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A new EU Sustainable Finance Strategy so support the EU Green Deal – key principles and recommendations

Dear President Von der Leyen,
Executive Vice-President Dombrovskis,
Executive Vice-President Timmermans,
Commissioner McGuiness,

The European Commission is preparing a new Sustainable Finance Strategy, seeking to lay out the major policy orientations needed for Europe to achieve the ambitions of the Green Deal, the EU Climate Law and ensure a sustainable social recovery from the COVID-19 pandemic. In this context, we are writing to you on behalf of Eurosif, the European Sustainable Investment Forum, to express our strong support for a new ambitious strategy and propose some key principles to articulate the strategy as well as concrete policy recommendations.

Through the 2018 EU Sustainable Finance Action plan the EU demonstrated truly global leadership in translating the objective of the Paris Agreement into a set of policies and regulations meant to orchestrate a re-orientation of capital flows towards sustainable investments, increasing transparency in the financial system about sustainability-linked risks and ensuring we gradually shift towards an economic system that operates within planetary boundaries will taking due account of social dimensions.

In recent months, discussions around the EU Taxonomy, the NextGenerationEU budget and the allocation of public funding to long-term sustainable investments to secure a green recovery have laid bare the inherent tensions existing between EU Member States, Members of the European Parliament, stakeholders and civil society on how to orchestrate this transition in a just way. These dialogues are essential to the political discourse in democratic societies. We should however not lose sight of the urgency of challenges around Climate Change and the severe consequences of an accelerating loss of biodiversity as well as the exacerbated social tensions in the wake of the COVID-19 pandemic. Therefore, we earnestly believe that the new EU Sustainable Finance Strategy should embed the following key principles. We need to ensure that the actions by the financial sector and investors have an impact and translates into real-world outcome that contribute to solving the problems we are facing.

Transparency is not enough – the EU Green Deal needs to convey price signals

The EU Action Plan focussed through the EU Taxonomy, Sustainable Finance Disclosure Regulation, the EU Climate Transition and Paris Aligned Benchmarks and many of the other policy actions focussed on bringing more transparency to the financial system around sustainability risks with the aim of reorienting capital flow towards sustainable companies. Transparency and disclosures are a precondition but are not sufficient to orchestrate the scale of investments needed fast enough. For example, in the EU around 50% of the investments required to reach carbon neutrality by 2050 are deemed not financially feasible for companies and investors in the current policy environment.[1] Increased transparency will not materially alter this. Therefore, sustainable finance policies focussed on transparency need to be complemented with EU sectoral policies under the EU Green Deal seeking to price negative climate, environmental and social externalities, sending very strong signals to companies and financial markets by making harmful investments more expensive and sustainable investments more competitive. For example, the review of the EU Emissions Trading System resulting in a structurally higher carbon price may be as impactful as the EU Taxonomy in reorientating capital towards sustainable investments aligned with the EU Climate Law objectives.

Coherent, Effective and Impactful sustainable finance policies

The sustainability challenges we face across Environmental, Social and Governance issues require rapid impactful policies. They are too important to focus on symbolic policies which may carry high political costs while having limited impact. Therefore, it is vital to focus on the core principles of better regulation: precisely identify market failures that need correction, identify specific policy tools that are likely to be most effective and conduct ex-post robust evaluations of whether these policies have reached their goal or need to be adjusted. For example, the EU Taxonomy on climate mitigation/adaption is much needed as it facilitates investors identifying economic activities compatible with the objective of carbon neutrality by 2050 and may help reorient capital. By contract, a significant harm Taxonomy, while bringing transparency, may not necessarily accelerate disinvestments from traditional fossil fuel sectors and is likely to be very divisive. Finally, it is necessary to achieve regulatory coherence between different legislative frameworks both in terminology, in substance and in the adequate sequencing of regulatory obligations between investee companies and financial institutions to make sure it is not unnecessarily complex.

From defining 'Green' towards the Transition Journey

The EU Sustainable Finance Action Plan focused on bringing more transparency to the financial system around a definition of sustainable investment aligned with long-term sustainability objectives, like carbon neutrality by 2050. The new EU Sustainable Finance Strategy needs to pivot towards focusing on the transition journey to meet these objectives, by defining a set of robust transition pathways and scenarios for the sectors of the economy whose transition is key to whether we will collectively reach the objective of carbon neutrality and then getting overtime companies to report against these. The policy tools to adequately capture a dynamic process like the transition of economic sectors may be different to the ones used to identify investments aligned already today with the long-term sustainability objectives.

[1] McKinsey, *How the European Union could achieve net-zero emissions at net- zero cost*" (December 2020) [Link]

Representing European ambitions in international discussions
Coherent and effective policies will ensure that Europe remains at the forefront of international policymaking to achieve our social, climate and natural conservation objectives and can shape that agenda. A cornerstone of the European approach is the principle of double materiality focusing both on financial materiality and sustainability impact to ensure ESG measurement translates into real-world outcomes. A European sustainability reporting standard underpinned by 'double materiality' will deliver the necessary level of transparency for governments, stakeholders, markets and investors to understand and start addressing and factoring risks, impacts and negative externalities. While we support as much as possible global alignment where possible, global alignment should not be an end in itself nor an impediment to the EU's ambitions to develop a sustainable finance ecosystem and reporting framework that goes beyond the international minimum common denominator.

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We have translated these key principles in a set of policy recommendations (see Annex) which we believe would ensure that the new EU Sustainable Finance Strategy is ambitious, effectively supporting the objectives of the EU Green Deal and ensures the financial sector can effectively play its part in reorienting capital flows to sustainable investments supporting the EU Agenda on social, environmental and governance challenges of our age. We stand ready to help the European Commission and the EU institutions in implementing legislation that will deliver on these goals and we remain available to discuss our specific recommendations with you and your teams.

Yours sincerely,

Victor van Hoorn
Executive Director, Eurosif

About Eurosif

Eurosif works as a partnership of Sustainable Investment Forums (SIFs) existing in different European countries whose members include institutional investors, asset managers, index providers and ESG research and analysis firms totalling over €20 trillion of assets under management, as well as other stakeholders such as NGOs, trade unions, think-tanks, and philanthropic foundations. Our mission is to promote through private and public finance sustainable investments making a measurable contribution to the sustainability objectives of the EU and the UN, through investor's capital allocation decisions, stewardship and engagement with investee companies and through policy advocacy.

Annex – our specific recommendations for the new EU Sustainable Finance Strategy

Transparency is not enough – EU Green Deal needs to send market signals

Theme	**Issue**	**Policy Recommendation**
EU Green Deal policies	It is essential that every proposal under the EU Green Deal agenda being cross-sectoral or sector specific is assessed on the clarity and strength of price signals (pricing negative externalities) it gives to companies, markets and investors as part of the Impact Assessment process.	In Impact Assessment process for EU Green Deal proposals, reflect on whether it sends adequate price signals
Revision of the EU Emissions Trading Scheme (ETS) and CBAM	In the context of the Fit-for-55 package the scope of the ETS regimes needs to be broadened to encompass more sectors and to address carbon leakage from imported goods. It needs to send strong signals about the phase-out of free allowances for sectors and should communicate 'targeted' rather than 'expected' prices for Emission Allowances Unites (EAU).	Ensure the revision of the ETS reaches broad sectoral coverage and is combined with a robust carbon border adjustment mechanism to send strong, long-term price signals to markets and investors. A clearly communicated price floor increasing between now, 2025 and 2030 could be an option.
Leverage Member States budget to stimulate blended finance	A critical part of the equation in solving sustainability challenges is using public finance in a smart way to leverage private finance for sustainable investments that may otherwise not be financed by the market. The European Commission could integrate this in its interactions with EU Member States as Member States budget represent. This would complement EU programs like InvestEU and scale up blended finance.	When DG ECFIN is reviewing draft budgetary plans of Eurozone Member States, suggest structural reforms supporting Sustainable Investments in sectors with identified investment deficits
Technical assistance to Member States	While some Member States have a greater transition challenge in the decades ahead and need to get support from the Just Transition Fund, this needs to be combined with Technical Assistance to stimulate regulatory, fiscal, and state aid policies incentivising sustainable investments.	Ensure advisory support through DG Reform to Member States stimulates public policies supporting sustainable investments

Coherent, Effective and Impactful sustainable finance policies

Theme	**Issue**	**Policy Recommendation**
EU minimum standards for ESG & Sustainable Investment Funds	The SFDR focussed only transparency of fund products. It does not set a standard for different types of products, limiting comparability and increasing the risk of market fragmentation. To remedy this and limit the risk of mis-	Commit to develop EU minimum standards for investment funds through a revision of SFDR

	selling of green products in the advice process, there is a need to develop minimum sustainability standards for investment funds. The EU Ecolabel process focussed on creating a pure green label linked to the EU Taxonomy with thresholds assuming European economy well underway to reaching the 2050 goals. This EU Ecolabel is unlikely to see scale and uptake with diversified investment funds for retail clients. But the need for a realistic Green Label and Transition Label at EU Level to identify ambitious and transition-focussed products remain.	
EU Green & Transition Labels	The EU Ecolabel process focussed on creating a pure green label linked to the EU Taxonomy with thresholds assuming European economy well underway to reaching the 2050 goals. This EU Ecolabel is unlikely to see scale and uptake with diversified investment funds for retail clients. But the need for a realistic Green Label and Transition Label at EU Level to identify ambitious and transition-focussed products remain.	Develop Commission Guidelines on an EU Green Fund label and Transition Fund label
Social Indicators	There is a need to develop more detailed and smart social indicators so that investors can understand better the risks and impacts of their investments on social aspects.	Sustainable Finance Platform focus on the development of social indicators that could inform a sustainability reporting standard or social taxonomy
Biodiversity Taxonomy	Need to develop more robust indicators on biodiversity to identify harmful activities and activities making significant contribution. A biodiversity Taxonomy could also contribute to the work of the Taskforce on Nature Related Financial Disclosure (TNFD), by setting – at least in the European context – nature and biodiversity restoration objectives. Like any part of the Taxonomy, it is vital it is science based.	Prioritise the adoption of a science-based taxonomy identifying economic activities making significant contribution to biodiversity protection and restoration
ESG Data Providers	Data providers are playing a key role in sustainable finance as they are pivotal to: 1) Climate modelling, which is vital for credible net-zero commitments 2) ESG Ratings of investee companies, which play an important role in asset allocation processes 3) Compliance with Taxonomy, SFDR and EU Paris-Aligned Benchmarks. More transparency would be required from these market participants around the quality, availability and raw/modelled data, transparency of methodologies used and conflict of interest policies.	Data providers should be placed in the regulatory perimeter and subject to transparency requirements around quality of data and methodologies.

Shift focus from defining 'Green' to the Transition journey

Theme	Issue	Policy Recommendation
Climate Scenarios & Net-Zero	It is essential for markets to understand in a transparent, robust and comparable how non-financial and financial companies align with the 2050 Climate Objectives. The EU should adopt a definition of net-zero (incl. role of offset) based on a set of uniform, robust and transparent climate scenarios built on credible sectoral transition pathways and mandating companies to report against it. This could also be considered specifically for financial institutions.	Ensure a robust definition of Net-Zero/Alignment with 1,5c in CSRD or EU Sustainability Reporting Standard or specific sectoral legislation
Engagement & Stewardship	Stewardship/engagement is a key lever for investors to orchestrate change within companies and stimulate transition. Therefore, there is need to strengthen the European regulatory framework so that investors are incentivised to exercise their voting rights and are held to account on their engagement objectives, activities and escalation plans with investee companies.	Accelerate the review of the SRDII legislation with the aim of strengthening framework for engagement, also in the context of SFDR