

IIGCC RESPONSE TO EUROPEAN COMMISSION CONSULTATION ON RENEWED SUSTAINABLE FINANCE STRATEGY

The Institutional Investors Group on Climate Change (IIGCC) is the European membership body for investor collaboration on climate change and the voice of investors taking action for a prosperous, low-carbon future. IIGCC has more than 250 members, mainly pension funds and asset managers, across 16 countries, with over €33 trillion in assets under management.

Our mission is to mobilise capital for the low-carbon transition and to ensure resilience to the impacts of a changing climate by collaborating with business, policy makers and fellow investors. IIGCC works to support and help define the public policies, investment practices and corporate behaviors that address the long-term risks and opportunities associated with climate change. Members consider it a fiduciary duty to ensure stranded asset risk or other losses from climate change are minimised and that opportunities presented by the transition to a low-carbon economy – such as renewable energy, new technologies and energy efficiency – are maximised. For more information visit www.iigcc.org and @iigccnews.

1. Section I of the consultation: General questions addressed to all stakeholders

Question 1: *With the increased ambition of the European Green Deal and the urgency with which we need to act to tackle the climate and environmental-related challenges, do you think that (please select one of the following):*

- Major additional policy actions are needed to accelerate the systematic sustainability transition of the EU financial sector.
- Incremental additional actions may be needed in targeted areas, but existing actions implemented under the Action Plan on Financing Sustainable Growth are largely sufficient.
- No further policy action is needed for the time being.

IIGCC's position is that the EU should take further action to accelerate the systematic sustainability transition of the EU financial sector.

Question 4: *Would you consider it useful if corporates and financial institutions were required to communicate if and explain how their business strategies and targets contribute to reaching the goals of the Paris Agreement?*

- Yes, corporates
- Yes, financial institutions
- Yes, both**
- If no, what other steps should be taken instead to accelerate the adoption by corporates and financial sector firms of business targets, strategies and practices that aim to align their emissions and activities with the goals of the Paris Agreement?
- Do not know.

Question 5: *One of the objectives of the European Commission's 2018 Action Plan on Financing Sustainable Growth is to encourage investors to finance sustainable activities and projects. Do you believe the EU should also take further action to: scale from 1 (strongly disagree) to 5 (strongly agree).*

- *Encourage investors to engage, including making use of their voting rights, with companies conducting environmentally harmful activities that are not in line with environmental objectives and the EU-wide trajectory for greenhouse gas emission reductions, as part of the European Climate Law, with a view to encouraging these companies to adopt more sustainable business models: scale from 1 (strongly disagree) to 5 (strongly agree). IIGCC response: 5 (strongly agree).*
- *Discourage investors from financing environmentally harmful activities that are not in line with environmental objectives and the EU-wide trajectory for greenhouse gas emission reductions, as part of the European Climate Law: scale from 1 (strongly disagree) to 5 (strongly agree). IIGCC response: 5 (strongly agree).*
- *In case you agree or strongly agree with one or both options [4-5]: what should the EU do to reach this objective? [BOX, 2000 characters] See below*

IIGCC's position is that the EU should take further action to encourage investors to engage companies to adopt more sustainable business models as well as discourage investors from financing environmental harmful activities.

EU action would have the most impact where accompanied by clarity on the net zero transition pathways per sector (as highlighted in IIGCC's response to questions 6, 7 and 9), with enhanced cross-economy measures (such as a strengthened EU ETS) and sector-specific measures (such as strengthened building codes and standards).

In general, with respect to investors, the overall preference is for guidance and clarifying existing requirements over further regulation. Any additional regulation of investors should be based on full evaluation of the impacts, and ensuring any additional efforts are proportional to their anticipated environmental benefits.

2. Section II of the consultation: Technical and strategic questions addressed to experts

Question 6: *What do you see as the three main challenges and three main opportunities for mainstreaming sustainability in the financial sector over the coming 10 years? [BOX, 2000 characters].*

IIGCC's position is to highlight the below challenges for mainstreaming sustainability in the financial sector over the coming 10 years, including:

- **lack of clarity regarding where capital needs to be deployed in individual sectors within the real economy in order to achieve net zero emissions**
- **disclosure of management of physical climate risk management including results of risk identification analysis and any mitigation actions taken**
- **inconsistency across the sustainable finance agenda and regulations; including data/information asymmetry between companies and investors, linked to a lack of standardisation of disclosures and methodologies.**

IIGCC's position is to highlight the below opportunities for mainstreaming sustainability in the financial sector over the coming 10 years, including:

- **clarity on the pre-2030 transition pathway for each sector in line with economy-wide net zero emissions, such as the timetable for phasing out fossil fuels and key technology changes (including timeline for phasing out subsidies to fossil fuel production and carbon**

- intensive sectors at the EU and member state level (e.g. State Aid))
- economic recovery policies, where sustainable, could provide additional sustainable investment opportunities
- EU global leadership on both sustainable finance (supporting global ambition and harmonisation on sustainable finance) and climate change policy (especially to encourage increased global ambition for second Nationally Determined Contributions via UNFCCC process).

Question 7: Overall, can you identify specific obstacles in current EU policies and regulations that hinder the development of sustainable finance and the integration and management of climate, environmental and social risks into financial decision-making? Please provide a maximum of three examples [BOX max. 2000 characters].

IIGCC's position is to highlight the misalignment of EU energy policies with 2030 and 2050 targets, including a need for:

- clarity on the transition pathway for each sector in line with economy-wide net zero emissions, such as the timetable for phasing out fossil fuels and key technology changes (including timeline for phasing out subsidies to fossil fuel production and carbon intensive sectors at the EU and member state level (e.g. StateAid))
- strengthened measures to increase confidence in carbon pricing (including but not limited to EU ETS)
- improved coordination and collaboration at the EU level between those developing net zero emissions policies with investors and those working on regulating sustainable finance to ensure maximum coherence between the two initiatives.

Question 9: As a corporate or a financial institution, how important is it for you that policy-makers create a predictable and well-communicated policy framework that provides a clear EU-wide trajectory on greenhouse gas emission reductions, based on the climate objectives set out in the European Green Deal, including policy signals on the appropriate pace of phasing out certain assets that are likely to be stranded in the future?

- o Please express your view by using a scale from 1 (not important at all) to 5 (very important). **IIGCC response: 5 (very important)**
- o For scores of 4 to 5, what are, in your view, the mechanisms necessary to be put in place by policy-makers to best give the right signals to you as a corporate or a financial institution? [BOX, 2000 characters] **See below**

IIGCC's position is to highlight the need for clarity on the transition pathway for each sector between now and 2050, set out in sector roadmaps (or otherwise) which:

- set out ambitious sectoral policy objectives aligned with economy-wide net zero emission by 2050, including a timetable for phasing out fossil fuels
- highlight opportunities and timeframes for investment in new technologies and infrastructure
- in aggregate set out a clear pathway to achieve net zero emissions across the economy by 2050.

These should be supported with enhanced cross-economy policy measures (such as a strengthened EU ETS) and sector-specific measures (e.g. strengthened building codes and standards).

Without this clarity and with only moderately ambitious sectoral policy objectives, there is unlikely to be the strength of market signal needed to mobilise investors and attract the levels of private finance required to fund the European Green Deal.

Question 10: *Should institutional investors and credit institutions be required to estimate and disclose which temperature scenario their portfolios are financing (e.g. 2°C, 3°C, 4°C), in comparison with the goals of the Paris Agreement, and on the basis of a common EU-wide methodology?*

- Yes, institutional investors
- Yes, credit institutions
- Yes, both
- No
- Do not know

IIGCC supports the assessment and disclosure of investment portfolios against the goals of the Paris Agreement. Specifically, IIGCC would encourage the development of EU guidance for investors and credit institutions to report on how they are aligning portfolios towards the goal of EU net zero emissions by 2050.

Our preference to focus on alignment against net zero emissions rather than a temperature scenario is because net zero emissions by 2050 is a clearer and more specific goal; greater transparency against this goal is possible compared to temperature metrics. While in theory, a temperature metric is an attractive option to express portfolio alignment, there are concerns as to whether portfolio performance can be summarised into a single temperature metric (e.g. 2°C, 3°C) in a technically robust way that avoids producing misleading results.

Our preference for EU guidance rather than an EU-wide methodology is for several reasons. Substantial methodological issues remain unresolved and further work is needed within the investment community to resolve these issues. In addition, to support clarity and ambition for investor net zero actions, the EU and its Member States need to deliver on their commitments under the Paris Agreement, including the EU publishing clear net zero trajectories for individual sectors (which investors could align with, rather than theoretical anticipated EU net zero trajectories).

Data availability and methodological challenges for assessing portfolio performance against net zero emissions by 2050 are substantial (and only exacerbated for assessments against temperature scenarios). Issues that would be helpful for any EU guidance to address would include:

- The methodology would need to take into account expected future scope 1, 2 and, where material, scope 3 emissions of assets. Ideally this would be based on forecasted production, investment plans and/or business model, rather than a simple trajectory from current emissions or based on a target which may not be credible (e.g. where a target is not supported by the business model or investment plan).
- How to assess the materiality of a company's scope 3 emissions aligned to net zero emissions.
- Lack of consistency across companies' emission reduction targets and investment plans, in order to assess alignment of these with net zero emissions (noting that these will

incorporate a range of assumptions including emission factors, anticipated carbon price, production/demand and GDP growth).

- Lack of adequate downscaled emission scenario datasets for assessing what level and timeframe for decarbonisation is required per asset to align to net zero emissions by 2050 - noting that datasets are required with granularity at a sector and regional level.
- What the appropriate or permissible contribution of offsetting should be within an asset's targets and plans, consistent with overall economy-wide net zero carbon budgets.

An additional issue for any EU guidance to address is how to account for a range of investor strategies, including those that may not result in immediate emission reductions but can still drive real economy emissions reductions over time. Activist investors may proactively take large stakes in high carbon companies or assets with the aim of delivering changes in business model through engagement (and hence reduce emissions over time).

We would encourage the European Commission to review the approach set out in IIGCC's Paris Aligned Investment Initiative Framework in developing any EU guidance for reporting on portfolio alignment.

3. Section II.1 of the consultation: Strengthening the foundations for sustainable finance

Company reporting and transparency

Question 14: *In your opinion, should the EU take action to support the development of a common, publicly accessible, free-of-cost environmental data space for companies' ESG information, including data reported under the NFRD and other relevant ESG data?*

- Yes**
- No
- Do not know.
- If yes, please explain how it should be structured and what type of ESG information should feature therein. [BOX, 2000 characters] [See below](#)

IIGCC's position (as set out in IIGCC's response to the NFRD consultation) is that a central, digital access point for companies' ESG information would be of benefit to all stakeholder groups and particularly useful for smaller investors. All stakeholder groups would benefit from a public database of tagged sustainability information. We recommend that the data space be open for voluntary reporting from non-EU companies.

Ideally, the data space would be managed by a neutral third party (e.g. a non-profit) – however, an outstanding question is which party(s) would bear the costs associated with establishing, monitoring and maintaining the database.

Digitalized sustainability information originated from companies would still have to be somehow vetted. Sustainability data is often not balanced and tagging itself might lead to a growing amount of data that is only structured on the surface, but actually does not add up (is not comparable). The application of reporting principles and standards has to be monitored / enforced by an independent authority.

Accounting standards and rules

Question 16: Do you see any further areas in existing financial accounting rules (based on the IFRS framework) which may hamper the adequate and timely recognition and consistent measurement of climate and environmental risks?

- ✓ **Yes**
- No
- do not know.
- If yes, what is in your view the most important area (please provide details, if necessary):
 - ✓ **Impairment and depreciation rules.** [BOX, 2000 characters]
 - ✓ **Provision rules.** [BOX, 2000 characters]
 - ✓ **Contingent liabilities.** [BOX, 2000 characters]
 - ✓ **Other, please specify.** [BOX, 2000 characters]

IIGCC's position is that improved enforcement of financial accounting rules is required to ensure Paris Agreement-aligned pricing is used within financial statements and inadequate climate accounting is sanctioned. In particular, it is important that EU regulators increase their scrutiny of company accounts to ensure material climate risks are properly disclosed. For example, the UK's Financial Reporting Council (FRC) recently sent out a reminder to Audit Committee Chairs and Financial Directors making it clear that financial statements must incorporate material climate risks (as part of existing financial accounting rules)¹. In February 2020, FRC set out their intention to review implementation of these requirements in coming months².

This is an issue with enforcement rather than the rules themselves, since it is noted that IFRS already requires information material to a company be included in financial statements (under IAS1). Materiality of information is determined by whether it could reasonably be expected to influence decisions made by investors. In terms of determining materiality, it should be clear that investors view climate risks as material for a wide range of companies- there are tens of trillions of assets backing the TCFD and its call for more quantitative data on climate risks facing businesses. Investors are specifically calling for companies to provide the following information in their financial statements and/or associated notes³:

- How critical accounting judgments have been tested against credible economic scenarios that are consistent with achieving net zero carbon emissions by 2050 to 2070 in line with the Paris Agreement, and any adjustments made to these assumptions⁴.
- Results of sensitivity and/or scenario analysis linked to variations in these judgements/ estimates, including one that is Paris-aligned, if this is not used as the base case.
- Implications for dividend paying capacity of Paris-alignment (e.g. adjustments to distributable reserves; threshold assumptions that would trigger cuts to dividends).
- Consistency between narrative reporting on climate risks and the accounting assumptions.

¹ [https://www.frc.org.uk/getattachment/71345784-8f60-438b-a474-fc7c79ace9e3/Year-end-letter-\(003\).pdf](https://www.frc.org.uk/getattachment/71345784-8f60-438b-a474-fc7c79ace9e3/Year-end-letter-(003).pdf)

² [https://www.frc.org.uk/news/february-2020-\(1\)/frc-assesses-company-and-auditor-responses-to-clim](https://www.frc.org.uk/news/february-2020-(1)/frc-assesses-company-and-auditor-responses-to-clim)

³ Over the past two years a growing group of institutional investors has been drawing attention to concerns that financial statements by a number of companies could be mis-representing the real economic outlook. In January 2019, investors representing around \$1 trillion in assets wrote to the UK's Big Four audit firms outlining their concerns and expectations that the auditors respond proactively. In November 2019, investors started writing to Audit Committee Chairs at exposed companies seeking information on how they are ensuring climate risks are considered in the accounting process.

⁴ Examples of which accounting judgements may require adjustment are covered under recent IASB guidance below.

- Steps taken by the Audit Committee to ensure material climate risks – including those associated with Paris-alignment – are properly considered by the external auditor, and the impact that this has had.

As part of this, financial reports should reflect and be consistent with any assumptions made over commodity or energy prices and consumer demand used in developing Paris Agreement-Aligned strategies and targets. For example, BP were previously using an oil price of \$50 per barrel to test whether capex projects are aligned with the Paris Agreement, yet disclosing a forward-looking price assumption of \$70 per barrel in their financial accounts; however, BP announced in June⁵ that they are now using a forward-looking price of \$55 per barrel and will take multi-billion dollar impairment charges as a result.

Recent guidance published by International Accounting Standards Board (IASB) Board⁶ outlines how climate risks should already be incorporated under existing accounting standards, providing a valuable framework for directors and audit firms. These cover all the categories noted in the question above, for instance:

- asset impairment, including goodwill
- changes in the useful life of assets
- changes in the fair valuation of assets
- effects on impairment calculations because of increased costs or reduced demand
- changes in provisions for onerous contracts because of increased costs or reduced demand
- changes in provisions and contingent liabilities arising from fines and penalties
- changes in expected credit losses for loans and other financial assets.

Another key mechanism to ensure accounting standards are properly enforced is via audit; with a few noteworthy exceptions, auditors are silent on climate risks. The EU needs to enforce auditor duties with respect to both accounting standards but also capital maintenance provisions in Company Law.

In January 2019, investors sent letters⁷ to the UK's largest audit firms (PWC, KPMG, Deloitte and EY). In December 2019, KPMG and Deloitte published detailed papers outlining how directors should ensure climate risks are incorporated into the accounting process, which builds on the IASB framework. In summary, the key actions auditors need to take include:

- Establish whether accounting standards have been properly followed, including necessary adjustments for material climate risks. Critical accounting estimates or judgements must reflect these factors. As noted above, for those using IFRS, the decision on materiality rests not just with directors' personal views, but must take account of whether investors have indicated that they believe the information to be material.
- Ensure consistency between the narrative disclosures around climate risks, the company's strategy and the financial statements.
- Ensure capital maintenance / solvency rules are adhered to, such as dividend legality. In the EU these rules are additional to following accounting standards, and often they demand

⁵ https://www.ft.com/content/2d84fc23-f38d-498f-9065-598f47e1ea09?accessToken=zWAAAXNN4nLokc8thPwj841j90QZVmPR-HqCQ.MEQCID572ZgZlBBXHSS-zhVM6h7NpyM06a1jO3QaV5-dVXMAiAc-ARZ8EYvbUQEn5LXLHWgEsxPra7OKAFTOy9E_bfpQg&sharetype=gift?token=41119ab5-86a4-4b0d-b8a4-5eebb81ce15d

⁶ <https://cdn.ifrs.org/-/media/feature/news/2019/november/in-brief-climate-change-nick-anderson.pdf?la=en>

⁷ <https://sarasinandpartners.com/stewardship-post/incorporate-climate-risks-into-company-accounts/>

greater prudence when dealing with foreseeable losses and liabilities⁸.

In the event that management chooses not to presume Paris-alignment in their accounting, for instance due to a belief that the Paris Agreement is unlikely to be implemented, then auditors need to consider two courses of action:

- **Opinion qualification:** the auditor must first determine whether managements' assumptions/ estimates are consistent with providing a true and fair view / fair representation of the entity's economic health. If not, then they should qualify their accounts to alert shareholders to this fact.
- **Supplementary disclosures including sensitivity analysis:** If the auditors determine the core assumptions meet local statutory requirements, and are consistent with accounting standards, then they should ensure that sensitivity /scenario analysis is produced in the Notes to the accounts indicating how Paris-aligned assumptions would impact the financial statements (as highlighted under recent IASB guidance for IAS1 above). If management and the board choose not to make these supplementary disclosures, auditors should make appropriate commentary in their report to shareholders. This is particularly important where shareholders have already made clear that they believe climate risks to be material.

Sustainability research and ratings

Question 20: How would you assess the quality and relevance of ESG **ratings** for your investment decisions, both ratings of individual Environmental, Social or Governance factors and aggregated ones?

- Individual: Please express your view by using a scale of 1 (very poor quality and relevance) to 5 (very good).
- Aggregated: Please express your view by using a scale of 1 (very poor quality and relevance) to 5 (very good).
- If necessary, please explain the reasons for your answer. [BOX, 2000 characters] [See below](#)

IIGCC's position is to call for improved transparency and, ideally, improved consistency between ESG ratings; however, we do not consider that heavy regulation of this industry is presently required. ESG ratings are one of many (not the only) data sources utilised by investors when assessing investments.

The rapid growth in the ESG ratings space has resulted in differences in methodology and metrics. Different rating agencies have different philosophies and users need to appreciate these in order to fully understand the rationale behind the ratings. As investors increase their experience of working with different agencies, their understanding of each agencies' methodology can often improve. The greater the transparency of the agencies' methodology

⁸ Where impacts are difficult to quantify or uncertain in timing – which is often the case for climate-related impacts – accounting standards may permit them to be omitted from the numbers (though a note is required to alert users under IAS 37 Provisions, Contingent Liabilities and Contingent Assets), but capital maintenance/solvency rules demand that directors account for foreseeable losses or liabilities even where the timing is unclear and magnitude hard to measure. This enables directors to discharge their duties to the company (and its creditors/shareholders) to ensure capital maintenance (solvency) to prevent distributions (e.g. dividend) out of capital (2nd EC Directive). See also Directive 2012/30/EU (particularly Article 17).

and the rationale underpinning the ratings, the easier it is for investors to understand and utilise the agencies' ratings.

Standards and labels in relation to green bonds

Question 22: The TEG has analysed four different options for an accreditation or supervision regime of verifiers of EU Green Bonds (green bonds following the EU GBS). Do you agree that verifiers of EU Green Bonds should be registered/authorised or supervised?

- Yes, at European level**
- Yes, at a national level
- No
- Do not know
- If necessary, please explain the reasons for your answer [BOX 2000 characters]

IIGCC's position is that verifiers of EU Green Bonds issued by European entities or issued by foreign entities into the European market (EUR denominated) should be registered/authorised or supervised.

Question 25: In those cases where a prospectus has to be published, do you believe that requiring the disclosure of specific information on green bonds in the prospectus, which is a single binding document, would improve the consistency and comparability of information for such instruments and help fight greenwashing?

- Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree).
IIGCC response: 4
- If necessary, please specify the reasons for your answer [BOX, 2000 characters]

Other standards and labels for sustainable financial assets and financial products

Question 29: Should the EU establish a label for investment funds (e.g. ESG funds or green funds aimed at professional investors)?

- Yes
- No
- Do not know.
- If necessary, please explain your answer [BOX, 2000 characters]
- If yes, regarding green funds aimed at professional investors, should this be in the context of the EU Ecolabel?
 - Yes
 - No**
 - Do not know
 - If necessary, please explain your answer [BOX, 2000 characters]

IIGCC's membership have diverse views regarding whether the EU should establish a label for investment funds (e.g. ESG funds or green funds aimed at professional investors) or not.

In case the EU was to go forward with developing a label aimed at professional investors at a later stage, then this would require a specific approach tailored to the needs of professional investors (and not just increasing the coverage of Ecolabel or other approaches focussed on retail investors). Institutional investors generally invest on a longer term basis compared to

retail investors and are often seeking more nuanced information than yes/no compliance with a particular standard (i.e. EU Ecolabel wouldn't meet the requirements of institutional investors). Any label aimed at institutional investors would likely involve graduated assessments of performance in relation to transition towards net zero and EU taxonomy-aligned activities.

Question 30: *The market has recently seen the development of sustainability-linked bonds and loans, whose interest rates or returns are dependent on the company meeting pre-determined sustainability targets. This approach is different from regular green bonds, which have a green use-of-proceeds approach. Should the EU develop standards for these types of sustainability-linked bonds or loans?*

- Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree).
- If necessary, please explain. [BOX, 2000 characters]

IIGCC's position is that the EU should establish guidelines for sustainability linked bonds and loans. We strongly recommend these guidelines build on existing initiatives such as the Sustainability-Linked Bond Principles⁹ and Sustainability-Linked Loan Principles¹⁰.

At present, there is potential for companies to self-determine their outcomes or targets, without a clear reference point for assessing an ambitious vs 'business as usual' outcome. As the market for these instruments grows, transparency and clarity regarding the setting, monitoring and reporting of outcomes will be essential to ensure the integrity of the market. There are challenges for investors to undertake in-depth assessment of the outcomes, both from a transparency perspective (given companies have much greater knowledge of their business models) as well as capacity perspective (for example, to assess dozens of issues as the market grows). By comparison, the approach for traditional green bonds (with ringfencing of proceeds against a green taxonomy) is easier in terms of assessment, as well as management and monitoring of budgeting and proceeds.

In addition, EU guidelines could support the growth of this market by providing an additional incentive for investors to ensure issuers are upholding sustainability principles, and to help ensure the credibility of sustainability-linked bonds or loans.

Question 31: *Should such a potential standard for target-setting sustainability-linked bonds or loans make use of the EU Taxonomy as one of the key performance indicators?*

- Please express your view by using a scale of 1 (strongly disagree) to 5 (strongly agree). **IIGCC response: 4 (strongly agree)**
- If necessary, please explain. [BOX, 2000 characters]

Question 32: *Several initiatives are currently ongoing in relation to energy-efficient mortgages¹¹ and green loans more broadly. Should the EU develop standards or labels for these types of products?*

⁹ <https://www.icmagroup.org/assets/documents/Regulatory/Green-Bonds/June-2020/Sustainability-Linked-Bond-PrinciplesJune-2020-100620.pdf>

¹⁰ <https://www.aplma.com/en/gsl>

¹¹ See for instance the work of the EFIG (Energy Efficiency Financial Institutions Group set by the EC and the United Nations Environment Program Finance Initiative or UNEP FI) on the financial performance of energy efficiency loans or the [energy efficient mortgages initiatives](#).

- ✓ **Yes**
- No
- Do not know.
- If yes, please select all that apply:
 - a broad standard or label for sustainable mortgages and loans (including social and environmental considerations);
 - ✓ **a standard or label for green (environmental and climate) mortgages and loans;**
 - a narrow standard or label only for energy-efficient mortgages and loans for the renovation of a residential immovable property;
 - other: please specify what type of standard or label on sustainability in the loan market you would like to see [BOX, 2000 characters]

Corporate governance, long-termism and investor engagement

Question 40: In your view, should there be a mandatory share of variable remuneration linked to non-financial performance for corporates and financial institutions?

- Yes
- ✓ **No**
- Do not know.
- If yes, please indicate what share. [box 2000 characters] [See below](#)

IIGCC's does not agree with a mandatory share of variable remuneration being linked to non-financial performance for corporates and financial institutions. IIGCC agrees that remuneration should be linked to non-financial performance (and that non-financial performance should include alignment with net zero emissions by 2050); however, it is a matter for individual companies to determine the appropriate share, based on their specific business needs and long-term strategy.

Companies should provide transparency and justification regarding what share they determine appropriate, as well as indicators and goals associated with the same. Clear and well-defined goals and oversight arrangements are required, to ensure robust and sufficiently ambitious incentives.

Question 41: Do you think that a defined set of EU companies should be required to include carbon emission reductions, where applicable, in their lists of ESG factors affecting directors' variable remuneration?

- Yes
- No
- Do not know.

IIGCC's position is that a defined set of EU companies should be required to include carbon emission reductions in their lists of ESG factors affecting directors' remuneration. We suggest not only carbon emission reductions would be included, but more specifically alignment with net zero emissions by 2050, with guidance (rather than regulation) provided regarding the underlying metrics and timeframe for achieving these in each sector to align to net zero emissions.

The defined set of EU companies should be restricted to those operating in material sectors. To inform the consideration of material sectors, the work of IIGCC's Paris Aligned Investment

Initiative may be helpful. The initiative is currently considering materiality in assessing portfolios' alignment to the Paris Agreement. IIGCC's Paris Aligned Investment Initiative's current recommendation (under review) is to use the EU taxonomy on sustainable finance as the basis for materiality.

Question 42: *Beyond the Shareholder Rights Directive II, do you think that EU action would be necessary to further enhance long-term engagement between investors and their investee companies?*

- Yes
- No
- Do not know.
- If yes, what action should be taken? Please explain or provide appropriate examples. [BOX max. 2000 characters] Access to Directors is good in Europe and could be strengthened, accountability over directors and meet with independent director.*

IIGCC's position is that some further EU action is needed beyond the Shareholder Rights Directive II, but with a focus on creating mechanisms that allow minority shareholders to engage and influence companies. This would include granting minority shareholders the ability to have a say on remuneration, board nomination and other important matters.

For example, the UK Corporate Governance Code includes the need for companies to explain, as part of publishing meeting results, how they intend to engage with shareholders when a significant percentage of shareholders vote against a resolution. The UK Corporate Governance Code defines 'significant' as 20% or more. The purpose is to encourage companies to describe the process they will take to assess the concerns of shareholders as well as respond to those concerns (noting that reporting on these may occur at different times).

The majority of companies in Europe have an ownership structure that involves one majority shareholder and a smaller percentage of minority shareholders. This is particularly true for mid and small caps. In practice, this means that minority shareholders (investors) have limited abilities to file a resolution or to vote against management when they disagree on the company's direction on environmental, social or corporate governance issues.

Question 43: *Do you think voting frameworks across the EU should be further harmonised at EU level to facilitate shareholder engagement and votes on ESG issues?*

- Yes
- No
- Do not know

IIGCC supports further harmonisation of voting frameworks across Member States. For activist investors proactively engaging with corporates in multiple Member States, different voting frameworks for different corporates adds a layer of complexity when seeking to file shareholder resolutions. If voting frameworks were harmonised, investors would be enabled to more efficiently and engage with corporates within their portfolios in relation to ESG issues.

Question 44: *Do you think that EU action is necessary to allow investors to vote on a company's environmental and social strategies or performance?*

- Yes**
- No
- Do not know.
- If yes, please explain. [BOX max. 2000 characters] [See below](#)

IIGCC's position is that it should be made compulsory for shareholders to approve environmental strategies at AGMs.

Question 45: Do you think that passive index investing, if it does not take into account ESG factors, could have an impact on the interests of long-term shareholders?

- Yes
- No**
- Do not know
- If no, please explain the reasons for your answer if necessary. [BOX max. 2000 characters]
- If yes, in your view, what do you think this impact is, do you think that the EU should address it and how? [box max. 2000 characters]

IIGCC's proposed position is that index investing can take into account relevant ESG factors in a variety of ways, e.g. investing in an index with a specific ESG strategy or engaging with companies on ESG issues. Governance and stewardship are important tools used by institutional investors to ensure that the expectations of clients investing in index strategies are met, which allows consideration of the most material ESG factors (e.g. transition risk for carbon intensive investments) that may impact the interests of long-term shareholders.

Question 46: Due regard for a range of 'stakeholder interests', such as the interests of employees, customers, etc., has long been a social expectation vis-a-vis companies. In recent years, the number of such interests have expanded to include issues such as human rights violations, environmental pollution and climate change. Do you think companies and their directors should take account of these interests in corporate decisions alongside financial interests of shareholders, beyond what is currently required by EU law?

- Yes, a more holistic approach should favour the maximisation of social, environmental, as well as economic/financial performance.**
- Yes, as these issues are relevant to the financial performance of the company in the long term.
- No, companies and their directors should not take account of these sorts of interests.
- I do not know.

IIGCC's position is that companies and their directors should take a more holistic approach to corporate decisions that favour the maximisation of social and environmental interests alongside and as part of the financial interests of shareholders. Institutional investors take a long-term view of value and returns; climate change presents short and long term risks to both and should be fully taken into account within corporate decisions. As part of this, as elaborated for question 16, financial statements should use Paris-Agreement aligned pricing, since investors view climate risks as material for a wide range of companies.

Question 47: Do you think that an EU framework for supply chain due diligence related to human rights and environmental issues should be developed to ensure a harmonised level-

playing field, given the uneven development of national due diligence initiatives?

- Yes**
- No
- Do not know.

Question 48: Do you think that such a supply chain due diligence requirement should apply to all companies, including small and medium sized companies?

- Yes**
- No
- Do not know.
- If yes, please select your preferred option:
 - All companies, including SMEs.
 - All companies, but with lighter minimum requirements for SMEs.
 - Only large companies in general, and SMEs in the most risky economic sectors sustainability-wise.**
 - Only large companies.
- If necessary, please explain the reasons for your answer. [box max. 2000 characters]

4. Section II.2 of the consultation: Increasing opportunities for citizens, financial institutions and corporates to enhance sustainability

Mobilising retail investors and citizens

Question 49: In order to ensure that retail investors are asked about their sustainability preferences in a simple, adequate and sufficiently granular way, would detailed guidance for financial advisers be useful when they ask questions to retail investors seeking financial advice?

- Yes**
- No
- Do not know.
- If necessary, please provide an explanation of your answer. [box max. 2000 characters]

Question 50: Do you think that retail investors should be systematically offered sustainable investment products as one of the default options, when the provider has them available, at a comparable cost and if those products meet the suitability test?

- Yes**
- No
- Do not know.

IIGCC's position is that retail investors should be systematically offered sustainable investment products as one of the default options, where the retail investor makes no active choice to invest (for example, in the context of auto-enrolment in pension products). Where retail investors make no active choice to invest and are defaulted into a product without any advice requirement, providing sustainable investment products as a default would support the overall objective of making sustainable investment products the norm.

Digital sustainable finance

Question 57: Do you think EU policy action is needed to maximise the potential of digital tools

for integrating sustainability into the financial sector?

- ✓ **Yes**
- No
- Do not know
- If yes, what kind of action should the EU take and are there any existing initiatives that you would like the European Commission to consider? Please list a maximum of three actions and a maximum of three existing initiatives. [BOX max. 2000 characters] [See below](#)

IIGCC's position is to support EU policy action to maximise the potential for digital tools for integrating sustainability into the financial sector, with some examples below:

- use of digital tools with the creation of an EU database for companies' ESG information (as mentioned in IIGCC's response to question 14)
- harmonised approaches for voting and AGMs.

Incentives to scale up sustainable investments

Question 66: In your view, does the EU financial system face market barriers and inefficiencies that prevent the uptake of sustainable investments?

- Please express your view on the current market functioning by using a scale of 1 (not well functioning at all) to 5 (functioning very well). **IIGCC response: 2**
- Please specify your answer. [BOX max. 2000 characters] [See below](#)

IIGCC's position is to highlight the need for the below:

- guidance is lacking regarding the net zero transition pathway per sector in line with economy-wide net zero emissions by 2050, noting that EU sector-specific scenario data is limited in public domain – as highlighted for questions 6, 7 and 9, this clarity is a key issue for investors seeking to align their portfolios with an economy-wide transition to net zero emissions
- increased R&D, subsidy and related support is required to support scaling up of newer, EU-taxonomy aligned technologies
- project pipelines for EU taxonomy aligned activities are not always at the right scale for institutional investors.

Promoting sustainable finance globally

Question 77: What can the Commission do to facilitate global coordination of the private sector (financial and non-financial) in order to deliver on the goals of the Paris Agreement and/or SDGs? Please list a maximum of three proposals. [BOX max. 2000 characters] [See below](#)

IIGCC's position to be supportive of the Commission engaging in global coordination of the private sector towards delivering on the goals of the Paris Agreement and SDGs. In particular, it is recommended that the Commission:

- Continue to provide policy leadership on sustainable finance, including developing EU guidance that supports international harmonisation and could be adopted internationally
- Encourage improved policy/investor dialogues, sharing lessons learned during the development and implementation of the 2018 Action Plan on Financing Sustainable Growth including engagement via the Technical expert group on sustainable finance (TEG)

- Proactively support the development of SDG-aligned financing in an emerging market context. This could help address sovereign debt problems (particularly following COVID-19), whilst supporting SDG delivery and addressing investor demand for assets that incorporate ESG factors. These innovations could include SDG-aligned bond funds, partially guaranteed SDG bonds and debt for sustainability swaps. These could be deployed with a strong SDG disclosure framework to measure the impact of different measures. For further information, please see a recent LSE article¹². Note that IIGCC's Paris Aligned Investment Initiative (PAII) encourages investors to increase allocation to SDG climate linked bonds as part of the overall portfolio objective of increasing allocation to green solutions.

5. Section II.3 of the consultation: Reducing and managing climate and environmental risks

Identifying exposures to harmful activities and assets and disincentivising environmentally harmful investments

Question 82: *In particular, do you think that existing actions need to be complemented by the development of a taxonomy for economic activities that are most exposed to the transition due to their current negative environmental impacts (the so-called “brown taxonomy”) at EU level, in line with the review clause of the political agreement on the Taxonomy Regulation?*

- Yes
- No
- Do not know.
- If no, please explain why you disagree [BOX max. 2000 characters]
- If yes, what would be the purpose of such a brown taxonomy? (select all that apply)
 - Help supervisors to identify and manage climate and environmental risks.
 - Create new prudential tools, such as for exposures to carbon-intensive industries.
 - Make it easier for investors and financial institutions to voluntarily lower their exposure to these activities.
 - Identify and stop environmentally harmful subsidies.
 - Other, please specify. [box max. 2000 characters]

IIGCC members have diverse views on this topic. IIGCC will be convening investors over the coming months to develop a position on the brown taxonomy.

Question 83: *Beyond a sustainable and a brown taxonomy, do you see the need for a taxonomy which would cover all other economic activities that lie in between the two ends of the spectrum, and which may have a more limited negative or positive impact, in line with the review clause of the political agreement on the Taxonomy Regulation?*

- Yes
- No
- Do not know.
- If yes, what should be the purpose of such a taxonomy? Please specify. [BOX max. 2000 characters]

¹² www.lse.ac.uk/GranthamInstitute/news/how-could-sustainable-finance-help-avoid-an-emerging-market-sovereign-debt-crunch/

IIGCC members have diverse views on this topic. IIGCC will be convening investors over the coming months to develop a position on a taxonomy that would cover activities in between a sustainable and brown taxonomy.

Banking prudential framework

Question 89: *Beyond prudential regulation, do you consider that the EU should take further action to mobilise banks to finance the transition and manage climate-related and environmental risks?*

- Yes one or both, please specify which action would be relevant [BOX max. 2000 characters]**
- No.
- Do not know.

IIGCC's position is that further EU action in the form of guidance would be beneficial in relation to climate stress testing (aligned with the approach being undertaken by Bank of England) and robust implementation of the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD).

Question 90: *Beyond the possible general measures referred to in section 1.6 [questions 38-48, under 'corporate governance, long-termism and investor engagement'], would more specific actions related to banks' governance foster the integration, the measurement and mitigation of sustainability risks and impacts into banks' activities?*

- Yes**
- No
- Do not know.
- If yes, please specify which measures would be relevant. [BOX max. 2000 characters]

Asset managers

Question 91: *Do you see merits in adapting rules on fiduciary duties, best interests of investors/the prudent person rule, risk management and internal structures and processes in sectorial rules to directly require them to consider and integrate adverse impacts of investment decisions on sustainability (negative externalities)?*

- Yes
- No
- Do not know.
- If yes, what solution would you propose? [BOX max. 2000 characters]

IIGCC position is to support having EU guidance on how the above-mentioned rules require asset owners and managers to consider and integrate the adverse impacts of investment decisions on sustainability. It may not be clear to asset owners, for example, the extent to which the Prudent Person Principle allows consideration of the broader well-being and interests of beneficiaries, as well as their financial interests. It is noted that asset managers' contractual instructions may not always provide clear and explicit directions in regard to sustainability.

However, in general, the preference here is for guidance and clarifying existing requirements, and monitoring the extent to which these measures have the desired impact, rather than further regulation that risks imposing requirements in the context of fiduciary duty in the immediate term. Any additional regulation of investors should be based on full evaluation of the impacts, and ensuring any additional efforts are proportional to their anticipated environmental benefits, to ensure focus on the most significant and material issues (and avoid a tick-box approach to ESG).

IIGCC acknowledges that the market's failure to adequately price the risks of adverse impacts (from climate impacts to biodiversity to human and social impacts) means the duty of financial market participants to their customers and beneficiaries needs to be addressed. The duty to seek financial returns should seek sustainable financial returns (i.e. not premised on short-term financial returns which deplete environmental and human resources) - recognising that all investments have impacts; negative impacts should be minimised and the worst impacts avoided.

Pension providers

Question 92: *Should the EU explore options to improve ESG integration and reporting beyond what is currently required by the regulatory framework for pension providers?*

- Yes**
- No
- Do not know
- If yes, please specify what actions would be relevant in your view. [BOX max. 2000 characters]

IIGCC would welcome the EU exploring options to improve ESG integration and reporting beyond what is current required by the regulatory framework for pension providers.

Member States currently can allow occupational pension providers to take into account ESG considerations when they invest (though not a requirement). Guidance would be beneficial so that pension funds improve their integration of and reporting on ESG factors, and in a more consistent way across Member States.

Question 93: *More generally, how can pension providers contribute to the achievement of the EU's climate and environmental goals in a more proactive way, also in the interest of their own sustained long-term performance? How can the EU facilitate the participation of pension providers to such transition? [BOX max. 2000 characters]*

IIGCC's position is for pension providers to make net zero emission commitments in line with initiatives such as IIGCC's [Paris Aligned Investment Initiative](#), which provides a methodology and approach for asset owners and asset managers to assess and align their portfolios with net zero.

Credit rating agencies

Question 95: *How would you assess the transparency of the integration of ESG factors into credit ratings by CRAs?*

- Please express your view by using a scale of 1 (not transparent at all) to 5 (very transparent)
IIGCC response: 2
- If necessary, please explain the reasons for your answer [BOX max 2000 characters] **See below**

IIGCC's position is to support greater transparency regarding the integration of ESG factors into credit ratings. For example, we would support the preparation of EU guidelines to provide direction and transparency for integrating ESG factors into credit ratings.

Climate-related loss and physical risk data

Question 99: In your opinion, should the European Commission take action to enhance the availability, usability and comparability of climate-related loss and physical risk data across the EU?

- ✓ **Yes**
- No
- Do not know.
- If yes, please select all that apply:
 - ✓ **Loss data, please explain why [BOX max. 2000 characters]**
 - ✓ **Physical risk data, please explain why [BOX max. 2000 characters]**

IIGCC's position is that the European Commission should take action to enhance the availability, usability and comparability of climate-related loss and physical risk data across the EU. In particular, one practical suggestion regarding physical risk would be for companies to be required to disclose the physical location (ideally longitude and latitude) of their principal operating assets, to support more robust assessments of companies' exposure to climate impacts.

Question 101: Specifically with regards to the insurability of climate-related risks, do you see a role for the EU in this area?

- ✓ **Yes**
- No
- Do not know.
- If yes, which actions you would consider to be useful? In particular, is there scope for EU action to improve the offer of products and services for climate-related disaster risk reduction, enhance insurers' potential to promote increased resilience of their policyholders beyond a mere compensatory role?¹³
 - Yes/No/Do not know.
 - If yes, please explain which actions and the expected impact (high, medium, low). [BOX max. 2000 characters]
 - If no, please explain. [BOX max. 2000 characters]

IIGCC position is to highlight concerns about an insurability crisis for assets exposed to acute

¹³ For instance, EIOPA in its [opinion on sustainability on Solvency II](#) talks about "impact underwriting which includes the development of new insurance products, adjustments in the design and pricing of the products and the engagement with public authorities without disregard for actuarial risk-based principles of risk selection and pricing".

and long term physical climate risk.

Question 102: *In your view, should investors and / or credit institutions, when they provide financing, be required to carry out an assessment of the potential long-term environmental and climate risks on the project, economic activity, or other assets?*

- Yes**
- No*
- Do not know.*
- If yes, what action should the EU take? Please list a maximum of three actions. [BOX max. 2000 characters] [See below](#)*

IIGCC's position is to be strongly supportive of the implementation of the TCFD recommendations, and considers the identification, assessment and management of climate risks to be an important part of an investor's fiduciary duty.