White Paper

Priority sustainable finance actions within the German EU presidency

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Frankfurt School - UNEP Collaborating Centre for Climate & Sustainable Energy Finance

Frankfurt School

The transformation towards a sustainable European economy is a key priority of the EU and its member states. Public and private actors are collaborating to ensure a just transformation. Sustainable finance is a major element in the sustainability transformation. It will enable the redirection of capital flows towards the Paris Agreement, the UN Sustainable Development Goals as well as the European Green Deal and national sustainability agendas. Efforts by the EU and member states are ongoing to establish adequate framework conditions for sustainable finance, e.g. through the EU Action Plan on Financing Sustainable Growth or the German Sustainable Finance Committee.

The German EU presidency provides the German government with the opportunity and the responsibility to steer relevant regulatory processes at the EU level. The existing momentum for sustainable finance provides a fertile ground for a series of policy achievements during the German presidency. At this crucial moment for the sustainability agenda, prioritising key sustainable finance actions will facilitate adequate progress.

Frankfurt School of Finance and Management has been conducting research, offering academic and executive education and providing consultancy services in the field of sustainable finance for more than ten years. Based on this vast knowledge base, the involvement in ongoing regulatory processes and the strong collaboration with the German financial market place, we would like to take the liberty to provide the German government with our view on five priority sustainable finance actions for the German EU presidency.

1. **EU Taxonomy – Delegated Acts**: according to the Taxonomy Regulation, the delegated acts setting out the EU Taxonomy technical screening criteria for the EU environmental objectives climate change mitigation and adaptation to climate change shall be adopted by the end of 2020. ***The German presidency shall support efforts to adopt the delegated acts by the end of 2020***, as it would provide certainty on the final design of the EU Taxonomy to market participants and thus reduce costs for the operationalisation of the EU Taxonomy. Particularly in light of the Disclosure Regulation and the update to the Non-Financial Reporting Directive, meeting the deadline is of high importance. Furthermore, ***the German presidency shall support the development of the delegated acts in accordance with the recommendations by the European Commission's Technical Expert Group on Sustainable Finance (TEG) in terms of scope, ambition and stringency.*** This will ensure that the principles of technology-neutrality and evidence based decision making are maintained, as set out in the Taxonomy Regulation. ***The German presidency should support efforts to clarify liability questions around EU Taxonomy disclosure and data collection***. This would help market participants in the operationalisation of the EU Taxonomy.

2. **Support an update to the Non-Financial Reporting Directive (NFRD) in accordance with the NBG**: the NFRD is currently under review and a review is planned for Q1 of 2021. A key element of the review constitutes the explicit integration of disclosures on climate-related risks and opportunities. In June 2019, the European Commission already published the non-binding guidelines on reporting climate-related information (NBG) as a supplement to the NFRD. The NBG largely reflect the recommendations by the final recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), a working group under the Financial Stability Board (FSB). ***The German presidency shall support the integration of mandatory reporting in accordance with the NBG and the TCFD in the reviewed NFRD***. The mandatory disclosure would enhance the ability of financial institutions to assess climate-related risks and opportunities and reflect them in firm valuation and financing

and investment decisions[1]. Moreover, ***the German presidency could encourage the integration of disclosure obligations for the other environmental dimensions of the EU taxonomy*** to accommodate financial institutions in their efforts to adequately price environmental risks, reduce environmental impacts of their financing and investment decisions, and to operationalise the requirements in the BaFin guidance notice on dealing with sustainability risks and similar publications by European supervisory authorities. In order to foster access to relevant information for financial institutions, the scope of the NFRD would need to be expanded to cover a more meaningful share of the economy (currently only ~6.000 companies report under the NFRD). Therefore, ***the German presidency shall support efforts to expand the scope of the NFRD to all publicly listed companies, medium-sized and large non-listed corporates (i.e. companies with 250+ employees), and companies in high-impact sectors*****.**

3. **Leveraging the potential of the Multiannual Financial Framework (MFF) and the recovery and resilience facility for a green recovery and the green deal**: on 27 May, the European Commission proposed a budget and recovery package of legislative and non-legislative measures for the new Multiannual Financial Framework (MFF, for the period 2021 – 2027) and a Next Generation EU programme including a EUR 560bn recovery and resilience facility (RRF), which is to be adopted by the end of 2020. Against the backdrop of the COVID-19 pandemic and the need for a swift and sustainable recovery, it is crucial to firmly enshrine the green deal objectives, 2050 carbon neutrality and the 2030 climate and energy targets as guiding principles in the distribution of this EUR 1.8 trillion proposal. ***The German presidency shall support efforts to establish a rigorous framework on transparency as well as for monitoring and accountability of the MFF's and the RRF's contribution to the green deal objectives*****.** This could involve replacing the existing climate tracking approach with a more evidence based and transparent approach. The utilisation of concepts of the EU Taxonomy such as the substantial contribution and the do no significant harm should be considered, as well as the established exclusion criteria and environmental and social safeguards of international finance institutions (such as the European Investment Bank (EIB), Kreditanstalt für Wiederaufbau (KfW) or the Worldbank).

4. **Emphasize a comprehensive approach to improving corporate governance as key element of the new sustainable finance strategy:** governance structures might strongly enhance the sustainable finance environment. Existing incentive systems tend to reward short-termism and usually do not sufficiently include long-term sustainability performance. ***The German presidency shall strengthen discussions on increasing sustainability aspects in incentive systems such as executive remuneration and in fiduciary duties as part of the renewed sustainable finance strategy***. The renewed sustainable finance strategy of the European Commission is planned for Q4 2020. Educational aspects on sustainability and sustainable finance should be further strengthened and matured. Experience from front runners on sustainable finance such as Allianz shows that it is pertinent to achieving leadership in

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[1] For the effectiveness of mandatory disclosure and an overview of the corresponding scientific literature, see e.g. the Policy Brief 2/2019 of the Research Platform Sustainable Finance @ https://www.diw.de/de/diw_01.c.794205.de/publikationen/sonstige_aufsaetze/2019_0000/verpflichtende_klimabezogene_unternehmens-berichterstattung_als_mittel_zur_reduzierung_von_co2-emissionen.html

sustainable finance for senior management to have a robust understanding of sustainability and to include sustainability in the corporate strategy. Therefore, ***the German presidency may support efforts to introduce educational minimum requirements for senior management on sustainability*****.** Furthermore, skill sets of operational level management need to be developed or improved to operationalise and mainstream sustainable finance. While executive education and internal trainings are increasingly coming onto the market, a unified and a comprehensive approach is still not existing. ***The German presidency may support efforts to harmonise and complement educational programmes at the university level and in on-the-job trainings*****.** Respective measures could be established within the EU Skills Agenda.

5. **International positioning and outreach**: the EU and its member states are at the forefront of developing and implementing the sustainable finance agenda. Currently, the EU runs the risk of losing momentum for its sustainable finance strategy as important international partners are not fully taken on board in its development. In many fields of sustainable finance such as taxonomy or disclosure, international cooperation is necessary to provide financial market actors with access to information by companies from around the globe. Reporting standards and formats as well as disclosure requirements need to be harmonised globally (or at least in close co-operation with key partner countries). ***The German presidency shall support efforts to develop a roadmap for international cooperation on and the harmonisation of sustainable finance efforts*****.** A central platform to foster international cooperation would be the International Platform on Sustainable Finance (IPSF), which was established by the European Commission in October 2019 and already has 14 members including major economies such as China. To utilise this resource most effectively, ***the German presidency shall support efforts to establish a working structure within the IPSF that allows ambitious and deep cooperation on sustainable finance related challenges and provide a platform for exchange and effective peer learning*****.**

We hope that the considerations can help the German presidency in formulating its priority actions on sustainable finance. We are happy to enter into an in-depth dialogue.

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