Response to the FCA Consultation
on
Finance for Positive Sustainable Change: Governance, Incentives and Competence in Regulated Firms

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Response to the FCA Consultation on Finance for Positive Sustainable Change Governance, Incentives and Competence in Regulated Firms

The following is Philanthropy Impact's initial response to FCA Consultation on Finance for Positive Sustainable Change: Governance, Incentives and Competence in Regulated Firms.

1.0 About Philanthropy Impact

Mission

Philanthropy Impact (www.philanhtgropy-impact.org) is a capacity building non-profit organisation at the intersection between ESG and impact investment, social investment and philanthropy. Our mission is to increase the flow of capital for good.

We are a membership network creating opportunities to increase and improve ESG/impact investing, social investment and philanthropy.

Means

We achieve this by building the will and capacity of professional advisors (private client advisors in wealth management, private banking, tax, accountancy and legal sectors) to support their (U)HNW private clients on their impact investment and philanthropic journey. Our stakeholders also include philanthropists, impact investors, trusts and foundations, and charities and social enterprises.

Our means for realising our vision includes:

- CPD Certified CISI endorsed training for private client professional advisors; the training addresses increased customer centricity focusing on achieving positive outcomes on customer support and consumer understanding improving an advisor's approach to client suitability and to meeting Consumer Duty's outcomes as well as to responding to changing client demand which includes clients seeking to align their wealth with their values.
- Thought leadership and sharing intelligence, events, bespoke networking opportunities, campaigning, publications including a magazine, and resources for advisors and other stakeholders.

2.0 Response to Consultation

Consumer Duty emphasises that wealth management firms must protect their clients and "For many firms, this will require a significant shift in culture and behaviour" (FCA) – resulting in increased customer centricity. Education and training will be essential in supporting this change, helping to reinforce an approach that ensures advisors are trained to address client values and motivations.

2.1 Questions 12-14 – Addressing Training Needs

Q12: 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?

There is a lack of will, knowledge and ability in the wealth management sector related to supporting clients on their values led sustainable investing across the spectrum of capital, including not having it as part of an advisor's KPIs. Balancing financial return and impact are an essential part of the advisor-client conversation (potentially contextualised within SDGs). As demonstrated in the summary research in 2.2 below there is a threat to firms if they do not meet this growing demand.

2.1.1 Addressing the Essence of Q12-14 See below for more detail on client demand and its changing nature.

Q13: 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.
Mandatory training for private client professional advisors is essential to achieving positive sustainable change. An advisor cannot achieve customer centricity demanded by Consumer Duty without the ability to discuss with clients their values, motivations, ambitions related to their sustainable preferences. Advisors need to be able to have these discussions with their wealth-holding clients (and their families as appropriate), to help them in their selection of investment products (assuming this will lead to a range of sustainable products being available) and to include working with other professional advisor firms across the 23 services (within the context of planning, implementation and review/evaluation) needed on a client's impact journey.

2.1.1 Addressing the Essence of Q12-14 See below for more information.

Q14: 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?

2.1.1 Addressing the Essence of Q12-14 See below for the rationale for training and for a brief outline of the training required to support clients on their sustainable impact journey.

2.1.1 Addressing the Essence of Q12-14

We agree that sustainability (environment, human rights, diversity, inclusion), changing client needs and demands and governance should be at the heart of Consumer Duty contributing to and driving positive change.

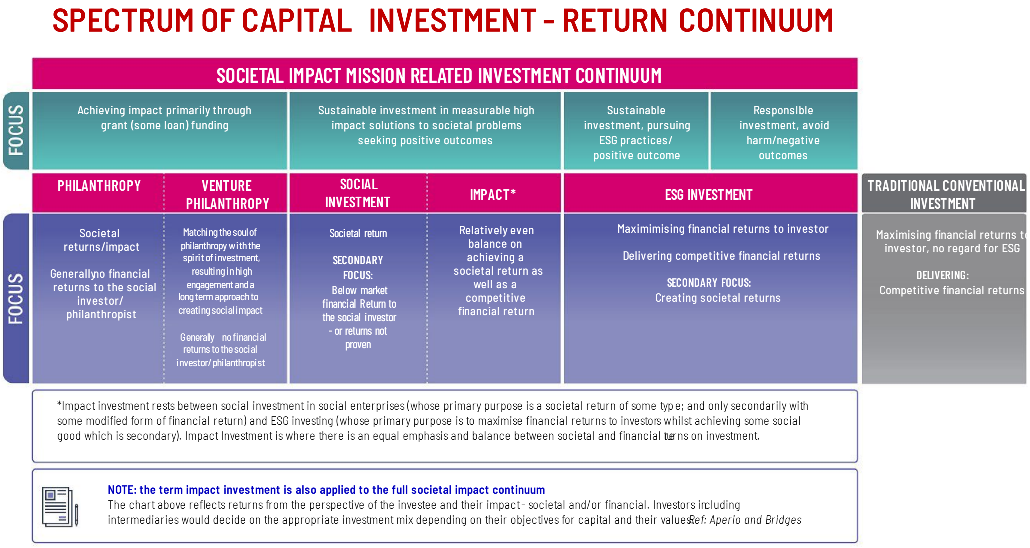
In order to be customer centric it is essential for professional advisors to help clients live their values. Advisors need to be aware of changing client needs and demands and to receive proper training to enable them to support clients on a values-based wealth journey across the spectrum of capital; addressing, developing the capacity and building into services, the ability to meet the 23 services needed by a (U)HNWI on their impact journey .

This is especially important in light of:

- Our recent research where Millennials and GEN Z wealth holders stated that they are increasingly seeking to align their wealth with their values, expecting their professional advisors to provide professional support related to responsible investing and philanthropy. They indicated that the professional advisory industry is falling short of the expectations of emerging wealth holders. There are warnings that the on-going wealth transfer could be accompanied by the next generation changing advisors en masse.
- A recent study 'Investing for Global Good - A Power for Good 2022' indicated that, for older generations, there is a growing demand for and satisfaction in impact investing and that investors are seeking better services from wealth advisors; with 70% reporting that sustainable investing is being embraced by the generation in charge of the family's wealth.
- Fidelity Charitable Research in 2022 demonstrated that firms who offer charitable gift planning to their clients had 6X the median assets of those who do not offer such planning, 3X organic growth, 1.3X new money; as well as gaining higher levels of trust.

In essence the elements of the model for consideration is:

The following is a summary of a values-based wealth journey across the spectrum of capital.



We recommend that training related to the above should be an essential part of the training of professional advisors.

An example of an approach to reinforcing customer centricity and to meeting Consumer Duty's two outcomes on customer support and consumer understanding is the CPD Certified and CISI endorsed training provided by Philanthropy Impact to professional advisors in the wealth and finance industries. It is designed to give advisors the confidence, tools and support they need to talk with their clients about their values, motivations and ambitions, moving beyond the current approach to suitability.

The Philanthropy Impact bespoke in-house training course is a personalised and customised approach to meet the needs of firms, advisors and customers. Its purpose is to:

- Prepare wealth advisors to meet FCA Consumer Duty compliance taking into account client sustainability preferences.
- Prepare wealth advisors for meaningful suitability conversations with their clients on matters related to their ESG/impact investment journey.
- Discover the benefits of putting suitability discussions into practice beyond the current approach.
- Develop impactful approaches to addressing a client's values, motivations, ambitions and goals, helping clients move from their values to choosing the most impactful approach to their investments.
- Understand the value that sustainable investing brings to the advisor's business practice including improving client engagement and satisfaction and creating new business opportunities.

Essentially more than a framework will be needed to help a firm meet the regulator's standards if the new skills do not "stick". That is why the training is needed to give advisors the confidence, tools and support they need to talk with their clients about their values, motivations and ambitions, moving beyond the current approach to suitability.

In summary, the highly interactive training, which is composed of two complementary sessions, is adjusted on a bespoke basis to the existing circumstances of a firm as assessed as part of the process. Module 1 covers:

- Trends and benefits to a firm
    - The context – meeting client expectations
    - Millennials, GEN Z and Women of Wealth – driving the change supported by older generations
    - Market trends – evidence/research/market studies
    - Consumer Duty and its implications for professional advisors
- Understanding terminology
    - Importance of understanding terminology
    - Spectrum of capital investment return continuum and its implications
    - Definitions, jargon, typology of sustainable investment
    - UN SDGs and their potential application
    - Greenwashing and measuring impact
- Engaging with clients (including exercises)
    - Being an effective professional wealth advisor - key knowledge areas
    - Consumer Duty and Suitability – enabling purpose driven wealth strategies and conversations
    - Creating a sustainable investment suitability strategy
    - Benefits
    - Understanding one's own and one's clients values and purpose
    - Where to start to establish suitability, understanding the complexity of and how to initiate the conversation including planning, implementation and monitoring and review
    - Internal organisational and readiness issues to be addressed
- Planning/implementation

Module two training aims to give a more in-depth insight into concrete engagements related to suitability, Consumer Duty and ESG/impact sustainable investment combining societal and financial returns. The training session will be case based including discussion of confidential examples from the attendees' experience with their clients and role playing scenarios.

It will reinforce module one training preparing advisors for meaningful suitability conversations with their clients on matters related to their sustainable investment journey – including combining wealth creation and preservation with their values, motivations, ambitions and goals; thereby increasing client satisfaction and trust.

The session will be highly interactive focusing on reviewing:

- The application of learnings from module one training, sharing experiences to date; and discussing how to move forward strengthening incorporation into an advisor's service offering and as part of organisational ethos and behaviour.

- The benefits of incorporating suitability discussions into practice beyond the current approach and results to date including reinforcing a values based sustainable investment journey and challenges to meeting client needs and preparations to meet changing FCA Consumer Duty requirements to take into account client sustainability preferences.
- Approaches to addressing a client's values, motivations, ambitions and goals, helping clients move from their values to choosing the most impactful approach to their investments and the value that sustainable investing brings to the advisor's business practise including improving client engagement and creating new business opportunities.
- The application of best practice for one's own advisory practice/service offering for them and their company.
- The awareness of buzz words e.g.: Measurement/Evaluation; how to deal with systems thinking/ behavioural change and systems transformation; ESG/SRI/SDG investment criteria; Mindful Finance/ Innovative Finance; Inclusion/Diversity as drivers of change; structuring possibilities; donor journey/NGO relationships (by age).

2.2 Q1

Q1: 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.

All wealth management firms should embed sustainability into their goals, plans and intended impact business including appropriate levels of investment. This would result in firms embracing the achievement of SDGs across the spectrum of capital. This means moving beyond negative screening and ESG investing to impact investing actively contributing to social and environmental solutions and transformations. It means:

- Not just impact investing but also social investment and philanthropy
- Addressing the harm vs. good argument doing good through philanthropic giving while doing harm through investing
- Utilising blended finance to support addressing high risk sustainable investment opportunities, innovation and growth; with philanthropic giving and social investment acting as a catalyst to achieving increased investment capital

Part of the problem is jargon including what 'sustainability' means. It is essential, if firms are to focus on sustainability, that there needs to be clear understanding of its meaning and not just of its implications. According to ChatGPT the definition of sustainability is: **Sustainability is the ability to meet the needs of the present without compromising the ability of future generations to meet their own needs. It involves taking a long-term view of economic, social, and environmental issues and making decisions that balance the needs of the present with the needs of future generations. In practice, sustainability involves finding ways to use resources efficiently, reducing waste and pollution, protecting natural habitats and biodiversity, and promoting social equity and economic development. The goal of sustainability is to create a world where people can enjoy a high quality of life without degrading the natural systems that support us.**

Additionally to achieve the essence, Consumer Duty firms must take a sustainable approach to their businesses and to their clients.

Of note, MiFID II says portfolio managers and professional advisors need to understand and consider investors' sustainability preferences.

2.3 Q2

Q2: 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.

Firms can play a significant role in supporting sustainable change individually and with its employees, stakeholders and customers; as part of a trade association and in partnership with civil society. It should be an integral part of their ESG and impact strategy. Minimal regulatory expectations together with appropriate guidance should be set by the FCA to achieve this end. Without this the impact of Consumer Duty will be minimised.

To achieve the change of the nature implied in Consumer Duty and this consultation, sustainability is an essential component in establishing and maintaining a sustainable wealth management environment. Without regulation a number of firms will not be incentivised to act in all matters with a sustainable focus – and to meet the needs for positive societal and environmental change.

To reinforce earlier points, firms in the finance sector when regulated in reference to sustainability would be encouraged to meet the changing demands of their clients and to address all aspects of the spectrum of capital. It would ensure private client professional advisors are incentivised to support their clients on their impact journey and to develop the skills to do so.

2.4 Q3

Q3: 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?

Issues are similar to those in Q2. For example firms and their Boards can play a significant role in supporting sustainable change individually and with its employees, stakeholders and customers; as part of a trade association and in partnership with civil society. It should be an integral part of their ESG and impact strategy. Minimal regulatory expectations together with appropriate guidance should be set by FCA to achieve this end. Without this the impact of Consumer Duty will be minimised.

To achieve the change of the nature implied in Consumer Duty and this consultation, sustainability is an essential component in establishing and maintaining a sustainable wealth management environment. Without regulation a number of firms will not be incentivised to act in all matters with a sustainable focus – and to meet the needs for positive societal and environmental change.

To reinforce earlier points, firms in the finance sector when regulated in reference to sustainability would be encouraged to meet the changing demands of their clients and to address all aspects of the spectrum of capital. It would ensure private client professional advisors are incentivised to support their clients on their impact journey and to develop the skills to do so.

Boards should be aware that client support s across the spectrum of capital and policies, planning and budgets are in place to enhance the firm's sustainability programme.

2.4 Q8

Q8: 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

There is a strong case for doing this especially if applied at multiple layers of management from CEO to Business Heads.

b. whether firms should break down their sustainability-related commitments into different factors, allocating specific weightings to each

This is a good idea as it identifies the key components of sustainability related commitments (environment, governance, social issues) – different firms will prioritise and give weight to these components differently depending on how important they are specifically to themselves

c. whether short-term or long-term measures are more appropriate, or a combination of both

Both are important as you need a long term vision and roadmap i.e. 2030/2050 targets but also shorter term measures/goals to maintain urgency and focus as one drives towards the longer term goals

d. whether sustainability-related incentives should be considered for senior management only, or a wider cohort of employees

Should be applied to the CEO, Board and Business Heads

e. how firms could consider remuneration and incentive plans in the design and delivery of their transition plans

Pay incentives should be based on shorter term and longer term goals and achievements, by keeping back some of the shorter term incentives in an escrow account and only handed out once the longer term goals have been achieved too

f. remuneration adjustments where sustainability-related targets (at either the firm level or individual level) have not been met

Or known otherwise as a clawback – good idea to levy against very senior individuals (CEO and Board) and Business Heads

2.5 Q15

Q15: **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.**

Misrepresentation may not be deliberate – it could be due to differing interpretations of ESG credentials and how they are dealt with – for example one person may have a blanket ban on investing in any fossil fuel related companies whilst another may take the view that it is ok to invest in such companies if they have a clear roadmap and time frame to net zero carbon emissions. Potential harm occurs when there is misinformation or if professionals do something different to what they say they are going to do with regard to ESG issues. MSCI ESG ratings and qualifications can help compare professionals' knowledge and capabilities within different firms.