World Benchmarking Alliance

CDSB Climate Disclosure Standards Board

Web-roundtable: Addressing systematic risk and encouraging sustainability transparency in the financial system, co-organised by the World Benchmarking Alliance and the Carbon Disclosure Standards Board on February 11 2021

Summary of discussions

The roundtable set out to explore how sustainable finance risks are considered, documented and reported on within existing standards and frameworks, and what gap there remains when it comes to incentivising sustainability action of financial institutions. The event addressed if the current policy toolbox for the EU financial sector is sufficient to identify and address the current unsustainable trajectory and the risk it poses to financial institutions and the economy, as well as to meet increasing stakeholder expectations on disclosure of the impacts of the private sector. The online event gathered 48 participants, representing the interests of the investor, regulatory, supervisory, reporting standards and civil society sector. It also formed part of the WBA Policy Collective Learning & Action Labs (Policy CoLABs) which are designed to find policy pathways to address critical bottlenecks that unlock a transformative business sector contribution to the SDGs.

Background

The UN Sustainable Development Goals (SDGs) and the Paris Agreement have aligned public, private and civil society as to the scale and urgency of the issues faced. However, financial flows towards the SDGs remain modest relative to the scale of investment needs. Mobilising private finance is essential as projected public sector financial flows are insufficient to deliver impact at the necessary speed and scale. Scaling up and redirecting private capital towards the SDGs could contribute to closing this gap. Coherent global policies must enable this transformation required.

The EU has shown strong leadership on sustainable finance policies and published a first sustainable finance strategy in 2018 with a set of ambitious policy initiatives and tools. The renewed Sustainable Finance Strategy, the revision of the Non-Financial Reporting Directive, and the implementation and broadening of the EU Taxonomy will be important initiatives to facilitate the necessary transformation needed in the financial sector.

These are the key reflections and policy recommendations that emerged during the event:

1. **EU sustainable finance policies should be science driven, reflect on best market practices and look at real world impacts to bridge the (data) gap between investment practices and global climate and environmental goals.**

   The upcoming review of the Non-Financial Reporting Directive[1] and the move towards alignment of reporting obligations of investees and investors, through identifying environmental risks on the basis of the six objectives set out in the taxonomy regulation,

[1] See CDSB report, The state of EU environmental disclosure in 2020

namely: climate change mitigation; climate change adaptation; sustainable use and protection of water and marine resources; transition to a circular economy pollution prevention and control; protection and restoration of biodiversity and ecosystems is welcome in this regard.

2. **The future sustainable corporate governance initiative of the European Commission will need to strike a balance between hard law and flexible approaches (such as comply or explain) to incentivise more sustainable and responsible business conduct, by choosing the most effective policy tools (directive, regulation, guidelines…) and the relevant policy areas to address.**

Corporate governance was already included in the Action 10 of the 2018 Action Plan on sustainable growth but the outcomes of the EU reflections on corporate governance will be presented in the upcoming sustainable corporate governance initiative.

3. **Regulatory developments on corporate sustainability and responsible investing requirements need to be supplemented by independent tools such as benchmarks to help accelerate progress on impact and drive standardisation.**

Regulation is critical to raise the floor, in terms of comparable understanding, reporting and action on the many sustainability challenges collectively faced. To supplement this raising of the floor, benchmarks can act as an accountability mechanism to further drive financial and non-financial corporate reporting and – more critically – associated action that leads to positive change in the underlying economy Improved corporate reporting will not in and of itself resolve the underlying drivers of short-termism and negative externalities that lead to unsustainable practices, but by using improved corporate reporting (enabled through regulation) to focus on comparing the progress made by the world's most influential institutions, such a spot lighting may indicate where specific institutions and clusters of institutions (by industry, by region) are leading, or lagging, encouraging a race to the top.

4. **Ensure mandatory disclosure of how a company's sustainability strategy is integrated into accountability at a senior board level through specific targets and Key Performance Indicators (KPIs).**

Despite uptake in sustainability reporting, such reporting is too often 'self-defined' as opposed to indicating progress in line with scientifically established planetary boundaries, and globally recognised societal norms.[2] It is therefore crucial to move toward globally consistent frameworks and standards if we are to achieve the Sustainable Development Goals, Paris Agreement and the UN Guiding Principles. It is also essential to evidence where senior level responsibility and expertise lies, for

[2] World Benchmarking Alliance (2021) Financial System Scoping Report

accountability purposes but also from a governance / management systems point of view.

5. **Reporting standards should clearly define the relationship between non-financial reporting and financial performance to embed societal and stakeholder expectations in their business practices.**

Financial institutions face a challenge in meeting increased societal and stakeholder expectations. There is a need to reinforce existing voluntary standards to prepare the ground for a future system of reporting that could be taken forward at a global level. A principle-based approach for measuring which sustainability issues impact on society and the economy, while demanding that standardised corporate disclosures are targeted to specific and aligned reporting requirements should be considered. Similarly, strong requirements on due diligence / materiality assessment will leave scope for companies to report in a meaningful way, but within a clearly defined framework. (i.e. without stipulating which specific risks and impacts to discuss but with the requirement to disclose the exact process for identifying & dealing with them). There needs to be clear guidance on the need to do this from the lens of risks to people & the environment, not (just) financial risks to the institutions. This requires the alignment of Key Performance Indicators (KPIs) and a degree of responsiveness to emerging issues to ensure the decisions on reporting standards made now remain fit for purpose in the future.

6. **The European Commission should address the sustainable finance powers of the European Supervisory Authorities as part of the initiative foreseen in the Action 16 of the 2020 Capital Markets Union Action Plan to foster further supervisory convergence.**

Enforcement and supervision are of the essence in order to guide companies in an evolving and complex regulatory landscape. The European Supervisory Authorities, whose revised mandate came into force in January 2020 and include further powers in the field of sustainable finance, should be properly equipped to be able to ensure a consistent implementation of adopted requirements which are about to become more granular and would therefore require further attention from a supervisory perspective.