AUTORITÉ DES MARCHÉS FINANCIERS

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The AMF publishes a summary on the internal processes that aim to ensure compliance with non-financial contractual commitments by asset management companies of ESG/SRI funds

The Autorité des Marchés Financiers has published a summary of a study and its findings following a series of short thematic inspections called SPOT. The study analyses the responses to a detailed questionnaire from 176 generalist portfolio asset management companies (AMCs) that have at least one contractual non-financial commitment for at least one of their funds. The inspection campaign targeted five of these 176 AMCs, whose ESG funds (incorporating environmental, social and governance criteria) or socially responsible investment (SRI) funds account for between 20% and 90% of their total assets under collective management. This publication highlights the good and poor practices observed.

The AMF had carried out an initial series of operational and thematic supervision of practices (SPOT) inspections of the SRI and ESG management systems of AMCs and published its findings in July 2019. For the SPOT inspections conducted in the second half of 2022, it selected five AMCs that manage a diversified range of funds invested in equities, money market instruments and bonds. Prior to this, the AMF had sent out a questionnaire to French AMCs in the second quarter of 2022 to understand how they monitor compliance with ESG/ISR commitments for their funds open as at 31 March 2022. The analysis of the responses from the 176 AMCs with traditional asset management activities that had defined

at least one contractual non-financial commitment in at least one of their funds served as a basis for the SPOT inspections and completed their conclusions and findings.

The study did not address the relevance of the non-financial commitments made by the AMCs that were inspected, but only the internal processes relating to these commitments.

Issues of particular interest to the AMF included:

- the organisation and resources used for ESG/SRI management;
- the ESG management and rating methodology;
- the process for selecting and monitoring external suppliers of non-financial data;
- the process for creating and reviewing the funds' initial investment universe and the ESG/SRI funds' investment process;
- the mapping of existing commitments, particularly with regard to the exclusion of issuers;
- the monitoring of compliance with commitments;
- information provided to investors on non-financial contractual commitments;
- the role of depositaries in monitoring the non-financial commitments of funds.

The AMF found that the five institutions inspected had put in place important and increasing human and technical resources to define, review, manage and monitor non-financial contractual commitments. Furthermore, although their ESG rating systems were often developed by the AMCs themselves, they remain dependent on external ESG data providers. Only one of the five AMCs checks the quality of this non-financial data before it is incorporated into the ESG rating algorithm.

The summary highlights the inadequacy of permanent controls to justify corrections made to ESG ratings calculated by the rating algorithm (known as override). Only 40% of the AMCs on the SPOT panel have a satisfactory process for this diligence.

With respect to the creation and review of the investment universe for ESG/SRI funds, the AMF found that the five AMCs inspected used a team that was independent of the management activity. This practice is less common among the 176 AMCs from the questionnaire. The AMF also found that only two of the five AMCs concerned by the SPOT inspection carry out ex post checks to ensure that the investment universe is consistent with

the fund's ESG policy. The results of the questionnaire were similar (50% of the AMCs surveyed had implemented this type of control).

The summary also gives details of the checks carried out on compliance with commitments before and after investments. Of the 176 AMCs that responded to the questionnaire, 77% had implemented manual checks and 74% had implemented automatic checks (blocking for 65% of them). However, not all firms use a combination of these two types of checks. Conversely, the AMF found that four of the AMCs concerned by the SPOT inspection had a robust audit trail for the checks they carried out.

The summary also addresses two types of non-compliance with non-financial contractual commitments: active breaches, which are the result of a voluntary decision by management, and passive breaches linked to developments outside the AMC's control. Of the 176 AMCs included in the questionnaire, 55% did not identify any breaches of this type in 2020 or 2021. Furthermore, the volume of non-financial breaches reported to the AMF between January 2021 and March 2022 accounted for only 0.4% of the total volume of (financial and non-financial) breaches reported. The AMF stresses the need to continuously reinforce the control process of non-financial commitments, particularly given the reinforcement of regulatory requirements, and taking into account the risk of making misleading promises to investors if these commitments are not met.

The AMF notes that depositaries continue to play only a limited role in the process of monitoring compliance with non-financial contractual commitments, as only 30% of the 176 AMCs stated that they had discussed the subject with the depositaries of the funds they manage. In the SPOT panel, only one of the six depositaries in question is involved in ex-post monitoring of some of the funds' non-financial commitments. The AMF reminds depositaries of their responsibilities in monitoring compliance with these commitments, and reminds AMCs of the need to provide depositaries with the data required for these checks.

About the AMF
The AMF is an independent public authority responsible for ensuring that savings invested in financial products are protected and that investors are provided with adequate information. The AMF also supervises the orderly operations of markets.Visit our website https://www.amf-france.org/en URL = [https://www.amf-france.org/en]

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Summary of SPOT inspection on compliance with non-financial contractual commitments by portfolio asset management companies

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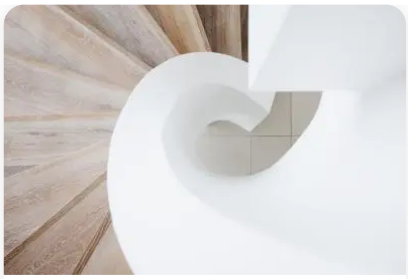

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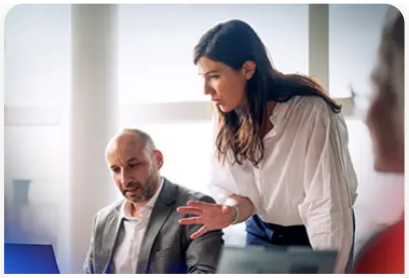

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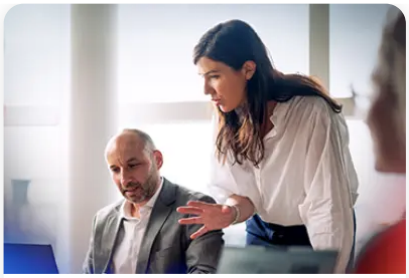

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