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**SUMMARY OF SPOT INSPECTIONS
ON THE SRI MANAGEMENT
SYSTEMS OF ASSET
MANAGEMENT COMPANIES AND
THE INTEGRATION OF ESG
CRITERIA**

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INTRODUCTION

As part of its new #Supervision2022 strategy, the AMF announced at the beginning of the year its intention to conduct briefer and more thematic "SPOT" inspections (*Supervision des Pratiques Opérationnelle et Thématique*), as well as its willingness to share the lessons learned from these exercises. Today it is publishing a summary of the SPOT inspections carried out between September 2018 and January 2019 on the SRI (Socially Responsible Investment) management systems of asset management companies. The SRI is an investment that aims to reconcile economic performance with social and environmental impact by financing companies and public entities that contribute to sustainable development regardless of their sector of activity. By influencing the governance and the behaviour of actors, the SRI promotes a sustainable economy. The SPOT inspections analysed the funds for which the SGP spotlights a SRI management, whether or not these funds are labelled.

These inspections covered Articles 18 (1 and 3), 37, 39, 40, 57(1)(c), 60(2)(f), 61(1), 61(2) and 62 of Commission Delegated Regulation (EU) No. 231/2013, Articles L. 533-22-1, L. 533-22-2-1 and D. 533-16-1 of the Monetary and Financial Code and Articles 319-21, 319-22, 319-23, 321-23 (IV), 321-30, 321-31, 321-35, 321-78, 321-101 (6 and 8), 321-132, 321-133 and 321-134 of the AMF General Regulation.

This summary does not constitute a policy element. It constitutes neither a position nor a recommendation. It describes the good practices identified in the SRI measures of the five asset management companies inspected and gives regulatory reminders related to the detected nonconformities. It does not herald future legislative and regulatory changes on the European and national levels.

1 SCOPE AND METHOD OF INSPECTIONS CARRIED OUT IN 2018

The professional obligations of asset management companies (AMCs) regarding SRI consist mainly of reporting requirements with respect to investors. For example, since 2011 AMCs are required to publish the ways in which social, environmental and governance quality (ESG) criteria¹ objectives² can be taken into account in their investment policy. The implementing decree for the "TECV" energy transition law (*Transition Énergétique pour la Croissance Verte*) extended and detailed the information to be provided for each of the ESG criteria.³ The reporting requirement defined by this decree is commonly called "Article 173" with reference to the article of the TECV Law.

Over and above reporting obligations, and in light of the observations made during classical inspections,⁴ the

¹ Environmental, Social and Governance quality criteria: criteria used to evaluate the extra-financial quality of issuers and companies.

² Article L. 533-22-1 of the Monetary and Financial Code.

³ Article D. 533-16-1 of the Monetary and Financial Code.

⁴ The AMF had on that occasion noted the following shortcomings:

- (i) SRI procedures not up-to-date, insufficiently precise regarding the methodology adopted, the sources of the extra-financial data used, and the operating procedures making it possible to trace and justify the changes made to the ESG scores and their frequency;
- (ii) insufficient SRI information made available to investors;
- (iii) information content not sufficiently clear (transparency codes not taking into account changes in the methods and not mentioning

SPOT inspections that were carried out jointly in five AMCs examined in particular:

- the organisation of SRI measures and the means employed;
- the sufficiently operational nature of the investment and risk management procedures that regulate the SRI system;
- the SRI methodology established (data, ESG criteria, factoring in climate risk, rating of issuers, selection of securities,⁵ exclusion of securities, engagement policy,⁶ whether or not external suppliers are used);
- the consistency of the investment process with regard to internal procedures by means of a test on a sample of 4 to 6 securities in the portfolio of the funds managed by the AMC;
- whether the *ex ante* and *ex post* information provided to investors is satisfactory;
- the internal control system established on the SRI theme.

The investigations covered the period from 1 January 2016 to 31 December 2018 and focused on the equity fund management of the AMCs in question. The five AMCs in the sample are very diverse in terms of size (from a few hundred million euros to several tens of billions of euros in AUM⁷) and organisation. They were selected because of the SRI management adopted, which they claim in their presentations to investors.

2 MAIN FINDINGS FROM THE INSPECTIONS

SUMMARY

Organisation of SRI measures and means employed:

Two AMCs chose a Best-in-class⁸ SRI approach, while the remaining three AMCs adopted a Best-in-universe⁹ SRI approach. The inspected AMCs have adopted a uniform approach for the socially responsible management of the entire range of managed funds. The allocation of human resources and deployment of technical resources by the AMCs reflect the diversity of the SRI methodologies adopted and the range of funds managed. Lastly, four

all the selected extra-financial data providers, fund monthly reports and annual reports that are imprecise or not very detailed regarding the SRI aspect, imprecise engagement report, fund-specific information which is not disclosed);

(iv) a lack of formalisation and traceability of the SRI investment process;

(v) a lack of precision and traceability of controls.

⁵ ESG selection: A SRI approach which consists of selecting or weighting issuers in a portfolio according to their extra-financial rating for three pillars: Environment, Social and Governance.

⁶ Shareholder engagement involves investors using their rights as shareholders to influence companies with a view to Environmental, Social and Governance improvements via direct dialogue, exercising voting rights at annual general meetings or submitting resolutions when the dialogue is unsuccessful.

⁷ Assets under Management

⁸ Type of ESG selection consisting of giving priority to the issuers best rated from an extra-financial viewpoint within their sector of activity, without favouring or excluding one sector relative to the benchmark investable universe (e.g. components of a stock market index). This selection technique, very widespread in France, makes it possible to not shift too far away from market benchmarks.

⁹ Type of ESG selection consisting of giving priority to the issuers best rated from an extra-financial viewpoint irrespective of their sector of activity, and accepting sector biases, because the sectors which are considered more virtuous on the whole will be more heavily represented.

AMCs manage funds which obtained a label (the SRI label,¹⁰ the TEEC label,¹¹ and the Finansol label¹² for solidarity funds, Luxembourg labels¹³). One AMC did not have its SRI funds labelled but merely opted for the AFNOR certification of the SRI approach for the group to which it belongs;¹⁴ the ESG process of this AMC is based on the financial expertise of its shareholder.

Investment and risk management policy/procedures governing the SRI measures:

Three of the five AMCs have an investment procedure describing the SRI measures established. However, one AMC has no investment procedure. Another AMC relies on a procedure of its shareholder which has not been specifically designed for the SRI funds managed by said AMC.

Only one AMC has an ESG risk management policy, but the risk which is defined there is basically a non-compliance risk (failure by the AMC to comply with its socially responsible commitments which could result in reputational damage and loss of the SRI label on its funds), and moreover the procedure does not indicate how this risk is managed.

For the AMCs as a whole, neither the procedures nor the risk management policy mention controls on data providers. However, the procedure of one AMC mentions a control on the service provider in charge of the exercise of voting rights.

Reminder of the applicable regulation

➤ AMCs shall establish and maintain appropriate operational policies and procedures to detect any risk of non-compliance with their professional obligations.¹⁵ In particular, they shall establish appropriate internal procedures for undertaking investment for each managed UCITS or AIF¹⁶ in order to ensure compliance of the investment decisions taken for the UCITS or AIF with the objective, investment strategy adopted and risk limits of the UCITS or AIF and in order to ensure that the selection and ongoing monitoring of

¹⁰ The SRI label, launched by the Ministry of Finance in August 2016, is a tool to make socially responsible and sustainable investments more visible to investors in France and Europe. The SRI label is granted by the certifier (AFNOR Certification or Ernst & Young) for a three-year period (renewable) during which the certifier carries out interim inspections to check that the fund continues to comply with the requirements of the label. According to the AFG website, the amount of assets under management in SRI-labelled funds exceeded €47 billion on 19 December 2018. In all, 39 asset management companies and 178 funds have obtained the SRI label.

¹¹ Launched at end-2015 by the French Ministry of the Environment, Energy and the Sea, the TEEC label (for *Transition Énergétique et Ecologique pour le Climat*), now Greenfin, is a tool to guarantee to investors that the labelled investment funds are committed to financing the green economy and to ecological and energy transition. AFNOR Certification, Ernst & Young and Novethic are the certification organisations for funds applying for the TEEC label. According to the Ministry of Ecology's website, in June 2018 19 funds were labelled for a total amount of about €3bn.

¹² Label existing since 1997 and issued by the association of the same name for solidarity-based savings schemes proposed by asset management companies, credit institutions and mutual insurance companies. The aim of solidarity-based savings schemes is to finance companies working mainly in the following fields: access to employment and housing, and support for ecological activities and entrepreneurship in developing countries.

¹³ Launched in 2014, this label created by the Luxembourg Fund Labelling Agency ("LuxFlag") is intended for investment funds meeting specific criteria concerning compliance with environmental, social and governance goals.

¹⁴ In this respect, it should be noted that there is no regulatory obligation regarding labelling, but merely a recommendation: "*The AMF recommends that any fund marketed in France and wishing to promote its SRI aspects publish a document that clarifies its approach, modelled on the European Transparency Code, or adhere to a charter, code or label that factors in criteria relating to the achievement of social, environmental or governance quality objectives. The AMF recommends that non-financial reporting (whether or not it is incorporated into traditional financial reporting) be easily accessible from web pages dedicated to SRI funds and that it be updated at least once a year.*" - See AMF Position-Recommendation 2011-24 "*A Guide to drafting collective investment marketing materials and distributing collective investments*".

¹⁵ Article 61(1) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-30 of the AMF General Regulation (UCITS).

¹⁶ Article 60(2)(f) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-35 of the AMF General Regulation (UCITS).

investments are performed with a high level of diligence.¹⁷

- AMCs shall establish and maintain a permanent risk management function, risk management policies and procedures.¹⁸ The risk management policy shall be appropriate and documented in order to address all the relevant risks to which the UCITS or AIFs managed by the AMC are or may be exposed. It shall enable the AMC, for each UCITS or AIF that it manages, to assess the exposure of said UCITS or AIF to any other risk, including operational risk, which could be significant for said UCITS or AIF.¹⁹
- AMCs shall establish detailed voting policies to set out the terms and conditions in which they intend to exercise the voting rights attached to the securities held by UCITS or AIFs that they manage.²⁰

Good practices

- Having a precise, operational and appropriate investment procedure, with regard in particular to the practical conditions of implementation of the methods for investment in and divestment of directly held shares or funds, and a description of the functioning of the list of exclusion of issuers from the investment universe.

Methodology adopted:

Environmental, social and governance (ESG) criteria:

The five AMCs use E, S and G criteria simultaneously. However, the AMCs have established very different methodologies.

One AMC has developed a qualitative evaluation system.

The remaining four AMCs have established a quantitative ESG evaluation, each being based on a particular methodology:

- a methodology based on a client satisfaction score supplemented by an analysis of the ESG criteria;
- a methodology based on verification of the consistency between the strategy stated by the company's management and the ESG data collected from it directly via an annual questionnaire. This AMC has thus established an internal ESG database concerning all the stakeholders in the company (staff, environment, clients, suppliers, partners, charitable and tax contributions, shareholders and governance);
- a methodology using ESG criteria of several data providers depending on the size of the issuers;
- a methodology developed by its shareholder based on ESG criteria of several data providers.

It should also be noted that the methodologies of two AMCs rely on evaluations based on the risks and opportunities related to the products/services proposed by the issuer, to its processes or to the sector.

In the event of downgrading of the ESG security rating, the managers shall exit the security within a fixed time limit of three (3) months.

Good practices

- Basing the SRI approach both on the risks related to the products and services proposed by the issuer and on the opportunities linked to the issuer's processes with regard to ESG issues.

¹⁷ Article 18 (1 and 3) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-101 (6 et 8) of the AMF General Regulation (UCITS).

¹⁸ Articles 39 and 40 of Delegated Regulation (EU) No. 231/2013 (AIF) and Articles 321-77 and 321-78 of the AMF General Regulation (UCITS).

¹⁹ Article 40 of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-78 of the AMF General Regulation (UCITS).

²⁰ Article 37 of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-132 of the AMF General Regulation (UCITS).

- Providing from the outset, as part of the investment policy, for monitoring of the eligibility over time of the securities in the portfolio and the exit, within a fixed time limit, of securities no longer complying with the ESG criteria (in this case three months).

Data:

The AMCs inspected use data from three of the four big data providers in the world. One of the AMCs inspected also uses the services of a company specialised in rating small and medium-sized companies, listed or unlisted.

Allowance for climate risk:²¹

The five AMCs inspected use several levers to allow for climate risk:

- divestment from companies whose business is based on coal or the most carbon-intensive companies;
- reduction of the carbon footprint of portfolios;
- investment in green solutions.

The five AMCs evaluate the carbon footprint of the companies present in the funds' portfolios: one AMC collects the data directly from the company, while the remaining four AMCs use the data from outside service providers. Three AMCs use both the direct CO₂ emissions resulting from the combustion of fossil fuels (scope 1), the emissions resulting from the purchase or production of electricity (scope 2), and other indirect emissions (scope 3). One AMC does not take into account scope 3. One AMC does not take into account scope 2.

Shareholder engagement policy:

For the five AMCs, engagement takes the form of a dialogue with the companies present in the funds' portfolio and a vote at those companies' annual general meetings.

Four AMCs have either a common voting and engagement procedure or separate engagement procedure and voting procedure. These procedures are available on the AMC website. One AMC has no engagement policy and relies on that of its shareholder.

The five AMCs vote at all the annual general meetings (AGMs) of the companies in the funds' portfolio, either by correspondence, on a voting platform, or by attending the AGM. Four AMCs rely on specialist agencies to vote at AGMs.

Good practices

- Sharing the shareholder engagement experience with other AMCs regarding ESG criteria.
- Reporting to those companies that so wish the ESG analyses performed and their positioning relative to the other companies in a given sector free of charge.
- In dialogue with issuers, focusing on the ESG criteria announced to clients.

Consistency of the investment process with regard to internal procedures:

The SPOT inspection team carried out for each AMC a test to verify the compliance of practical implementation

²¹ Climate risk (source: <https://www.actu-environnement.com/ae/news/risque-climat-finance-arsenal-legislatif-canfin-grandjean-24792.php4>) includes:

- carbon risk: how the business model of the company in which the fund has invested is impacted by the establishment of a carbon price, a cap on emissions or a normative constraint limiting greenhouse gas emissions;
- the risk of impacts of climate change: how a certain supply chain or a certain infrastructure is impacted by rising waters or by this or that other consequence of climate change.

of the investment and security monitoring policy with the system of procedures. For each AMC, it selected four to six securities which represented more than 1% of the net asset value of two or three funds as at 28 September 2018.

In general, for the four AMCs, their investment processes comply with the procedural arrangements.

However, the stages of dialogue with the issuer, inclusion in the SRI universe and the investment decision are not systematically documented. Four AMCs had no dialogue with the issuers for certain securities before the investment decision. One AMC has not formalised the inclusion of two securities. Sometimes, the investment and divestment decisions for directly held shares or funds are not formalised.

The inspection team noted that the portfolios of the funds of three AMCs contain securities of issuers whose carbon footprint is high (e.g. issuers in the automotive sector or local utilities or chemicals firms), but without any conflict with the established SRI policy.

Moreover, the inspection team noted that, as at 30 April 2018, 16% of the assets of the fund of one AMC were not part of the eligible SRI universe but constituted a legacy of the funds acquired and/or transformed since 2013, which was not foreseen in the investment procedure.

Good practices

- Holding regular dialogue with the issuers and performing follow-up of this dialogue to measure their impacts, while complying with the principle of proportionality.
- Establishing a formal and exhaustive audit trail of the investment and divestment process to ensure consistency between the investment policy, the methodology announced to investors and the process applied in practice. The audit trail thus makes it possible to understand the due diligence performed to analyse the security, the criteria for awarding the rating, the reasons for including the security or the fund in the portfolios, how the investment decision was taken, and by whom, dialogue with the issuer before inclusion in the SRI universe and after the investment decision, the updating of the rating, the AMC's votes at the issuer's AGMs, allowance for climate risk (e.g. by measuring the carbon footprint).

Reminder of the applicable regulation

- AMCs shall maintain operational policies and procedures,²² notably those established in order to ensure the compliance of investment decisions with the investment strategies adopted and to ensure that the selection and ongoing monitoring of investments are performed with a high level of diligence.²³

Information provided to investors:

The information disclosed to investors is multi-faceted. In general, for all the AMCs, the information disclosed to the fundholders is consistent from one document to another. However, as discussed below, the information presented in a given document is sometimes incomplete and not very clear.

²² Article 61(1) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-30 of the AMF General Regulation (UCITS).

²³ Article 18 (1 and 3) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-101 (6 et 8) of the AMF General Regulation (UCITS).

Moreover, the inspection team noted a fairly broad heterogeneity in the AMCs' practices concerning the publication and quality of the information disclosed to investors.

Concerning ex ante information:

The information contained in the prospectuses/KIIDs of the funds managed by three AMCs is incomplete. In the case of one of these three AMCs, neither the prospectus nor the KIID mentions that the management objective is to implement a SRI strategy.

For a single AMC, the prospectuses/KIIDs of the funds present the portfolio's investment strategy, the SRI approach applied, and the providers of the data used, the type of criteria taken into account and the type of companies selected. Moreover, the prospectuses of this AMC mention that the management objective is to implement a SRI strategy.

In general, for the five AMCs, the Transparency Codes,²⁴ available on the AMCs' website, describe the ESG evaluation methodology of the issuers and the choices adopted for the selection of ESG criteria. The codes of three AMCs mention the names of the extra-financial data providers selected. Two AMCs present the control and reporting system. Three AMCs have Transparency Codes for each fund; one AMC has a common Transparency Code for its funds; one AMC has Transparency Codes for each investment category. Finally, one AMC publishes sector sheets presenting maps of sustainable development issues according to the opportunities and risks, and a summary sheet of the issues. Two AMCs report both on the number of companies in the initial universe based on which the SRI analysts perform the ESG reviews and on the number of securities after application of the exclusion filters, which makes it possible to assess the selectivity of the ESG strategy.

One AMC publishes the engagement policy in the "legal notice" section.

Concerning ex post information:

Two AMCs have established very detailed reporting security by security, resolution by resolution (and fund by fund for one of the two AMCs), which enables the client to know the resolutions passed for the securities in the portfolio of the fund held.

However, the following point of attention should be highlighted: for all the AMCs, the reports on the exercise of voting rights do not enable the investor to know whether a resolution has been ultimately adopted or not, nor do they mention what the weight of the AMC is in the voting rights.

One AMC does not publish²⁵ engagement report although its engagement policy mentions the existence of an engagement table which recaps, for each of the securities, the engagement date, the person in charge of dialogue, the means used, the theme of the dialogue and a comment on follow-up of the dialogue action.

The presentation of the "Article 173" reports is very heterogeneous. In general, for all the AMCs, the scope of

²⁴ The Transparency Code is compulsory for all SRI funds open to the public managed by asset management companies that are members of the AFG (French asset management association) or the FIR (French sustainable investment forum). By adhering to this code, asset management companies agree to answer the questions asked for each of the SRI funds open to the public that they manage.

²⁵ Document reporting on how the AMC exerts its influence with a view to better allowance for sustainable development issues in financial markets. The objective of the engagement report is to list the actions carried out by an AMC on all the asset classes that it manages and with all the market participants: the marketplace, the regulators and the companies in the portfolio.

the ESG analysis is clearly defined. One AMC publishes an AMC "Article 173" report that is not very clear and not highly structured (presentation of a long list of indicators without any other details, relatively unsubstantiated presentation of the rating process). Another AMC did not publish "Article 173" reports for funds for which the assets under management exceeded €500m. Only two of the five AMCs present the proportion of AUM dedicated to SRI.

The inspection team also found that only one AMC reports, within the framework of "Article 173" reporting, on the funds' contribution to compliance with targets for limiting global warming and for the energy and ecological transition.

The inspected companies do not delegate the analysis of their portfolios and the drafting of their "Article 173" reports to third parties.

The monthly report on the funds of one AMC presents information on stock picks, on the latest movements, an analysis of the fund's portfolio rating by comparing it with the investment universe, the entire portfolio together with the weight of each security in the fund's assets, and the ESG rating and sources of the data presented.

This AMC publishes carbon footprint reports presenting the assessment of funds' carbon footprint, and a comparison of each fund's carbon footprint with the benchmark index (by sector), the sectors most exposed to carbon risk, the highest-emitting companies in the portfolios, and the transition²⁶ and physical²⁷ risks of the most exposed sectors.

This AMC also publishes a report on the social footprint of the funds: maps presenting the portfolio's exposure to social risks from both the sector and geographic viewpoints.

Good practices

- Presenting in the prospectuses/KIIDs the data service providers used, making sure that the information provided is updated where necessary. Alternatively, a reference can be made in the prospectuses/KIIDs to the Transparency Code or the "Article 173" report.
- Presenting all or part of the fund's inventory in the documents presenting the SRI approach, while complying with the rules in force regarding market timing and late trading²⁸.
- Providing information concerning the effectively discriminating nature of the extra-financial approach by a statement presenting the selectivity rate of the ESG strategy relative to an initial universe, specifying the number of issuers forming it, the differential between the initial universe and the number of stocks excluded after applying the exclusion filters, or again the number of stocks making up the fund's portfolio. As mentioned in the previous AMF report on sustainable finance,²⁹ *"Given the limitations of the selectivity ratio and how difficult it is for non-professional investors to understand the impact of ESG methodologies on the*

²⁶ Transition risks result from the adjustments made with a view to a transition to a low-carbon economy, especially when they are not very well anticipated or take place abruptly.

²⁷ Physical risks result from the damage caused directly by meteorological and climatic phenomena.

²⁸ This practice is an extension of the good practice in the AMF report on socially responsible investment in collective investment schemes published in December 2017, according to which: *"A growing number of management companies explain the impact of ESG methodology on the portfolio in the marketing materials provided to investors. Management companies can, in particular, provide investors with the inventory of the stocks held in SRI UCIs' portfolios on a dedicated page of their websites on a half-yearly basis, while obeying the current market timing and late trading rules (AMF position DOC-2004-07)."*

²⁹ AMF report on socially responsible investment in collective investment schemes, published in December 2017.

makeup of funds, the AMF invites management companies to be more educational in their communication with their non-professional investors".

- Performing reporting on the exercise of voting rights fund by fund (and not for all funds combined), specifying, for each of the securities in the portfolio, the list of resolutions.³⁰
- Presenting fund by fund the companies emitting most CO₂, by defining the various scopes considered.
- Specifying in the engagement report the universe of companies concerned by the engagement (proportion of companies with which the AMC has initiated a dialogue), the themes of the engagement policy and the actions for following up on this engagement.
- Grouping the documents concerning engagement in a section easily accessible on the website.³¹
- Presenting in a few pages in the funds' reports (annual reports, or even also half-yearly reports), the most relevant information concerning the characteristics of the fund, the methodology for selection of assets, and the SRI approach.

Reminder of the applicable regulation³²

- The "Article 173" report must describe clearly³³ the nature of the ESG criteria taken into account, the information used for analysis of the issuers on the basis of ESG criteria, the methodology for the analysis conducted on the ESG criteria and its results, and how the results of the analysis performed are incorporated in the investment policy.
- The "Article 173" report must list the managed funds, simultaneously taking into account ESG criteria, specifying, as a percentage, the weight of these funds' AUM in the total amount of the AMC's AUM.
- When the AMC manages funds for which the AUM exceed €500m, it must establish an "Article 173" report for each of those funds.

Control system:

The inspection team analysed the second-level controls concerning the SRI issue: controls relating to the investment process, controls relating to outside service providers (excluding voting rights), controls on the exercise of voting rights, controls on conflicts of interests, and controls relating to the information provided to investors.

The AMCs do not perform second-level controls concerning the quality of ESG data. One AMC proposed deploying an AFG working group to analyse this subject. Only one AMC performs a control on the exercise of voting rights. Only one remaining AMC has established a second-level control aiming to ensure that exchanges with the companies in the funds' portfolios generate no conflicts of interests liable to affect its free exercise of voting rights and ultimately the interest of the unitholder. A third AMC performs no control on the SRI commercial documentation.

³⁰ This practice is an extension of the good practice in the AMF report on socially responsible investment in collective investment schemes published in December 2017, according to which: "The publication by AMCs on their website of the votes on resolutions presented during the general meetings of companies whose securities they holds in portfolios (especially if the security accounts for more than 1% of a fund's portfolio) is a good practice observed by the AMF."

³¹ This practice is an extension of the good practice in the AMF report on socially responsible investment in collective investment schemes published in December 2017, according to which: "To make it easier to access this information, the AMF recommends publishing information about the entity (paragraph II, sub-paragraph 1 of article D. 533-16-1 of the COMOFI) in a single document that is easily accessible on the AMC's website (e.g. through links on pages discussing sustainable development issues) and written in French if the AMC targets non-professional investors in France"

³² Article D. 533-16-1 of the Monetary and Financial Code.

³³ Article L. 533-22-2-1 of the Monetary and Financial Code.

The formal presentation and documentation of control work are highly satisfactory for two AMCs. They are insufficient for two remaining AMCs. In the case of the fifth AMC, the controls are performed, but the inspection team noted that they lack formalisation.

Reminder of the applicable regulation

- AMCs shall establish and maintain adequate operational internal control mechanisms to secure compliance with decisions and procedures at all levels of the AMC.³⁴
- AMCs shall establish and maintain an operational permanent and effective compliance function which, in particular, monitor and, on a regular basis, assess the adequacy and effectiveness of the measures, policies and procedures established and actions taken to remedy any deficiency in compliance with their professional obligations.³⁵

2.1 ORGANISATION OF SRI MEASURES AND MEANS EMPLOYED

Two AMCs chose a Best-in-class SRI approach, while the remaining three AMCs adopted a Best-in-universe SRI approach. The ESG process of one AMC is based on the financial expertise of its shareholder. The inspected AMCs all adopted a uniform approach to SRI management for the whole product range.

The allocation of human resources and deployment of technical resources by the AMCs reflect the diversity of the SRI methodologies adopted by the AMCs and the range of managed funds.

Regarding human resources, one AMC has a team consisting of 80 personnel (specialists in thematic investment management, engineers, financial and ESG analysts, and project financing and solidarity finance professionals) broken down into three teams: SRI/ESG research (10 ESG analysts), equity investment (9 managers, 2 analysts, 1 assistant manager), fixed-income investment (2 managers, 1 analyst, 1 assistant manager).

Conversely, one AMC has a single manager of ESG development. At the same time, it is supported by the financial expertise of 17 outside analysts.

The remaining three AMCs have teams of analysts consisting of about three people.

Regarding technical resources:

- Three AMCs rely on extra-financial environmental, social and governance data from outside providers;
- One AMC has developed an in-house extra-financial database;
- Another relies on data collected by survey institutes or directly from companies via a questionnaire;
- One AMC delegates votes to its shareholder, while the remaining four AMCs rely on voting service providers;
- For measuring the carbon footprint, one AMC collects data directly from companies. The remaining four AMCs rely on an outside service provider.

³⁴ Article 57(1)(c) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-23 (IV) of the AMF General Regulation.

³⁵ Article 61(2)(a) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-31 of the AMF General Regulation.

The AMCs manage funds which obtained³⁶ the public SRI label, the TEEC label (renamed Greenfin), the Finansol label for solidarity funds, and Luxembourg labels (LuxFlag Environnement and ESG) issued by the Luxembourg Fund Labelling Agency. On the other hand, one AMC opted for the AFNOR certification of its shareholder's SRI procedure.

2.2 INVESTMENT AND RISK MANAGEMENT POLICY/PROCEDURES GOVERNING THE SRI MEASURES

One AMC has no investment procedure. However, this AMC describes the investment process, in an operational manner, in the Transparency Code.

One AMC relies on its shareholder's procedure. The scope of the latter is very general, covering all the portfolios managed by the group's subsidiaries without taking into account the specific risk of SRI funds managed by said AMC.

For the funds selected by the inspection team, one AMC has dedicated investment procedures which are operational. They describe all the stages of ESG opinion building and the various outside data sources used. The long-term and sustainable aspect of the investment is taken into account at all stages of the investment process and in the AMC's governance. Moreover, this investment procedure mentions the performance of nine controls related to the SRI investment process, including one control on the financial and extra-financial data appearing in the monthly and annual reports.

For the remaining two AMCs, the system of investment procedures relating to SRI is documented to varying degrees:

- The investment procedure of the funds of one AMC is confined to describing the objective and investment strategy of each of the funds. It does not describe the operational stages of the investment process nor the controls to be executed as part of the investment process;
- For the last AMC, the system of SRI investment procedures is based on various procedures updated in 2018 and is well documented.

Regarding the specific SRI risk of the managed funds, only one AMC has a risk management policy to monitor ESG risk, but the risk which is defined there is basically a non-compliance risk (failure by the AMC to comply with its socially responsible commitments which could result in reputational damage and loss of the SRI label on its funds), and moreover the procedure does not indicate how this risk is managed.

For the five AMCs, neither the risk management procedures nor policy mention controls on data providers. However, the procedure of one AMC mentions a control on the service provider in charge of the exercise of

³⁶ In AMF Position-Recommendation 2011-24 "A Guide to drafting collective investment marketing materials and distributing collective investments", the AMF "recommends that any fund marketed in France and wishing to promote its SRI aspects publish a document that clarifies its approach, modelled on the European Transparency Code, or adhere to a charter, code or label that factors in criteria relating to the achievement of social, environmental or governance quality objectives. The AMF recommends that non-financial reporting (whether or not it is incorporated into traditional financial reporting) be easily accessible from web pages dedicated to SRI funds and that it be updated at least once a year."

voting rights.

Reminder of the applicable regulation

- AMCs shall establish and maintain appropriate operational policies and procedures to detect any risk of non-compliance with their professional obligations.³⁷ In particular, they shall establish internal procedures for undertaking investment for each managed UCITS or AIF³⁸ in order to ensure compliance of the investment decisions taken for the UCITS or AIF with the objective, investment strategy adopted and risk limits of the UCITS or AIF and in order to ensure that the selection and ongoing monitoring of investments are performed with a high level of diligence.³⁹
- AMCs shall establish and maintain a permanent risk management function, risk management policies and procedures.⁴⁰ The risk management policy shall be appropriate and documented in order to address all the relevant risks to which the UCITS or AIFs managed by the AMC are or may be exposed. It shall enable the AMC, for each UCITS or AIF that it manages, to assess the exposure of said UCITS or AIF to any other risk, including operational risk, which could be significant for said UCITS or AIF.⁴¹
- AMCs shall establish detailed voting policies to set out the terms and conditions in which they intend to exercise the voting rights attached to the securities held by UCITS or AIFs that they manage.⁴²

Good practices:

- Having a precise, operational and appropriate investment procedure, with regard in particular to the practical conditions of implementation of the methods for investment in and divestment of directly held shares or funds, and a description of the functioning of the list of exclusion of issuers from the investment universe.

2.3 THE METHODOLOGY ESTABLISHED

Environmental, social and governance (ESG) criteria:

The five AMCs use E, S and G criteria simultaneously. Two AMCs stated that they include in social criteria pay differences between male and female employees. However, the methodologies established are very different.

One AMC has developed a proprietary evaluation system based on a **qualitative** analysis designed to distinguish between sectors according to their degree of exposure to seven sustainable development issues classified in three categories:

- issues having an environmental impact: climate stability, healthy ecosystems, security of resources;
- issues having a social impact: fundamental needs, well-being, decent work;
- issues of financial materiality.

For this AMC, governance is treated transversely as a process which is a source of risk having a potential impact

³⁷ Article 61(1) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-30 of the AMF General Regulation (UCITS).

³⁸ Article 60(2)(f) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-35 of the AMF General Regulation (UCITS).

³⁹ Article 18 (1 and 3) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-101 (6 et 8) of the AMF General Regulation (UCITS).

⁴⁰ Articles 39 and 40 of Delegated Regulation (EU) No. 231/2013 (AIF) and Articles 321-77 and 321-78 of the AMF General Regulation (UCITS).

⁴¹ Article 40 of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-78 of the AMF General Regulation (UCITS).

⁴² Article 37 of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-132 of the AMF General Regulation (UCITS).

on all sustainable development issues.

The remaining four AMCs have established a **quantitative** ESG evaluation:

- One AMC has developed, over a period of more than 10 years, an investment methodology designed to identify the leaders in client satisfaction via questionnaires concerning ESG criteria with 44 survey institutes (outside data providers). According to this AMC, a high level of client satisfaction is a guarantee of a company's financial success via three levers: customer retention, recommendation and pricing power. Satisfied clients are loyal, they recommend the products, consume more and are less sensitive to the price criterion. Researching the company via the prism of clients makes it possible to have an overall understanding of it. For this AMC, companies which endeavour to meet the expectations of their clients are those that have social, governance and environmental values;
- The originality of the methodology of another AMC is to verify the consistency between the strategy stated by the company's management and the ESG data collected from it directly via an annual questionnaire. This AMC has thus established an internal ESG database concerning all the stakeholders in the company (staff, environment, clients, suppliers, partners, charitable and corporation tax contributions, shareholders and governance) for 167 European companies, with 123 indicators, over a period of 10 years;
- One AMC uses different environmental, social, societal and governance criteria depending on the size of the issuers in the portfolio. For SMEs, for example, this AMC relies on analyses and data from a service provider to select small and mid caps whose business generates human, social or environmental value added. Each year, the SRI team asks this service provider to perform a study on 15 companies, and organises a tripartite meeting with the service provider and the company. The SRI team presents a formal analysis of the selected companies based on four criteria (governance, social, environment, stakeholders) as part of a positive integration approach;
- One AMC uses the methodology developed by its shareholder based on 36 environmental, social and governance criteria. The ratings used are those of several data providers. These criteria take into account sector issues. The ratings on each of the pillars, environmental, social and governance, are aggregated and weighted to obtain the ESG rating;
- The methodologies of two AMCs rely on sector SRI evaluations based on the risks related to the products and services proposed by the issuer and on the opportunities related to the issuer's processes with regard to ESG issues. The methodology of one of the two AMCs is very detailed and links these evaluations to the Sustainable Development Goals.⁴³

In addition to the sector evaluations, the methodology of one AMC focuses on an analysis of companies' **sustainable development policies** according to the following ESG guidelines:

⁴³ Created in 2012 at the Rio Sustainable Development Conference, the Sustainable Development Goals ("SDGs") established by the UN Member States are a global appeal to act to eradicate poverty, protect the planet and ensure that all human beings live in peace and prosperity. Each of the 17 Goals is interdependent with the others, the success of one contributing to the success of the others. The SDGs are becoming a reference framework for investors looking for sustainable products having positive environmental and social impacts.

- the social policy conducted by the company;
- management of the environmental impacts related to its business;
- the governance employed, the quality of relationships established with suppliers and clients, and partnerships forged with the local communities in the locations where they are established.

It should also be noted that the ESG analysis of two AMCs is based on the **classification of generic strategies by the economist Michael Porter**⁴⁴ (analysis of the various strategic options open to the company in order to thereby obtain a competitive advantage).

Data:

Three of the AMCs inspected use data from three of the four big data providers in the world. One of the AMCs also uses the services of a company specialised in rating small and medium-sized companies, listed or unlisted.

Allowance for climate risk:

The five AMCs evaluate the carbon footprint of the companies present in the funds' portfolios. One AMC collects data concerning the carbon footprint directly from the company. The remaining four AMCs use data from outside providers.

Three AMCs use both the direct CO₂ emissions resulting from the combustion of fossil fuels (scope 1), the emissions resulting from the purchase or production of electricity (scope 2), and other indirect emissions (scope 3).

One AMC does not take into account scope 3. Another AMC does not take into account scope 2.

Rating of the issuers:

For the AMCs as a whole, updating of the investment universe is performed at least once a year. One AMC updates the ESG scores each month. The frequency of updating of the company's ESG evaluation is 12 to 36 months. In the event of a controversy concerning a company, its score can be updated and the investment universe adjusted.

Stock picking and exclusion of securities:

A single AMC performs an ESG analysis at the same time as a financial analysis. For the remaining AMCs, ESG analysis is performed ahead of the financial analysis of companies.

In the event of downgrading of the security rating, the inspection team noted that the fund managers of all the AMCs inspected have to exit the stock within a time limit of three months.

The practices regarding exclusions are also very different. Two AMCs perform no sector exclusion on principle. However, the rating level assigned to companies in a particular sector entails implicit exclusions. One AMC carries out exclusions based on the company's sector and business (e.g. a company specialised in coal mining). It may also exclude companies at the specific request of clients. For one AMC, whether or not companies are excluded from funds' portfolios depends on the fund's investment objective.

⁴⁴ Professor of Business Strategy at Harvard University and business consultant.

Lastly, one AMC excludes companies according to very specific criteria. Apart from an exclusion⁴⁵ required by law, one AMC applies an exclusion filter to the companies concerned by the following criteria:

- proven controversies in the field of human rights;
- unassisted dismissal practices in the past three years;
- refusal to disclose extra-financial and/or financial information, or else deliberately irrelevant or dilatory replies by the company.

Shareholder engagement policy:

For the five AMCs, engagement takes the form of a dialogue with the companies and a vote at the annual general meetings of the companies in the funds' portfolio.

Four AMCs have either a common voting and engagement procedure or a separate engagement procedure and voting procedure. These procedures are available on the AMC's website. One AMC has no engagement policy and relies on that of its shareholder.

The five AMCs vote at all the annual general meetings (AGMs) of the companies in the funds' portfolio, either by correspondence, on a voting platform, or by attending the AGM. Four AMCs rely on specialist agencies to vote at AGMs.

One AMC discloses to those companies that so wish their relative positioning compared with companies in the same sector.

Two AMCs have established shareholder coalition systems that can strengthen the impact of the AMCs' voting policies at annual general meetings. In one of the two AMCs, the team of SRI analysts shares its shareholder engagement experience with other European AMCs via a European network that it has founded with six European AMCs. This network allows member companies to take part jointly in annual general meetings, co-sign letters to companies, meet companies and exchange information on their respective engagements. The SRI team makes available to the European network its research and analyses on companies based in France. Conversely, the SRI team has experience feedback on shareholder engagement from the members of the network located in other European countries concerning companies located outside France. The same AMC forwards analyses ("pleas") to the institutions called on to establish the SRI standards in order to help improve and develop the SRI market. In this case, the AMC, alone or with other investors, is engaged with professional associations, politicians and NGOs.

ESG criteria:

Good practices

- Basing the SRI approach both on the risks related to the products and services proposed by the issuer and on the opportunities linked to the issuer's processes with regard to ESG issues.
- Providing from the outset, as part of the investment policy, for monitoring of the eligibility over time of the securities in the portfolio and the exit, within a fixed time limit, of securities no longer complying with the ESG criteria (in this case three months).

Shareholder engagement policy:

Good practices

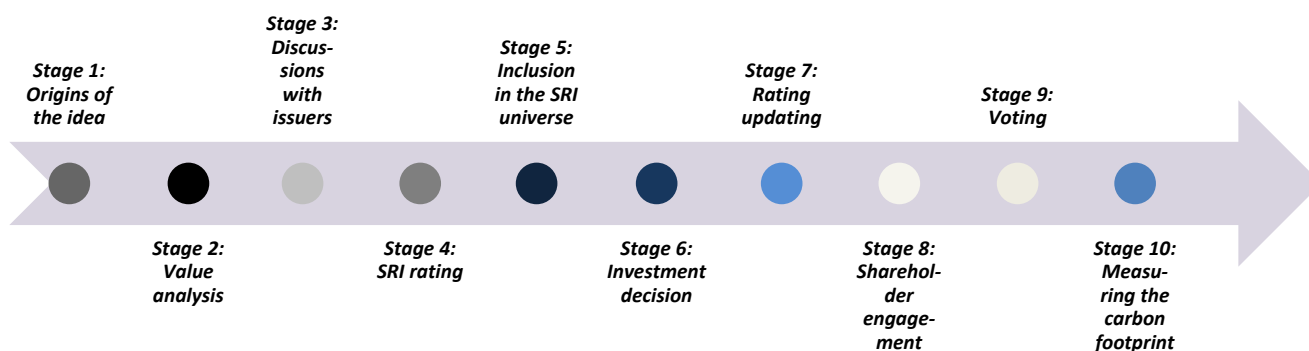
⁴⁵ A direct relationship with activities related to cluster bombs and anti-personnel mines.

- Sharing the shareholder experience with other AMCs regarding ESG criteria.
- Reporting to those companies that so wish the analyses performed and their positioning relative to the other companies in a given sector free of charge.
- In dialogue with issuers, focusing on the ESG criteria announced to clients.

2.4 CONSISTENCY OF THE INVESTMENT PROCESS WITH REGARD TO INTERNAL PROCEDURES

The inspection team carried out for each AMC a test to verify the compliance of practical implementation of the investment and security monitoring policy with the system of procedures. For each AMC, it selected four to six securities which represented more than 1% of the net asset value of two or three funds as at 28 September 2018.

The inspection team analysed the 10 stages in the investment process.



In general, for the four AMCs, their investment processes comply with the procedural arrangements.

However, the stages of dialogue with the issuer, inclusion in the SRI universe and investment decisions are not systematically documented. Three AMCs had no dialogue for certain securities in the funds' portfolio before the investment decision. One AMC has not formalised the inclusion of two securities entered in the portfolio recently. Sometimes, investment decisions are not formalised.

Stage 1 - Origins of the idea:

Either the SRI team is the originator of the idea to include the security in the portfolio, or the fund manager has decided to invest in the security which has passed the SRI filter, or the SRI team and the investment management team have together decided to include the security, or an outside company has recommended investing in the security.

Stage 2 – Value analysis:

The SRI and investment management teams analyse securities systematically. They formalise the value analysis by writing a note.

Stage 3 – Dialogue with issuers:

Dialogue is formalised via emails, phone discussions and participation in conferences. One AMC communicates systematically with companies whose shares are in its portfolio, regarding the three main aspects of its

engagement policy. It has regular dialogue with issuers, at least once a year. The only AMC which communicates frequently with issuers already did so before investing. However, the remaining four AMCs had no dialogue for certain securities in the funds' portfolio before the investment decision.

Stage 5 - Inclusion in the SRI universe:

For all the AMCs in the sample group, the inclusion of securities in the portfolio is formalised via the investment committee's report. However, one AMC has not formalised the inclusion of two securities.

Stage 6 - Investment decisions:

These decisions are a matter for the fund manager. For the five AMCs, investment decisions are not formalised.

Stage 7 - Updating of security ratings:

The rating of securities is updated correctly. However, the frequency of rating updates is not always complied with.

Stage 8 – Shareholder engagement:

Four AMCs did not initiate shareholder engagement for seven securities in all.

Stage 9 - Voting:

The AMCs vote at AGMs either through a physical presence or by sending a voting form.

One AMC is very active in its shareholder policy with companies. It also had discussions with brokers. For example, for the AGM of one security in 2017, the AMC voted differently than its shareholder.

Stage 10 - Measuring the carbon footprint:

The AMCs measure the carbon footprint of the selected securities. Four AMCs collect the carbon footprint for year n-1, and one AMC for year n-2.

The inspection team noted that the funds' portfolios contain securities of issuers whose carbon footprint is high (e.g. issuers in the automotive sector or local utilities or chemicals firms), but without any conflict with the established SRI policy.

Moreover, the inspection team noted that, as at 30 April 2018, 16% of the assets of a fund of one AMC were not part of the eligible SRI universe but constituted a legacy of the funds acquired and/or transformed since 2013, which was not foreseen in the investment procedure.

Good practices

- Holding regular dialogue with the issuers and performing follow-up of this dialogue to measure their impacts, while complying with the principle of proportionality.
- Establishing a formal and exhaustive audit trail of the investment and divestment process to ensure consistency between the investment policy, the methodology announced to investors and the process applied in practice. The audit trail must make it possible to understand the due diligence performed to analyse the security, the criteria for awarding the rating, the reasons for including the security or the fund

in the portfolios, how the investment decision was taken, and by whom, dialogue with the issuer before inclusion in the SRI universe and after the investment decision, the updating of the rating, the AMC's votes at the issuer's AGMs, and allowance for climate risk (e.g. by measuring the carbon footprint).

Reminder of the applicable regulation

➤ AMCs shall maintain operational policies and procedures,⁴⁶ notably those established in order to ensure the compliance of investment decisions with the investment strategies adopted and to ensure that the selection and ongoing monitoring of investments are performed with a high level of diligence.⁴⁷

2.5 INFORMATION PROVIDED TO INVESTORS

The information disclosed to investors is multi-faceted.

	Required information	Non-required information
Ex ante information		
	Prospectus/KIID	Product data sheet
	Transparency Code	Issues fact sheet
	Voting and engagement policy	Research report
	Investment policy/ESG policy	
Ex post information		
	Funds' annual report and half-yearly report	Funds' monthly or weekly report
	"Article 173" report of the AMC	Engagement report
	Funds' "Article 173" report	Report on the exercise of voting rights
	Inventory	Carbon footprint report
	Fund fact sheet	Social footprint report

For all the AMCs, the information is available to the public via the website. However, one AMC's report on the exercise of voting rights, located in the "Legal notice" section, is not easily accessible.⁴⁸

The inspection team notes that for the five AMCs, the information disclosed to the fundholders is consistent from one document to another. However, the information presented in a given document is sometimes incomplete and not very clear, as discussed below.

Moreover, the inspection team noted a fairly great heterogeneity of the AMCs' practices concerning the publication and quality of the information disclosed to investors.

Concerning ex ante information:

For a single AMC, the prospectuses/KIIDs of the funds present the portfolio's investment strategy, the SRI approach applied, and the providers of the data used, the type of criteria taken into account and the type of companies selected. The prospectuses of the funds of this AMC mention that the management objective is to implement a SRI strategy. For the remaining four AMCs, the information contained in the prospectuses/KIIDs of

⁴⁶ Article 61(1) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-30 of the AMF General Regulation (UCITS).

⁴⁷ Article 18 (1 and 3) of Delegated Regulation (EU) No. 231/2013 (AIF) and Article 321-101 (6 et 8) of the AMF General Regulation (UCITS).

⁴⁸ Recommendation No. 6 of the 2015 SRI Report: "The AMF recommends that non-financial reporting (whether incorporated into traditional financial reporting or not) be easily accessible from web pages dedicated to SRI funds and that it be updated at least once a year."

the funds managed by these AMCs is incomplete.

The Transparency Codes of the five AMCs describe the ESG evaluation methodology of the issuers and the choices adopted for the selection of ESG criteria. One AMC presents in the Transparency Code the complete list of funds (with the positions and the percentage of assets owned).

Three AMCs have Transparency Codes for each fund. One AMC has a common Transparency Code for its four funds. Another AMC has Transparency Codes for each investment management category. Two of the five AMCs present the control and reporting system. The codes of three AMCs mention the names of the extra-financial data providers selected. Two AMCs report both on the number of companies in the initial universe based on which the SRI analysts perform the ESG reviews and on the number of securities after application of the exclusion filters, which makes it possible to assess the selectivity of the ESG strategy.

Finally, one AMC publishes sector sheets presenting maps of sustainable development issues according to the opportunities and risks.⁴⁹

Concerning *ex post* information:

For all the AMCs, the reports on the exercise of voting rights do not enable the investor to know whether a resolution has been ultimately adopted or not, nor do they mention the weight of the AMC in the voting rights. Two AMCs have established very detailed reporting, security by security and resolution by resolution. One of the two AMCs has established reporting resolution by resolution and fund by fund, which enables the unitholder to know the resolutions passed for the securities in the portfolio of the fund held.

One AMC publishes in the engagement report the universe of companies concerned by the engagement (proportion of companies with which the AMC has initiated a dialogue), the themes of the engagement policy and the actions for monitoring this engagement. One AMC does not publish engagement reports although its engagement policy mentions the existence of an engagement table which recaps for each of the securities the engagement date, the person in charge of dialogue, the means used, the theme of the dialogue and a comment on follow-up of the dialogue action.

The presentation of the "Article 173" reports is very heterogeneous. One AMC has not established separate "Article 173" reports for the asset management company and for the managed funds. Another AMC publishes an "Article 173" AMC report that is not highly structured. Another AMC did not publish "Article 173" reports for funds for which the assets under management exceed €500m.

The inspection team also found that only one AMC reports, within the framework of "Article 173" reporting, on the funds' contribution to compliance with targets for limiting global warming and for the energy and ecological transition.

One AMC goes beyond the objective of reducing the carbon intensity of the portfolios in the short term, and

⁴⁹ This AMC also published a summary sheet of the issues, but which turned out to be inconsistent with the sector fact sheets and has no longer been applicable since 2018.

gives priority to investments in companies developing on a long-term basis goods and services for a lower-carbon economy. Moreover, one AMC tracks the carbon intensity of the portfolios' revenues against temperature rise scenarios on the 2025 horizon.

One AMC publishes reports that are generally very clear and instructive. The funds' half-yearly and annual reports summarise in a few pages the characteristics of the fund, the methodology for selection of assets, and the SRI approach. The monthly report on the funds of this AMC presents information on stock picks, on the latest movements, an analysis of the fund's portfolio rating by comparing it with the investment universe, the entire portfolio together with the weight of each security in the fund's assets, and the ESG rating and sources of the data presented.

The carbon footprint report of this AMC presents the assessment of the funds' carbon footprint, and a comparison of the fund's carbon footprint with the benchmark index (by sector), the sectors most exposed to carbon risk, the highest-emitting companies in the portfolios, and the risks. This AMC also publishes a report on the social footprint of the funds: maps presenting the portfolio's exposure to social risks from both the sector and geographic viewpoints.

Good practices

- Presenting in the prospectuses/KIIDs the data service providers used, making sure that the information provided is updated where necessary. Alternatively, a reference can be made in the prospectuses/KIIDs to the Transparency Code or the "Article 173" report.
- Presenting all or part of the fund's inventory in the documents presenting the SRI approach, while complying with the rules in force regarding market timing and late trading.⁵⁰
- Providing information concerning the effectively discriminatory nature of its extra-financial approach via an indication of the selectivity rate of its ESG strategy relative to an initial universe. As mentioned in the previous AMF report on sustainable finance, *"Given the limitations of the selectivity ratio and how difficult it is for non-professional investors to understand the impact of ESG methodologies on the makeup of funds, the AMF invites management companies to be more educational in their communication with their non-professional investors"*.
- Performing reporting on the exercise of voting rights fund by fund (and not for all funds combined), specifying, for each of the securities in the portfolio, the list of resolutions.⁵¹
- Presenting fund by fund the companies emitting most CO₂, by defining the various scopes considered.
- Specifying in the engagement report the universe of companies concerned by the engagement (proportion of companies with which the AMC has initiated a dialogue), the themes of the engagement policy and the actions for following up on this engagement.

⁵⁰ This practice is an extension of the good practice in the AMF report on socially responsible investment in collective investment schemes published in 2017, according to which: *"A growing number of management companies explain the impact of ESG methodology on the portfolio in the marketing materials provided to investors. Management companies can, in particular, provide investors with the inventory of the stocks held in SRI UCIs' portfolios on a dedicated page of their websites on a half-yearly basis, while obeying the current market timing and late trading rules (AMF position DOC-2004-07)."*

⁵¹ This practice is an extension of the good practice in the AMF report on socially responsible investment in collective investment schemes published in 2017, according to which: *"The publication by AMCs on their website of the votes on resolutions presented during the general meetings of companies whose securities they holds in portfolios (especially if the security accounts for more than 1% of a fund's portfolio) is a good practice observed by the AMF."*

- Grouping the documents concerning engagement in a section easily accessible on the website.⁵²
- Presenting in a few pages in the funds' reports (annual reports, or even also half-yearly reports), the most relevant information concerning the characteristics of the fund, the methodology for selection of assets, and the SRI approach.

Reminder of the applicable regulation

- The "Article 173" report must describe clearly the nature of the ESG criteria taken into account, the information used for analysis of the issuers on the basis of ESG criteria, the methodology for the analysis conducted on the ESG criteria and its results, and how the results of the analysis performed are incorporated in the investment policy.
- The "Article 173" report must list the managed funds, simultaneously taking into account ESG criteria, specifying, as a percentage, the weight of these funds' AUM in the total amount of the AMC's AUM.
- When the AMC manages funds for which the AUM exceed €500m, it must establish an "Article 173" report for each of those funds.

2.6 CONTROL SYSTEM

The inspection team analysed the second-level controls concerning the SRI issue: controls relating to the investment process, controls relating to data quality, controls on the exercise of voting rights, controls on conflicts of interests, and controls relating to the information provided to investors.

Regarding controls on the investment process:

- One AMC performs no formalisation of said controls;
- The controls performed by one AMC since 2017 make it possible to ensure at the least that all the activities of the labelled funds are in compliance with the labels' guidelines, and that the exercise of voting rights complies with the voting policy;
- The controls performed by one AMC are very incomplete and insufficiently formalised. The work sheet does not set out formally or trace the work effectively carried out, and does not make it possible to understand the conclusions of the control. No recommendation is expressed, and no remediation measure is proposed. Moreover, these controls do not concern the consistency between the securities held in the portfolio and the investment selection criteria foreseen in the prospectuses and/or the Transparency Code of the funds;
- The controls by one AMC are performed but are insufficiently formalised. The Internal Control and Compliance Officer (ICCO) performs controls throughout the investment process. Before the investment committee, the ICCO checks the eligibility of securities, the ESG analysis score, and compliance with the exclusion criteria. The ICCO systematically verifies portfolio investments/divestments. Furthermore, the ICCO's participation in the investment committee on a non-voting basis strengthens the investment and control system.

No AMC performs second-level controls on the quality of ESG data. One AMC proposed deploying an AFG working

⁵² This practice is an extension of the good practice in the AMF's 2017 report on socially responsible investment in collective investment schemes, according to which: "To make it easier to access this information, the AMF recommends publishing information about the entity (paragraph II, sub-paragraph 1 of article D. 533-16-1 of the COMOFI) in a single document that is easily accessible on the AMC's website (e.g. through links on pages discussing sustainable development issues) and written in French if the AMC targets non-professional investors in France"

group to initiate marketplace thinking concerning the implementation of second-level control on the data provided by outside service providers.

Only one AMC performs controls on the exercise of voting rights. These controls performed since 2016 are well documented (specified scope, documentary source used, observations and recommendations).

Only one AMC has established second-level controls aiming to ensure that dialogue with the companies in the funds' portfolios generate no conflicts of interests liable to affect its free exercise of voting rights and ultimately the interest of the unitholder. It has performed these controls since 2017.

One AMC performs no control on the SRI commercial documentation.

Generally, the formal presentation and documentation of second-level control work are highly satisfactory for two AMCs. They are insufficient for two remaining AMCs. In the case of another AMC, the controls are performed, but the inspection team noted that they lack formalisation.

Reminder of the applicable regulation

- AMCs shall establish and maintain adequate operational internal control mechanisms designed to secure compliance with decisions and procedures at all levels of the AMC.
- AMCs shall establish and maintain an operational permanent and effective compliance function which, in particular, monitor, and on a regular basis, assess the adequacy and effectiveness of the measures, policies and procedures established and actions taken to remedy any deficiency in compliance with their professional obligations.

Upgrading

- The AMF's policy regarding extra-financial information will evolve to take these observations into account.
- Also, the third AMF report on sustainable finance in collective investment schemes will enrich this information with additional observations and good practices.