectives and strategies? If so, what should be the scope of such expectations? Please explain your views.**
  - 1.1 AFME members note that firms are already taking steps to embed sustainability-related considerations into their business objectives and strategies, based on not only existing legal and regulatory requirements but also on firms' existing business models, strategies and specific approaches to sustainability. For example, as part of meeting existing FCA disclosure requirements relating to entity-level climate strategy (under the FCA's rules for TCFD-aligned disclosures for premium listed issuers, asset managers and asset owners), many firms are already embedding climate-related considerations into their business objectives and strategies. Firms are also anticipating the steps they will need to take to embed climate-related considerations in light of the disclosure obligations contained in Sub-element 1.1 (*Objectives and priorities*) and Sub-Element 1.2 (*Business model implications*) of the UK's draft Transition Plan Task Force ("**TPT**") Disclosure Framework. AFME members therefore do not think that introducing an expectation in this regard would provide additional benefit.
  - 1.2 Further, a prescribed set of expectations to embed sustainability-related considerations into business objectives and strategies would not be suitable for the diverse range of firms (with a diverse range of profiles and geographical footprints) that such considerations would apply to:
    - (a) The appropriateness of sustainability-related objectives and strategies are highly firm-specific and firms need to be able to develop a sustainability approach that is specific to their business model, and to their "strategically material" sustainability-related concerns. Any constraint to this approach is likely to prove counterproductive.
    - (b) The position of UK branches and subsidiaries of third-country firms would also be of particular concern in this context. Such branches/subsidiaries may be subject to a firm-wide set of objective/strategies that were set in the context of the home jurisdiction's regulatory and political landscape, which may be mis-aligned with the UK approach. In such cases, branches/subsidiaries would need the latitude to defer to the approach taken in HQ's home jurisdiction.
- 2. Beyond the FCA's ongoing work on diversity and inclusion, and introduction of the Consumer Duty, should we consider setting regulatory expectations or guidance on how firms' culture and behaviours can support positive sustainable change? Please explain your views.**
  - 2.1 AFME members agree that firm culture is at the heart of the delivery of positive sustainable change and agree that firms must take steps to build a culture and encourage behavior that supports positive sustainable change. However, AFME members take the view that specific requirements around culture relating to sustainability would not provide any additional benefit.
  - 2.2 The FCA's detailed expectations on healthy firm culture are already clearly articulated through the Conduct Rules and associated guidance contained in COCON, through the SMCR, the Remuneration

Codes and guidance on appropriate incentive structures and the [various non-Handbook materials](#) produced by the FCA on culture (inclusive of the new Consumer Duty). The current regulatory expectations and guidance provide a comprehensive framework for firms to apply in order to build a culture and encourage behaviors that support positive sustainable change. AFME members are already utilising existing FCA expectations and guidance to formulate cultural frameworks that support measures to bring about positive sustainable change.

- 2.3 Furthermore, given the diverse range of firm profiles that these rules would apply to, additional, more prescriptive requirements around culture may be difficult for firms to apply in a productive and helpful way. Once again, this would prove particularly difficult for branches and subsidiaries of third country firms, that may be following internal policies on culture set at HQ level in a different jurisdiction that may have a different political and regulatory landscape.
3. **What steps can firms take to ensure that they have the right skills and knowledge relating to material climate- and sustainability-related risks, opportunities and impacts on their boards? Should we consider setting any regulatory expectations or guidance in this area? If so, what should be the scope of such expectations?**

#### **Skills and knowledge**

- 3.1 AFME members take the view that it would not be beneficial to introduce prescriptive expectations or guidance on the breadth of sustainability knowledge and types of training that the FCA expects of firms.
- 3.2 AFME members note that firms' boards and managing bodies are already subject to rules and expectations on their skills and experience, for example: (i) the duty for directors under s.174 Companies Act 2006 to exercise reasonable care, skill and diligence; (ii) SYSC fitness and propriety requirements; and (iii) ECB-level fit and proper assessments for management bodies of significant credit institutions.<sup>2</sup> AFME members take the view that this existing body of rules is sufficient and can be applied by firms in a sustainability context.
- 3.3 One example of an approach currently being taken by firms, based on their application of existing legislative and regulatory frameworks, to ensure that they have the right skills and knowledge on their boards is to establish units of sustainability expertise within the firm<sup>3</sup>, and ensure that seniors from such units brief and advise the board on sustainability-related matters. Further, in accordance with PRA requirements, dual-regulated firms have multiple dedicated sustainability briefings to boards.
- 3.4 Due to the diverse range of firm profiles that would be in-scope, additional sustainability-specific prescribed expectations would not be suitable and would not provide any additional benefit. As noted above, the sustainability issues that are considered "strategically material" will vary significantly from firm-to-firm. Therefore, a set of prescriptive expectations as to the right set of skills and knowledge would not be appropriate. The better approach is to allow firms to apply existing frameworks and determine the right set of skills and knowledge for their "strategically material" sustainability issues.

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<sup>2</sup> In addition, dual-regulated firms are already subject to PRA requirements to ensure that board members or subcommittees with accountability for climate are sufficiently qualified or trained in climate risk (and to ensure that boards are supplied with enough high-quality, relevant information from senior management).

<sup>3</sup> This includes, for example, creating dedicated financing teams focused on Green, Social and Sustainability bonds, creating dedicated advisory teams focused on transition infrastructure, creating research capabilities and centres of expertise and potentially establishing academic partnerships.

In addition, the extent to which sustainability-related skills and expertise are needed in a firm will need to be proportionate to that firm's size and activities. This consideration is particularly relevant for smaller UK branches and subsidiaries of third country firms that have a limited UK presence, for which a suite of staff with extensive sustainability-related skills and experience at subsidiary/branch-level may not be necessary.

- 3.5 AFME members also wish to highlight that firms may be at different stages in terms of ensuring the right level of sustainability knowledge and expertise within their organisations. Some firms may already be at an advanced stage of implementation and embedding in their organisation, whereas some firms may just be at the beginning of implementation. Given the varying needs of firms, a set of prescriptive expectations is unlikely to be helpful.
- 3.6 Lastly, AFME members note that the FCA does not take a prescriptive approach in respect of skills and knowledge relating to risks other than sustainability. AFME members cannot identify a justification for taking a more prescriptive approach for sustainability, as opposed to other risks.

### **Board composition**

- 3.7 Please see our response to Q6 below in respect of updates to the Senior Managers Regime. Beyond this, if FCA guidance is introduced on how existing corporate governance frameworks in the Companies Act 2006, the Financial Reporting Council (the "FRC") Corporate Governance Code and (for issuers) DTR 7 should be applied in the sustainability context, this guidance should come at a later stage. The FRC are [intending to revise](#) the FRC Corporate Governance Code, with the intention that a revised Code will apply on or after 1 January 2024. Amongst the other issues being considered, the FRC revisions will focus on making the necessary changes to reflect the wider responsibilities of the Board and Audit Committee for expanded sustainability- and ESG-reporting. AFME takes the view that the changes introduced by these reforms and the impacts of these changes should be understood before any additional guidance is introduced at an FCA-level, with a view to ensuring a consistent approach and ensuring that any additional guidance is targeted towards the FCA clarifying how it sees the updated Code being implemented within regulated firms. This is a deviation from the general position set out in the introduction to this response, that additional guidance would generally not be helpful and may in fact be counterproductive.
- 3.8 As above, due to the diverse range of profiles of firms and the diverse range of "strategically material" ESG issues, AFME members do not consider that a more prescriptive set of sustainability-specific expectations would be appropriate.
- 3.9 AFME members assume that any guidance as to board composition would apply at a UK-level. As previously noted, for branches and subsidiaries of third country firms, sustainability strategy may be set at a global level, as part of the global corporate strategy, and driven at a global level, by the (non-UK) parent company board. Any additional guidance introduced by the FCA should expressly state that such guidance may not be relevant for branches or subsidiaries of third-country firms.
- 4. What are likely to be the most effective strategies in embedding climate- and sustainability-related considerations across a firm's operations? What is the potential benefit of initiatives such as the appointment of functional 'champions', or the creation of dedicated working groups or forums? And how can the value of such initiatives be enhanced?**
- 4.1 AFME members are particularly concerned about the possibility of introducing a requirement for sustainability champions, either within or outside of the context of the SMCR framework.

- 4.2 AFME members consider that the implementation of effective strategies in embedding climate and sustainability related considerations across a firm's operations would not benefit from the introduction of champions. Effective implementation of such strategies are multi-disciplinary in nature, requiring the cross functional collaboration, inclusive of risk management and oversight by the second and third line of defence. For example, some firms take the view that the specialist Sustainability Team is the centre of expertise that can work with SMCR ownership units to develop as needed to address sustainability-related issues.
- 4.3 AFME members are of the opinion that the SMCR already defines roles and responsibilities across functions and therefore appropriate implementation of business strategy and, by proxy, the consideration of sustainability and climate related factors, are inherent in the roles and responsibilities of approved Senior Management Functions. The introduction of dedicated champions would dilute accountability and only act to fracture climate- and sustainability-related issues from being considered/implemented as part of a holistic business model and strategy, which takes into account climate risk and sustainability as part of a wider risk appetite, alongside the development and implementation of a sustainable business model in the broader sense.
- 5. What management information does senior management use to monitor and oversee climate- and sustainability-related developments, and to monitor progress against public commitments? Should we set expectations or guidance for decision-making processes, including systems and controls, audit trails and the flow of management information to key decision-makers? If so, what should be the scope of such expectations?**
- 5.1 AFME members take the view that existing UK regulatory requirements on systems and controls are sufficient and are already being applied in a sustainability context to monitor and oversee climate- and sustainability-related developments and to monitor and track progress against public commitments. In light of this, a sustainability-specific framework is unlikely to provide any additional benefit.
- 5.2 In addition, such a framework is unlikely to be suitable for the vast range of firm profiles that it would apply to, as the processes that would need to be put in place for such tracking is likely to be highly firm-specific. For example, for third country firms with a smaller UK branch or subsidiary, such tracking may not take place at UK-level.
- 6. Should we consider setting new regulatory expectations or guidance on senior management responsibilities for a firm's sustainability-related strategy, including the delivery of the firm's climate transition plan? If so, which existing SMF(s) would be the most suitable to assume these responsibilities? Please explain your views.**
- 6.1 AFME members consider that current / proposed regulations, such as those referenced within other sections of this response, and the continued evolution of guidance and standards related more broadly to sustainability, is sufficient to set out expectations and/or provide guidance for firms on the responsibilities related to sustainability related strategy (including climate transition plans).
- 6.2 With this in mind, AFME members understand that the SMCR framework has been designed to accommodate the evolving nature of regulation, by ensuring that each SMF has inbuilt/inherent responsibilities, supported by the additional flexibility for firms to identify and allocate overall (local) responsibilities where appropriate, taking into consideration the activities that each firm undertakes and their business models. As such, adding additional prescribed responsibilities, or mandating any additional allocation would undermine the concept of inherent responsibilities and reduce the inbuilt flexibility of the SMCR, therefore also undermining the principles of proportionality and appropriateness.

- 6.3 The UK TPT Disclosure Framework, in particular Sub-element 5.2 (*roles, responsibility and accountability*) already requires a description of senior management roles and responsibilities for the execution of the transition plan (as well as the entity's wider control, review and accountability mechanisms). Additionally, Board/Director responsibilities as outlined in legislation, such as the Companies Act 2006, and built upon in guidance (such as guidance being introduced by the FRC and guidance introduced by the Basel Committee for Banking Standards) also sets out the expectations related to the design and development of sustainable business models and strategies. Furthermore, as noted in the Discussion Paper, PRA SS3/19 already sets out an expectation for dual-regulated firms to allocate responsibility for identifying and managing financial risks from climate change to an appropriate existing SMF within the firm's organisational structure, ensuring that sustainability- and climate-related risks drive the development of business strategy and, by proxy, long term transition to more environmentally sustainable business models.
- 6.4 Therefore, any additional Prescribed Responsibilities, guidance or regulatory expectations at this stage may be counteractive to the SMCR's original purpose, adding additional complexity into an already complex and evolving area, while diluting established principles of the SMCR and the concept of inherent responsibilities.
- 6.5 Furthermore, we note that the UK Government is considering reform of the SMCR as part of its wider package of Edinburgh Reforms. AFME members therefore take the view that any consideration of sustainability in the context of the SMCR would be more appropriately considered as part of the wider package of legislative reform of the SMCR.
7. **Should we consider introducing specific regulatory expectations and/or guidance on the governance and oversight of products with sustainability characteristics, or that make sustainability claims – for example to clarify the roles and expectations of governing bodies such as Fund Boards? If so, which matters in particular would benefit from clarification?**
- 7.1 Firms in-scope of disclosure requirements under the EU Sustainable Finance Disclosure Regulation ((EU) 2019/2088) ("**SFDR**") and Delegated Directive (EU) 2017/593 ("**MiFID II**"), or firms preparing to comply with labelling requirements under the FCA Sustainability Disclosure Requirements ("**SDR**") are already taking steps to ensure that sufficient product governance and oversight systems are in place for products with sustainability characteristics or for products that make sustainability-related claims, also relying on ESMA guidelines on product governance.
- 7.2 As noted in the Discussion Paper, we understand that the FCA is currently considering feedback to its proposal in CP22/20 that one of the core principles of the criteria to qualify for a label under SDR should be to ensure appropriate resources, governance and organizational arrangements to support the delivery of a product's sustainability objective, including oversight by a governing body, where appropriate. AFME's view is that the existing product governance rules set out in PROD are sufficient for guiding firms on the steps they would be required to take in order to meet this core principle. Non-exhaustive high-level guidance on applying the existing product governance framework in a sustainability-context would be helpful. This is a deviation from the general position taken in this response, that additional guidance would generally not be helpful and may in fact be counterproductive. However, consistent with our general position, it is also the case that in this area additional prescriptive expectations or guidance would not be necessary. In-scope firms will have a diverse range of regulatory profiles, with a diverse range of "strategically material" sustainability considerations relevant to their product offerings. Therefore, prescriptive expectations or guidance in this respect are unlikely to be helpful.

- 8. What matters should firms take into consideration when designing remuneration and incentive plans linked to their sustainability-related objectives? In particular, we welcome views on the following: (a) the case for linking pay to sustainability-related objectives; (b) whether firms should break down their sustainability-related commitments into different factors, allocating specific weightings to each; (c) whether short-term or long-term measures are more appropriate, or a combination of both; (d) whether sustainability-related incentives should be considered for senior management only, or a wider cohort of employees; (e) how firms could consider remuneration and incentive plans in the design and delivery of their transition plans; (f) remuneration adjustments where sustainability-related targets (at either the firm level or individual level) have not been met. Please explain your views.**
- 8.1 In respect of point (a), AFME members are supportive of the case for linking pay to sustainability-related objectives, where appropriate. However, AFME members take the view that prescriptive expectations or guidance on how firms should consider sustainability when designing remuneration and incentive plans would not be appropriate. Guidance would only be appropriate and workable in so far as it is limited to high-level guidance stating that firms should consider sustainability in the context of remuneration and incentives and set their own objectives.
- 8.2 Branches and subsidiaries of third country firms will already be navigating a regulatory landscape in their home jurisdiction and may be navigating a different political/regulatory appetite towards linking sustainability to remuneration and incentives. Where this is the case, AFME members note that any guidance should emphasise that such subsidiaries and branches are permitted to pay attention to the best practices and norms in their home jurisdiction.
- 8.3 In respect of point (b), AFME members note that prescribing a process for linking sustainability to remuneration and incentives may also increase the risk of greenwashing. The risk of this is increased where such processes are not calibrated in a firm-specific way and instead are calibrated according to a broader prescribed standard that may not be suitable for precise tracking of progress towards a firm's "strategically material" sustainability objectives. As noted above, appropriate sustainability-related objectives and strategies will be highly firm-specific. Therefore, the process of linking progress towards these objectives with remuneration and incentives will also be highly firm-specific. AFME members also highlight the difficulty around mandating prescribed sustainability-metrics, on the basis that monitoring progress towards sustainability-related objectives is often a qualitative assessment rather than quantitative assessment.
- 8.4 In respect of points (c) and (f), AFME members note, as also acknowledged in the Discussion Paper, that sustainability-related objectives are often long-term, whereas the periods over which staff performance is measured tend to be shorter-term. With this in mind, factoring sustainability-related objectives into remuneration processes will be a complex and highly firm-specific calculation, in particular when considering the extent to which malus and clawback may be appropriate in relation to progress towards longer-term objectives. Prescribed expectations or guidance in this respect are unlikely to provide additional benefit.
- 8.5 In respect of point (d), AFME members wish to highlight that linking performance measures to sustainability-related factors would not be appropriate for firms' wider workforces or cohorts of staff, as many members of staff will not have a role with any relevance towards sustainability. Furthermore, a greenwashing risk is also presented when sustainability-related factors are integrated into performance measures for roles that do not have relevance to sustainability. In the context of UK branches and subsidiaries of third-country firms, this risk is particularly pertinent, as sustainability strategy and objectives are often set at a global level. Staff on the ground in the UK may have a role with very little relevance to sustainability, including members of the UK leadership team in the UK who



may have very little ability to impact on the firm's overall approach to sustainability. Therefore prescribed sustainability-related expectations in relation to performance measures for such staff would have little benefit.

8.6 In respect of point (e), AFME members note that this forms part of Sub-element 5.4 (*incentives and remuneration*) of the UK TPT Disclosure Framework. AFME members are therefore of the view that any additional guidance in this respect will not be necessary.

**9. Should we consider additional regulatory expectations or guidance in any of the areas considered in Q8? Please explain your views.**

9.1 As noted above, in the context of remuneration and incentives, anything beyond high-level guidance (stating that firms should consider sustainability in the context of remuneration and incentives and set their own objectives) is unlikely to provide an additional sustainability benefit, and in some cases may lead to increased green-washing risk.

**10. Should we consider additional regulatory measures to encourage effective stewardship, particularly in relation to firms' governance and resourcing of stewardship, and associated incentive mechanisms and conflict of interest policies? Are there regulatory barriers that we should consider? Please explain your views.**

10.1 Whilst we agree that stewardship has an important role to play in influencing positive sustainability outcomes, AFME members nevertheless recommend that the FCA does not introduce any prescriptive rules around stewardship at this stage. Since the introduction of the 2020 Stewardship Code (the "**Stewardship Code**") by the FRC, firms have significantly progressed and embedded their approach to stewardship, including in relation to governance and resources. Implementation of many of the requirements for signatories of the Stewardship Code have naturally resulted in more formalised processes and improved recording of outcomes as well as enhanced resourcing for delivering those outcomes. It is important that firms have the flexibility to adopt a meaningful approach to stewardship - in this respect, the most important part of stewardship is the outcome, rather than a strict and rules-based approach to the stewardship process.

**11. What additional measures would encourage firms to identify and respond to market-wide and systemic risks to promote a well-functioning financial system? How can the collective stewardship efforts of asset owners and asset managers best be directed towards the most pressing systemic issues? And how can remaining barriers best be reduced? Please explain your views.**

11.1 Please see our response to question 10 above. As noted above, since the introduction of the Stewardship Code, firms have significantly progressed and embedded their approach to stewardship, including in relation to governance and resources. Introducing additional measures would risk compromising flexibility, which is important for firms in order to adopt a meaningful approach to stewardship.

**12. What do you consider to be the main sustainability-related knowledge gaps across the financial sector and how can these best be addressed? What do you consider to be the potential harms to market integrity, consumer protection or competition arising from these knowledge gaps?**

12.1 Please see our response to question 13 below. AFME members take the view that the sustainability-related issues that are "strategically material" will vary from firm-to-firm and therefore it is most

appropriate for firms to have the latitude to decide the issues and associated knowledge gaps to prioritise and address.

**13. Do you think there is a need for additional training and competence expectations within our existing rules or guidance? If so, in which specific areas do you consider further rules and/or guidance are required? Please explain your views.**

13.1 AFME members agree that training and competence is an important area for firms to focus on to ensure positive sustainability-impact.

13.2 However, expert knowledge on the underlying relevant subject matter is evolving at a very fast rate and therefore the sustainability market is also rapidly evolving, both in relation to sustainability solutions and in relation to firm and regulator understanding of sustainability risks. AFME members take the view that it is too soon to set out specific expectations for training and that to do so at this stage would be counterproductive. In addition, as noted above, the sustainability issues that are “strategically material” will vary from firm-to-firm. It is therefore more appropriate for firms to have the latitude to decide how to prioritise the issues to focus on in their training. AFME members note that the FCA does not take a prescriptive approach in respect of training on risks other than sustainability. AFME members cannot identify a justification for taking a more prescriptive approach for sustainability, as opposed to other risks.

13.3 Similarly, as we believe firms must have the flexibility to create their own expectations of employees which are unique to individual firm business models, we therefore do not believe that it would be appropriate at this stage to introduce regulatory rules outlining specific sustainability competence requirements to be met by individuals. It would be extremely challenging to identify an appropriate sustainability qualification which (i) would not interfere with a firm’s ability to develop and understand its own unique challenges and opportunities; and (ii) would not risk becoming out of date very quickly in a rapidly evolving market. As the FCA has identified in the Discussion Paper, SYSC 5.1 (the competent employees rule) already requires firms to ensure that individuals engaged in regulated activity have the appropriate skills, knowledge and expertise necessary for the discharge of the responsibilities allocated to them. We believe that maintaining relevant skills and expertise in relation to sustainability is included within that overall requirement, and for the reasons outlined, would not recommend that the FCA take a distinct or separate approach to sustainability at this stage.

**14. Which aspects of the training and capability-building initiatives discussed above, or any others, would be particularly useful to consider (for example in identifying which skills and/or training is needed) and how best should we engage with them?**

14.1 Please see our response to question 13 above. AFME members take the view that sustainability-specific rules and guidance on competence and training would not be beneficial.

**15. Have you seen misrepresentation of ESG credentials among ESG professionals and, if so, what are the potential harms? Have you seen any consistent training metrics that can help compare firms’ knowledge/capabilities? Please describe.**

15.1 AFME members do not have specific examples to provide. Please see our response to question 13 in relation to training and competence more generally.

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## **About AFME**

AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.<sup>4</sup>

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<sup>4</sup> AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia. AFME is registered on the EU Transparency Register, registration number 65110063986-76.