EU Strategy on Sustainable Finance

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EU keeps on increasing ambition on climate change

Jean Claude Juncker, 2014

1 November 2014-2019

A Resilient Energy Union with a Forward-Looking Climate Change Policy

Target

- **40%** cuts in greenhouse gas emissions by 2030
- **32%** renewables in energy consumption
- **32,5%** energy savings

Progress

Climate and energy legislation, if implemented: 45% greenhouse gas emission by 2030


Ursula von der Leyen, 2019

1 November 2019-2024

A European Green Deal

Target

- **50%** cuts in greenhouse gas emissions by **2030**
- **Climate-neutral** continent by **2050**

An enormous amount of investments is required to reach our climate goals

Valdis Dombrovskis
Executive Vice-President-designate for an Economy that Works for People

"To achieve climate neutrality, Europe needs up to ***€290bn*** *in extra yearly investment over the next decades.*

Public money will not be enough*. This is why the EU has proposed hard law to incentivise private capital to flow to green projects. "*

"We hope that ***Europe's leadership will inspire others*** *to walk next to us."*

Financing the Green Transition

Ambition

Reaching climate neutrality by 2050 while ensuring that the transition is just and fair

Massive investments will be needed

EU Budget	Commission's proposed target = 25% of EU expenditure contributing to climate objectives for the 2021-2027 Multi-Annual Financial Framework
Blended Finance	InvestEU & European Fund for Sustainable Development (EFSD)
Private Finance	**Commission Action Plan on financing Sustainable Growth**

Commission Action Plan on financing sustainable growth

Reorient capital flow towards more sustainable investments

1. Establish a **Taxonomy** of environmentally sustainability activities
2. Create **standards and labels** for green financial products
3. **Foster investment in sustainable projects**
4. Incorporate sustainability in providing investment advice
5. Develop sustainability benchmarks

Mainstreaming sustainability in risk management

6. Better integrate sustainability in ratings and market research
7. Clarify institutional **investors**' and asset managers' **duties**
8. Incorporate sustainability in prudential requirements

Foster transparency & long-termism

9. Strengthen corporate **sustainability disclosure**
10. ↑sustainable **corporate governance** and ↓ short-termism

Key actions of the EU Commission

	Action	Objective	Legislation Level 1 (framework)	Technical advice	Legislation Level 2 (detailed technical criteria)
1	**Taxonomy**	Develop an EU common language on environmentally sustainable economic activities	*Status:* under negotiation ✓	Technical Expert Group (**TEG**) ✓	Pending the negotiation of level 1
2	**Standards and labels**	Develop EU standards (such as EU Green Bond Standard) and labels for sustainable financial products (via Ecolabel) to protect integrity and trust of sustainable finance market	To be considered/assessed	**TEG**: EU Green Bond Standard; JRC: ecolabel for financial products ✓	To be considered/assessed
4	**Disclosures by financial market participants**	Enhance transparency to end-investors on how financial market participants consider sustainability	*Status*: approved ✓	European supervisory authorities ✓	Delegated act under development
5	**Benchmarks**	Develop climate benchmarks and ESG disclosures for benchmarks	*Status*: approved ✓	**TEG** ✓	COM drafting secondary legislation based on TEG advice
8	**Sustainability in prudential requirements**	Explore the feasibility of reflecting sustainability in prudential rules (where justified from a risk perspective)	Pending the result of technical assessment	EBA and EIOPA ✓	Pending the result of technical assessment
9	**Corporate sustainability disclosure**	Enhance climate and sustainability-related information provided by corporations	Depending on the result of the ongoing fitness check, possible amendment of the non-financial reporting directive*	**TEG** (climate-related information) COM fitness check on corporate reportin[g] ✓	Pending the result of technical assessment

* The Commission issued guidelines on reporting climate-related information in June 2019

TEG on Sustainable Finance assists the Commission

35 experts - from July 2018 to year-end 2019

1	2	3	4
Disclosures (reporting)	**Taxonomy**	**Benchmarks**	**Green Bond Standard**
guidance to improve corporate disclosure of climate-related information	Technical screening criteria for environmentally sustainable economic activities	Minimum standards for the two new types of climate benchmarks & Benchmarks ESG disclosures	An EU Green Bond Standard

Call for feedback

Call for feedback

Interim
June 2019

Call for feedback

Interim
Mars 2019

Call for feedback

European Commission

Commission proposal for an EU Taxonomy

Objective

Provide a **classification tool** to help investors and companies to make informed investment decisions on environmentally sustainable activities

We need a taxonomy that is **robust, science-based, and ambitious**, in line with our shared environmental objectives, including going towards climate neutrality in line with the Paris agreement

Use: is it obligatory ?

- Obligatory disclosures for institutional investors and asset managers marketing investment products as 'green' in the EU
- EU Member States are required to use the EU Taxonomy when creating public labelling schemes for 'green' investment products and corporate bonds

Further voluntary use by a range of actors

What is it?

A list of economic activities that are environmentally sustainable based on a **rigorous methodology**.To be included in the Taxonomy, an economic activity must meet the following criteria:

substantially contribute to 1 of the 6 objectives + Do not significantly harm any of the other 5 obj. + Minimum social* safeguards

6 environmental objectives

1. Climate change mitigation
2. Climate change adaptation
3. Sustainable use & protection of water
4. Circular economy, waste prevent & recycling
5. Pollution prevention and control
6. Protection of healthy ecosystems

* Observe International Labour Organisation (ILO) core labour conventions

What is it not?

- A rating of good or bad companies
- A mandatory list to invest in
- Making a judgement on the financial performance of an investment
- Inflexible or static

The TEG report on taxonomy – June 2019 (1/3)

TEG

Composed of **35 experts** from civil society, academia, business and the finance sector, as well as **10 additional** members and observers from EU and international public bodies

- All assessments made by TEG were based on **scientific evidence, literature and international practice**
- TEG report **initial** focus is on **climate change mitigation and adaption**

7 Sectors

67 activities

- highest-emitting macro sectors (represent 93.2% of GHG emissions in the EU)

- Agriculture and forestry
- Manufacturing
- Electricity, gas, steam and air conditioning supply
- Water, sewerage, waste and remediation
- Transport
- Information and Communication Technologies (ICT)
- Buildings

Screening criteria

- Substantial contribution to one environmental objective (for climate change mitigation → e.g. GHG emission thresholds)
- Do not significant harm to any of the other environmental objectives

The TEG report on taxonomy – June 2019 (2/3)

Characteristics	Type of activity	Criteria	Example
"Greening of"	**Already low carbon** (very low, zero or net negative emissions). Compatible with net zero carbon economy by 2050.	Likely to be stable and long term	Electricity generation from solar PV
	Contribute to a transition to a zero net emissions economy in 2050 or shortly thereafter, but are not currently close to a net zero carbon emission level.	Likely to be revised regularly and tightened over time	Manufacturing of steel
"Greening by"	Activities that **enable emissions reductions** in either of the two previous categories.	Some likely to be stable and long term, some likely to be revised regularly	Manufacturing of wind turbines

Activities that undermine mitigation objectives are **not** included.

The TEG report on taxonomy – June 2019

TEG Guidance on taxonomy use

Five steps to implement taxonomy

Step 1:

Identify activities conducted by the company, issuer or covered by the financial product (e.g. projects, use of proceeds) that could be eligible.

Step 2:

For each activity, assess whether the company or issuer meets criteria for a **substantial contribution**, e.g. electricity generation <100g CO2/kWh.

Step 3:

Verify that DNSH criteria are being met by the issuer. Investors using the Taxonomy would most likely use a due-diligence like process for reviewing the performance of underlying investees.

Step 4:

Conduct due diligence to avoid any violation to the **social minimum safeguards** stipulated in the Taxonomy regulation (article 13).

Step 5:

Calculate alignment of investments with the Taxonomy and prepare **disclosures** at the investment product level.

The TEG report on taxonomy – June 2019 - example

24.4 Infrastructure for low carbon transport

Sector classification and activity	
Macro-Sector	F - Construction
NACE Level	4
Code	F42.1.1, F42.1.2, F42.1.3
Description	**Infrastructure for low carbon transport** – **land transport** including NACE categories: • Construction of roads and motorways • Construction of railways and underground railways • Construction of bridges and tunnels
Mitigation criteria	
Principle	Demonstrate substantial GHG emission reduction.
Metric	CO_2e emissions per passenger-kilometre, per tonne-kilometre, or per kilometre (gCO_2e/pkm, gCO_2e/tkm or gCO_2e/km).
Threshold	The construction and operation of transport infrastructure is eligible in the following cases: 1. Infrastructure that is required for zero direct emissions transport (e.g. electric charging points, hydrogen fuelling stations or electric highways). 2. Infrastructure and equipment for active mobility (walking and cycling) 3. Infrastructure that is predominantly used for low-carbon transport if the fleet that uses the infrastructure meets the thresholds for direct emissions as defined in the relevant activity (the biofuels criteria does not apply here as it is not possible to monitor). 4. Non-electrified rail infrastructure with an existing plan for electrification or use of alternatively powered trains. For all cases: • Only infrastructure that is fundamental to the operation of the transport service is eligible. • Infrastructure that is dedicated to the transport of fossil fuels or blended fossil fuels is not eligible
Rationale	
The construction and operation of infrastructure for low carbon land transport is considered eligible because this is considered a key enabling factor for improving the uptake of the transport activities that are considered eligible under the rest of the land transport section of the Taxonomy. Criteria 3. above would accommodate all electric rail lines and non-electrified lines with battery powered and hydrogen trains operating. However even if non-electrified there might be a case for renewal of rail infrastructure in order to ensure continuity of the service while alternative powered trains (hydrogen, battery) are deployed in the future years, hence the inclusion of criteria 4 above. There is no significant risk of lock-in in those cases where the fleet is due for renewal. It is acknowledged that embedded carbon emissions in infrastructure projects (e.g. upstream emissions from manufacture of construction materials) may be significant in certain circumstances.	

The level of uncertainty around data in this respect makes it challenging at this time to incorporate this consideration within thresholds for infrastructure. However, this element should be considered for ongoing work on the Taxonomy. Transport of fossil fuels is considered to have potential negative impacts on climate change and therefore is excluded.	
Do no significant harm assessment	
The main potential significant harm to other environmental objectives from infrastructure activities are attributed to noise and vibration pollution, water contamination, waste generation and impacts on biodiversity (habitat and wildlife) and land use, specifically: • Contamination of water during construction and unsustainable use of water during construction and operations • Unsustainable use of resources during constructions, e.g. generation of high amount of waste, no recycling/reuse of construction waste • Noise pollution can be relevant for both rolling stock and railway infrastructure as noise can be generated by both rolling stock and poor conditions of rail tracks.[359] • Construction of infrastructure can cause significant harm when taking place in protected areas or areas of high biodiversity values outside protected areas. • Infrastructure can cause fragmentation and degradation of the natural and urban landscape due to the "barrier" effects of the infrastructure and can involve risks of wildlife accidents caused by collisions. Railway infrastructure (in particular tunnels) can cause change and degradation of hydromorphological conditions of water bodies and therefore have impacts on aquatic ecosystems.	
(2) Adaptation	A1: Reducing material physical climate risks. The economic activity must reduce all material physical climate risks to the extent possible and on a best effort basis. This means the activity integrates physical and non-physical measures aimed at reducing - to the extent possible and on a best effort basis - all material risks that have been identified through a risk assessment. The above-mentioned assessment has the following characteristics: • considers both current weather variability and future climate change, including uncertainty; • is based on robust analysis of available climate data and projections across a range of future scenarios; • is consistent with the expected lifetime of the activity. A2: Supporting system adaptation. The economic activity must not adversely affect adaptation efforts of others. This means: • The activity does not lead to increased climate risks for others or hamper adaptation elsewhere • The activity is consistent with sectoral, regional, and/or national adaptation efforts.
(3) Water	Ensure that no harmful substances are released into water to avoid water contamination, during operation, renewal, upgrade and new construction of

[359] http://www.diva-portal.org/smash/get/diva2:675304/FULLTEXT02

The TEG report on taxonomy – June 2019 - example

	infrastructure, in accordance with the environmental objectives of Directive 2000/60/EC[28], Art. 4(1).
(4) Circular Economy	• Re-use parts and use recycled material during the renewal, upgrade and construction of infrastructure. • At least 80% (by weight) of the non-hazardous construction and demolition waste (excluding naturally occurring material defined in category 17 05 04 in the EU waste list) generated on the construction site must be prepared for re-use, recycling and other material recovery, including backfilling operations using waste to substitute other materials. This can be achieved by executing the construction works in line with the good practice guidance laid down in the EU Construction and Demolition Waste Management Protocol[360].
(5) Pollution	• Minimise noise and vibrations from use of infrastructure by introducing open trenches/ wall barriers/ other measures. • Minimise noise, dust, emissions pollution during construction / maintenance works.
(6) Ecosystems	• Projects likely to affect designated protected areas, or areas of high nature and biodiversity value and vulnerability including UNESCO World Heritage and Key Biodiversity Areas (KBAs) may be implemented only if the Environmental Impact Assessment and the appropriate assessment conducted in compliance with the provisions of the EU Habitats[361] and Birds[362] Directives (or other analogous provisions in case of non-EU countries) have concluded that the infrastructure will not adversely affect the integrity of the site, and all necessary mitigation measures are in place to reduce the impacts on species and habitats. Possible mitigation measures could be: a) measures to reduce fragmentation and ensure the connectivity of habitats (e.g. tunnels and viaducts, under-or above-ground wildlife crossings), b) minimisation of collision risks through and barriers/fences for wildlife, c) avoid works during critical periods of species such as mating, reproductive, breeding or migration periods.

[360] EU Construction and Demolition Waste Protocol. Available at https://ec.europa.eu/growth/content/eu-construction-and-demolition-waste-protocol-0_en

[361] Council Directive 92/43/EEC of 21 May 1992 on the conservation of natural habitats and of wild fauna and flora

[362] Directive 2009/147/EC of the European Parliament and of the Council of 30 November 2009 on the conservation of wild birds

International Cooperation on Sustainable Finance

- Europe cannot act alone
- The EU's approach to global climate action is going beyond the public sphere, with initiatives to **mobilise international private investors across the globe.**

- The global nature of financial markets offers a great potential to help all countries on their transition path by linking financing needs to global sources of funding. This potential however, is still largely untapped
- To mobilise international investors => promoting **integrated markets for environmentally sustainable finance** and, develop a coordinated approach, while respecting national and regional contexts.
- This is the reason why the European Union together with relevant authorities from Argentina, Canada, Chile, China, India, Kenya and Morocco launched on 18 October 2019:

International Platform on Sustainable Finance (IPSF).

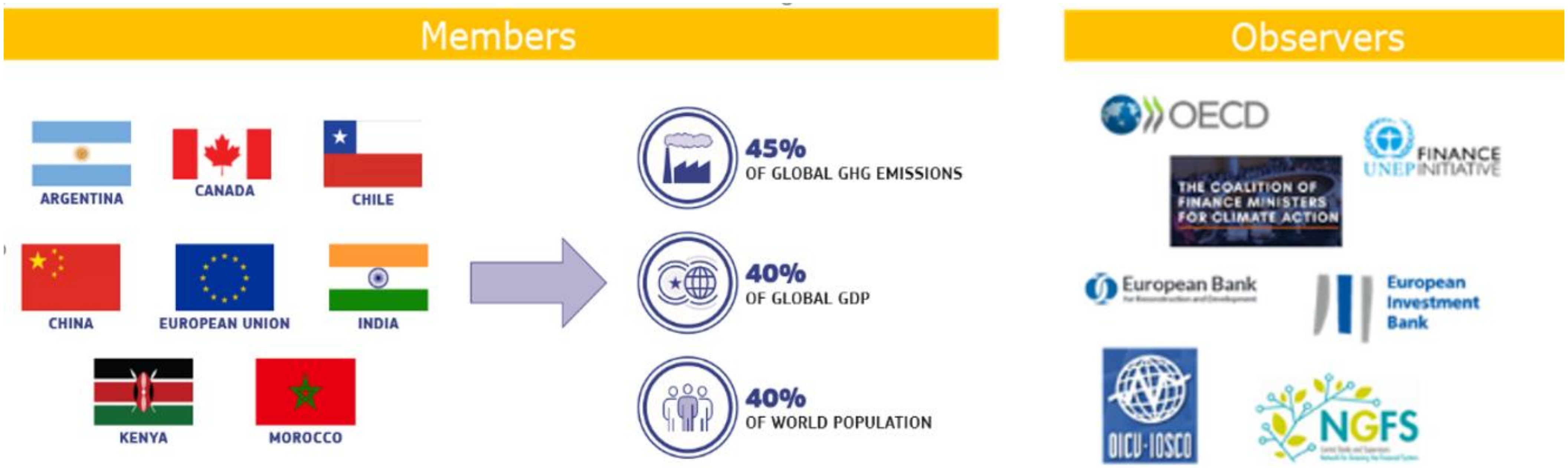
The International Platform on Sustainable Finance

Objective

- Countries agree to exchange best practices and coordinate efforts on environmentally sustainable finance initiatives in the areas of taxonomies, disclosures, standards and labels.

- The IPSF is members-driven and open to those jurisdictions which are taking actions and willing to promote international cooperation in the area of environmentally sustainable finance.

- Building coherent international strategies such as the **IPSF is vital** to stimulate investment and redirect capital flows towards our climate objectives at the scale required for the most important economic transition of our times.



Towards a renewed sustainable finance strategy

We need a renewed sustainable finance strategy as a part of the European Green Deal

European Green Deal

Sustainable Europe Investment Plan

Biodiversity Strategy for 2030

New Circular Economy Action Plan

Sustainable Finance Strategy

European Climate Law

Just Transition Fund

Renewed sustainable finance strategy

Public consultation

to define the basis of a new strategy and hear views from all stakeholders

Early 2020 for 12 weeks

Publication of the future strategy

Q3 2020

Back-up

Additional slides on AP implementation and TEG‘s work

The TEG report on benchmarks – September 2019

- **Recommends minimum technical requirements for the methodology of both climate benchmarks and on ESG disclosures**

Climate Benchmarks

EU Climate Transition Benchmark (EU CTB)

Relative decarbonization: min. reduction in GHG emissions intensity compared to market index: **30%**

Ratio between **green** and **brown** compared to market index: **= or >** (*voluntary*)

EU Paris-aligned Benchmark (EU PAB)

Relative decarbonization: min. reduction in GHG emissions intensity compared to market index: **50%**

Ratio between **green** and **brown** compared to market index: **4*>** (*voluntary*)

Both types of climate benchmarks must:

- demonstrate a **significant decrease in GHG emissions intensity** compared to their underlying investment universes or parent indices.
- be sufficiently **exposed to sectors** relevant to the fight against climate change.
- **demonstrate their ability** to reduce their own GHG emissions intensity on a year-on-year basis.
- exclude companies involved in controversial weapons; in violations of global norms or in controversies arising from significant harm of at least one environmental objectives.

Benchmarks ESG disclosure

- ESG factors are one of the key elements of the benchmark methodology
- All benchmarks should disclose whether or not they pursue ESG objectives and disclose key ESG factors in the benchmark statement; also should report on their degree of alignment with the Paris Agreement.

Asset Classes

All, except interest-rate and currency benchmarks

KPIs

Relevant to each asset class

supported by global standards

Climate Scenario Alignment

Which temperature scenario?

Methodology and data used

Disclosure templates

1. Methodology
2. Benchmark statement
3. Climate Scenario Alignment

EU law: sustainability disclosure by financial market participants and financial advisers

Disclosure regulation places the following requirements on financial market participants

Scope	What to disclose	Where to disclose	Who should disclose
All investment products	**How negative impacts on financial returns arising from sustainability risks are integrated in risk policies**	Websites, pre-contractual information, marketing communication	all financial entities
All investment products	**How the financial entity considers adverse impacts on sustainability factors (negative externalities)**	Websites, pre-contractual information	compulsory for financial entities >500 and holding companies, other entities to disclose on a comply or explain basis
Investment products with sustainability characteristics or objectives	**How these sustainability characteristics or objectives are met**	Pre-contractual information, websites, periodical reports, marketing communication	all financial entities

TEG report on Green Bonds Standard – June 2019

Proposed core components

Alignment with EU taxonomy

Publication of a Green Bond Framework explaining the voluntarily alignment and investment strategy

Mandatory Reporting
Allocation report
Impact report

Mandatory Verification by external reviewer

How would the EU-GBS work?

BEFORE OR AT ISSUANCE

GRADUAL ALLOCATION…………………..FULL ALLOCATION

Publication of Green Bond Framework

Issuer's Green Bond strategy and alignment with the

EU TAXONOMY

Description of types of Green Projects to be financed

Description of methodology and processes regarding allocation and impact reporting

Use of proceeds specified in the legal documentation

…

Annual Allocation Reports

Confirmation of alignment with EU GBS

Breakdown of allocated amounts per project or portfolio

Geographical distribution of Projects

Final Allocation Report

Impact Report

Impact reporting at least once (at full allocation), or annually

ACCREDITATION OF EXTERNAL VERIFIERS

DOCUMENT VERIFIED BY ACCREDITED EXTERNAL VERIFIERS

EU law - The Non-Financial Reporting Directive

Currently under assessment: fitness check on corporate reporting

4 issues

- Environment
- Social & employee
- Human rights
- Bribery & corruption

5 areas

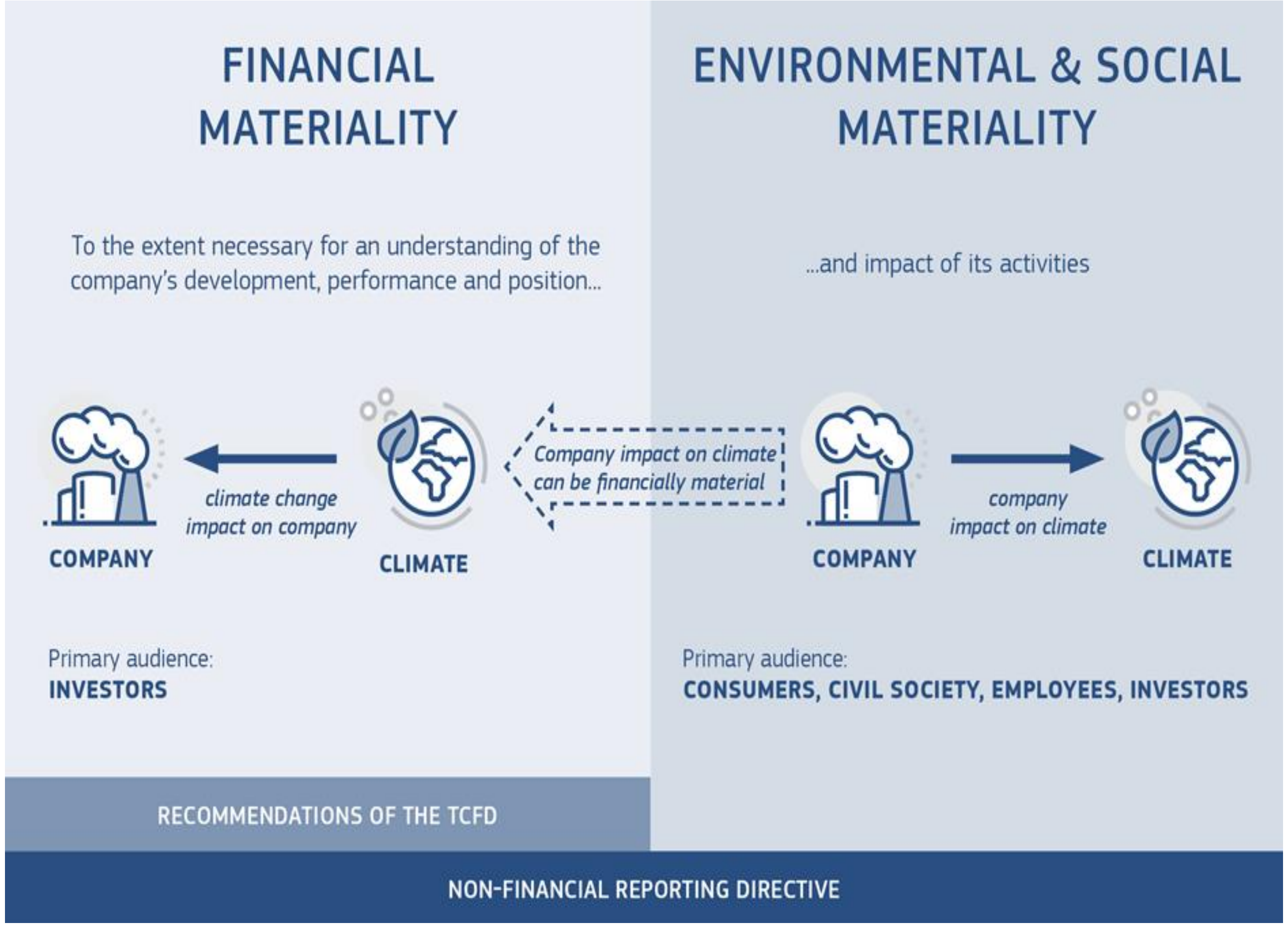
- Business model
- Policies and due diligence
- Outcomes
- Risks and risk management
- KPIs

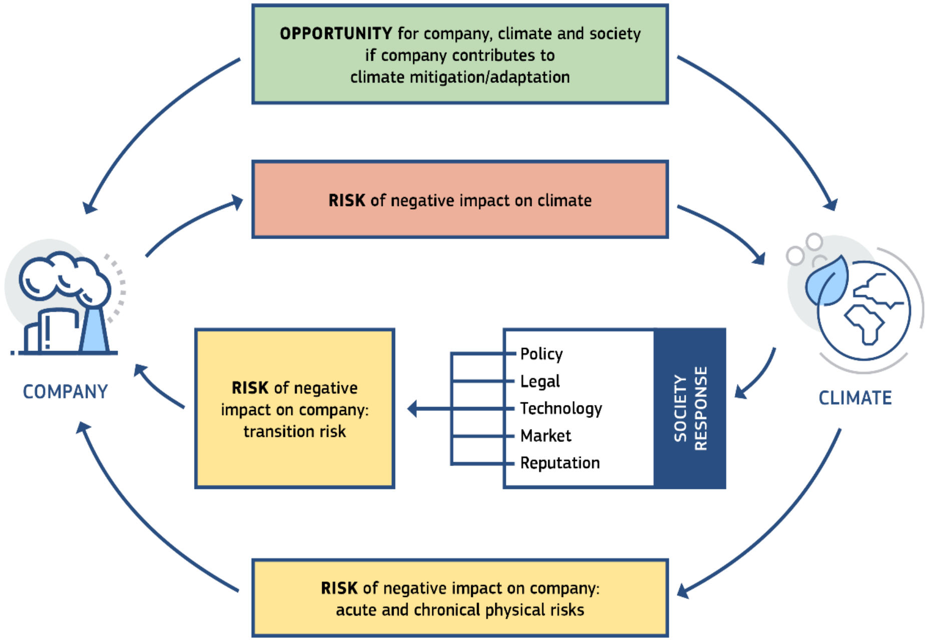
Large listed companies, and banks and insurance companies, with >500 employees

Materiality: "to the extent necessary for an understanding of the undertaking's development, performance, position, and impact if its activities…"

COM guidelines and NFRD work with double materiality

Two important perspectives are considered in COM work on corporate disclosures…





Commission ongoing fitness check on the Non-Financial Reporting Directive

Material information not reported

Information not reliable

Information not comparable

Some companies do not report even though users want them to

Information not easy to find

Coherence with other requirements

Companies are confused and face additional info demands

Commission's climate reporting guidelines – updated in June

Climate reporting Guidelines – June 2019

- Consistent with Non-Financial Reporting Directive.
- Supplement to general guidelines on non-financial reporting published in 2017, which still apply.
- Integrate TCFD recommendations.
- Based on proposals from the Technical Expert Group on Sustainable Finance.
- Target audience: the +/- 6,000 listed companies, banks and insurance companies under the scope of the Non-Financial Reporting Directive.
- Not legally binding.

Structure of the guidelines

5 reporting areas of the Non-Financial Reporting Directive

Business model | Policies | Outcomes | Risks | Indicators

13 recommended disclosures and 10 KPIs
indicating which ones are TCFD recommended disclosures

Further guidance
+ specific further guidance for banks and insurance companies